

## Dollars &amp; Sense

## The Investment Company Price War

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Vanguard has been the low-cost leader in the investment industry. Recently, though, its major competitors, Fidelity and Charles Schwab, have been lowering the cost of their index mutual funds and exchanged traded funds. In some cases, Vanguard is no longer the low-cost leader.

For example, Vanguard's S&P 500 Index Fund (Vanguard 500 Index Fund Admiral Shares) has an expense ratio of 0.04%. Remember that the expense ratio according to Investopedia is "a measure of what it costs an investment company to operate a mutual fund." When I went to Charles Schwab's website (Schwab.com), their site said, "Think Vanguard has the lowest costs? Think again."

They tout, "Schwab market cap index funds and ETFs are up to 80% less than comparable funds at Vanguard and 70% less than Fidelity. Everyone pays the same — whether you have \$5 or \$5 million to invest, you get the same low cost for Schwab market cap index funds." Here is a comparison chart on the S&P 500 index funds:

As you can see, the Schwab fund is cheaper. In addition, in order to get into Vanguard's Admiral share class and get the lowest cost, you need to invest \$10,000. At Schwab, everyone gets the lowest cost shares. You'll notice as well that Fidelity's funds are all cheaper than Vanguard's.

Why are they doing this? Does this mean that Schwab and Fidelity are the new sheriff in town and Vanguard, where I do all my investing outside of the military retirement plan, should be put out to pasture?

The same thing has happened in the past with brokerage commissions. While it used to cost \$50-100 to execute a brokerage trade over the phone, now they are less than \$10 and often free. This is the evolution that occurs in a free, competitive market.

Part of the reason for this price war among Vanguard, Fidelity, and Schwab is that investors are moving billions of dollars from actively-managed funds, where managers are trying to beat the market, to index funds that passively track the market. And Vanguard has been all about index funds since its inception and is practically synonymous with the term "index fund." Schwab and Fidelity are doing everything they can to

get investors in the door, even potentially operating these funds at very low profit margins or even at a loss.

Should everyone switch to Schwab or Fidelity? I'd argue no for two reasons.

First, the difference between a 0.03% expense ratio at Schwab and a 0.04% expense ratio at Vanguard on a \$1 million portfolio is only \$100. On \$100,000 it is only \$10. In other words, we are talking about small amounts of money relative to the overall size of the portfolio.

Second, while Schwab and Fidelity are lowering expenses on their most popular index funds, Vanguard has a unique structure. It is owned by its shareholders. This makes it equivalent to a non-profit investment company, and ensures it will have low costs across the board no matter what product you are looking to invest in. For example, the Vanguard Target Retirement 2030 fund has an expense ratio of 0.15%. The equivalent at Fidelity, the Fidelity Freedom 2030 fund, has an expense ratio of 0.7%, which is more than four times more expensive. How about Schwab? Schwab's Target 2030 Index Fund has an expense ratio of 0.08%, lower than Vanguard's.

What's the bottom line? This price war among Schwab, Fidelity, and Vanguard benefits the investor as costs come down. All three are large, well-established companies managing trillions of dollars, and you can likely do well investing with any of them if you know what you are doing.

Will I switch from Vanguard? No, because I know that no matter what investment I pick the cost may not be the lowest, but it'll be among the lowest in the industry.

### Reference

1. [https://www.schwab.com/public/schwab/investing/accounts\\_products/schwab\\_index\\_funds\\_etfs](https://www.schwab.com/public/schwab/investing/accounts_products/schwab_index_funds_etfs)

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S&P 500® Index	Schwab® S&P 500 Index Fund	Vanguard 500 Index Fund	Fidelity 500 Index Fund
\$3K Investment	SWPPX 0.03%	VFINX 0.14%	FUSEX 0.09%
\$10K Investment		VFIAX 0.04%	FUSVX 0.035%
\$5M Investment		N/A	FXSIX 0.03%

Figure 1. A comparison of the cost of the S&P 500 index funds at Charles Schwab, Vanguard, and Fidelity.<sup>1</sup>