



Vanguard[®]

Memo

To: Investment Managers
From: Gus Sauter, Chief Investment Officer
Date: January 3, 2012
Re: New Line of "Black Swan" Funds

The last five years have been some of the most volatile the financial markets have ever seen. Since 2008, we've faced a meltdown in global capital markets, "flash-crashes" in the US stock market, revolutions in Europe, and an unending stream of catastrophic natural disasters. Increasingly, it seems our customer's portfolios are at the mercy of high impact, low probability events.

Author and hedge fund manager Nassim Taleb labeled these types of wide scale, unpredictable events as Black Swans. We can never be sure when a Black Swan will appear, or what form it will take, but we do know there is always a Black Swan lurking somewhere.

Some banks and investment management firms, including Citi and Pimco, have started selling "tail-funds" that are advertised to do well against the backdrop of a bad economy. Although I still believe the best way to hedge against any global calamity is through broad diversification, I think investors in Vanguard funds may be interested in specific protection for their portfolios.

Therefore, I am proposing the creation of a new line of "Black Swan" mutual funds. I need each investment management team to create a diversified mutual fund that will provide portfolio growth and/or protection during a Black Swan event. Your team will predict the Black Swan event, and choose the assets that will protect investors should the event happen.

Your fund should meet or exceed the high performance standards that Vanguard customers have come to expect, and its expenses must be in-line with other actively managed Vanguard funds.

You will have the opportunity to sell your fund to a group of investment advisors at the beginning of the subscription period in February.

I am excited about this chance to serve our customers and believe these Black Swan funds will complement our already-strong array of income, growth, and aggressive growth mutual funds, index funds, and ETFs.

The timetable for the creation of your team's fund is as follows:

- January 13: Teams will present background research on historical Black Swans during inner-office meeting
- January 17: Our marketing department will unveil the "Black Swan Funds" television ad campaign
- January 27: SEC Form N-1A (Mutual Fund Prospectus) due at 5:00 pm
- February 3: Sales presentation to investment advisors

Best Regards,

Gus Sauter

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About Vanguard

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