

The Buffet Bet - Basket of Funds vs. All Passive

Stats 107 Project Proposal

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Abstract

Ten years ago, Warren Buffett made a famous bet: the ultimate passive investment, the Vanguard S&P 500 Index Fund Admiral (VFIAX), vs. a basket of funds determined by a team of hedge fund experts. Whoever had a lower return after ten years would donate \$1 million to the charity of choice of the winner. After eight years, it looks increasingly likely that Buffett will win the bet.

Type: Simulating a trading strategy.

Can a basket of funds beat the market in long term?

Our project aims to create a Mutual Fund selector for semi-passive investor. A typical Vanguard customer may have to choose from over one hundred mutual funds without any guidance. We will create a portfolio to maximize returns over the long term using several common, non-esoteric investment strategies, such as maximizing the Sharpe Ratio. In order to make this more realistic, we will take into account fees and transaction costs. Since this is aimed at a typical Vanguard retail customer, no shorting will be allowed.

We will simulate whether rebalancing on a bi-monthly, monthly, quarterly, semi-annual or annual basis is the best strategy.

We will not account for taxes on the assumption that the funds are in a tax deferred account such as 401(k) or IRA. For this reason, we will not evaluate ETFs which are at a disadvantage in a tax deferred account.

The portfolio will start with \$100,000, which is current average 401(k) balance ([source](#)).

The overall time period will be evaluated on a twenty year history, or the maximum history of the security, whichever is shorter. The starting point for the basket of funds will be a common default used by many organizations: a Vanguard Target Retirement Fund, such as VTHR, the 2030 Retirement Fund. The baseline or benchmark will be investing the same amount in VFIAX and leaving it there for the duration.

References and Data Sources

- List of Vanguard funds, including fees and transaction costs, supplied by Vanguard <https://investor.vanguard.com/mutual-funds/list#/mutual-funds/asset-class/month-end-returns>
- The Buffett Bet <http://fortune.com/2016/05/11/warren-buffett-hedge-fund-bet/>