1940

Problems of the investor--1929--1938

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THESIS

*Problems of the Investor--1929--1933*

by

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(B. S. University of New Hampshire 1926)

submitted in partial fulfillment of the requirements for the degree of

MASTER OF BUSINESS ADMINISTRATION

1940
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INTRODUCTION

This thesis has been written with one thought in mind—how can the better understanding of American Industries and their related problems lead an investor to the intelligent use of the security markets?

Separate books have been written on each division of the index by many; yet, in spite of the limited treatment of several herein, a background is constructed for continued study of correspondingly increasing value because of the interrelationships developed.

The selection of any particular decade in the history of a nation does not alter human reactions to similar conditions of varied intensity found in other periods; but intensifies the importance of a genuine understanding of the fundamental principles of investment which pervades this study.
RUDIMENTS OF INVESTMENT

Types of Investors: Since the overall aim of this thesis is to bring American industry into closer focus for the average wage earner, the first two sections emphasize its requirements and prospects for business blood transfusion.

As in medicine, specific types are imperative for particular patients. Not everyone is similarly adapted to proximity to danger; yet each contributes much. "After twelve years' experience, we know that there are some temperaments that are wholly unsuited to investment."

Ambition, industry, and thrift result in savings on an installment plan toward financial independence and a greater degree of security. By the attempted method employed, investors subdivide themselves and their returns.

Within the span between the small, regular saver who puts compound interest to work for him through a savings bank account and the gambler whose secret is luck, moves the more aggressive individuals, professional traders, and institutional buyers.

The freedom with which a fund may be applied may severely restrict its use, as in the case of banks, trust funds, and insurance companies. Safety of principal, assured income, and liquidity are essentials. Because these are

1. The Tillman Survey--publicity
associated with "long-term" obligations, the consolidated action of this group casts its broad shadow over other investment fields. This group is "not vitally interested in price fluctuations, but are content ordinarily to hold bond investments to maturity for interest returns--as long as the basic security or issue is unimpaired." 1

An individual, restricted not by law but experience, may be termed a "long-term" investor. He is one "who holds on to his investments through thick and through thin. An article in the Saturday Evening Post for April 3, 1937, 'Gilt-Edged Insecurity', told of the high percentage of bankruptcies that took place in companies that, a decade before, were the leaders of industry. The long-term holder tends to keep stocks of companies that are undergoing long-term deterioration. The long term investor rides up the hill and then rides down again, so that he has no appreciation in his capital--and he may have several years without dividends. He feels that his stocks will recover in the next bull market, but many of them never do. For example, look at the man who held utilities from 1929--1932--they never did recover to any extent comparable to the collapse. Long-term deterioration is a definite hazard." 2

In direct contrast to this type of investor is the short-term trader. "The short-term trader jumps in and out of the

2. Wood, Gaylord--"The Dow Theory Barometer"--Introduction to Weekly Letters
market every few days or weeks. The odds against success are exceedingly great. Taxes and commission consume his capital, not to mention the unpredictable and unexpected movements that eventually overtake him."

"In between the long-term investor and the short-term trader is the intermediate-term investor. In the first place, the investor avoids that most agonizing of all experiences, riding thru a bear market. The long-term investor, holding for the long pull, rides through several secondary reactions, and each time his stocks recover and go on up to new highs. Finally, the bull market reaches its peak. The first decline in a bear market is often mistaken for a secondary reaction in a bull market. The long-term trader, being used to riding out such storms, calmly sits back--and is caught not in a storm but in a hurricane. Retreating every so often, as the intermediate-term trader does, is excellent practice, because it prevents him from going over the Niagara Falls of a bear market. Secondly, it is often possible to hold stocks during an intermediate swing upwards. Selling them at or near the culmination of the movement, and then replacing them later on at lower prices; thus if a bull market consists of an upward movement from low to high of 100 points, by selling occasionally and repurchasing at lower levels. Not always will stocks be replaced at lower levels; if they are repurchased at levels higher than those at which sold, the difference will merely be the insurance premium paid for the peace of mind (and pocketbook) in not having to ride out a disturbing secondary reaction

1. Ibid
that might be the first downswing in a bear market. Thirdly, stocks are not held so long that long-time deterioration is a factor; the shelves are swept clean every so often, so to speak, and a fresh supply installed."1

"Control of America's 1,000 leading corporations is held by a large middle group constituting only 20% of the total shareholders, but holding 59% to 70% of the common stock. These 'middle class' holders lie in between the two extremes. They hold 100 shares or more in every business in which they are interested, but do not own as much as 10% of the total stock or participate as officers or directors in the management of the companies."2

"In spite of the two devastating bear markets within the past ten years, common stocks have not lost their popularity as investment media. Back in 1929 even the bootblacks had a stake in the stock market. Marginal traders may now be fewer in number, but there is no doubt that today stock ownership is more widely distributed than ever before.

These are among the results revealed by a comprehensive survey of stockholders, which included almost every corporation on the New York Stock Exchange and all the important companies either listed or actively traded on the New York Curb Exchange.

Most of this widespread distribution of common stock has occurred since 1900. Of course the mergers and consolidations which have resulted in our huge industrial corporations were

1. Ibid
2. "Middle Class" Investors in the Saddle--Barron's 7/25/38-13
Consequently, the knowledge of paramount importance is the fundamental character of the stock market, bull or bear. To invest money simply because cash is available is the worst mistake that can be made. Just a moderate shrinkage in principal resulting from investing at an inopportune time can wipe out the dividends of several years. Therefore, the most important phase of speculation is an understanding of the main trend. "Nothing stands still, least of all the stock market."  

Once the investor finds himself in this moving picture, he quickly senses the relative unimportance which any mob plays and the growing importance placed on the leads. If he is to travel with them, he must know their parts. Likewise, the investor must study to find what the 'big money' is doing. "This is clearly reflected by the indexes of the Dow Theory."  

The mobs in the movies support, but never replace the stars. Although momentary importance is given the mob scenes, the sustaining interest is on the leads. The fan is quite unaware of the mob leaving; likewise in the stock market, if he is a part of the mob, he is unconscious of his own exit via perilous passageway. "The Dow Theory Separates You From The Crowd."  

1. Ibid  
2. Wood, Gaylord--Weekly Letter--"The Dow Theory Barometer"  
3. Ibid
Before one can appreciate the bondholder of this decade, he must recognize any bondholder as a first line creditor of any organization who seeks primarily safety of his principal and a steady income with little or no emphasis on appreciation. He loans his money for relatively long term expansion activities, his risks are minimum and his returns comparative. Premiums or discounts paid in bond prices align themselves closely with the proximity of the maturity date, and the percent of return is figured only after amortizing the same over the period held. With rising business activity, idle funds seek maximum profit if not restricted by law; therefore, bond prices fall when stock prices rise. The speed at which each changes is, however, not uniform, as bond trends are much slower than stocks.

A brief review of American industry in 1929 reveals overexpansion of production facilities for prevailing consumption. The underlying cause for bond flotations was negligible. Bond prices fell as their yields increased. At the depth of the depression in 1932, signs of business recovery presented themselves. With visions of better business ahead and its relative improved ability to pay its debts, bond prices started to rise. With the rise in the cost of living, greater selectivity in choice of bonds was needed to maintain a steady income. Plans for switching part of funds into high grade common stocks were attracting attention.

Available to the investor are industrial, railroad, utility, municipal, foreign, and government and miscellaneous bonds. Each depends upon an individual set of circumstances
for its value, and the subdivisions including: convertible, debenture, callable, sinking fund bonds, equipment certificates and others complicate one's analysis.

Assisting him in his choice from speculative to United States Savings Bonds, which pay at the rate of 2.9% compounded semi-annually to maturity, are numerous Bond Manuals such as Poor's, Fitch's, Standard Statistics, and Moody's. However, since ratings are not forecasts and rarely are revised downward "until market quotations already have declined considerably", the investor must look elsewhere for information on their future prospects. As, by the very nature of a bond, it is constantly deteriorating, it needs constant surveillance to detect inherent weakness in the issuing company. A steady return and adequate margin of safety may be maintained only by timely switching of funds to better situated issues.

As soon as the investor eliminates U. S. Savings Bonds and ventures to choose other profitable government securities, he is confronted with the new 'managed currency' which experts cannot satisfactorily explain. The government, envisioning higher commodity prices as fundamental to recovery set in motion activities to effect the same. It marked up the value of gold and silver, printed currency to the amount of the write-ups and showed the amount of the write-ups as income. The general effect was, of course, to make an easier money condition than otherwise existed.

1. U. S. Booklet--"United States Savings Bonds"--1
With the U. S. Treasury in command of banking policies, "The banks have truly underwritten the bull bond market from 1932--1938, and any rise in interest rates with its relative fall in bond prices would greatly impair the capital of the banks."¹

"Business has taken advantage of low money rates to refund outstanding obligations, not to put men to work, buy machinery, and expand facilities--as a recovery expedient, low money rates have been largely a dud".²

"Adding to the perplexity of the situation has been the constant pouring of foreign gold to the U. S. Treasury as a haven of safety. There is a close correlation between surplus funds in the banking system and the movement of bond prices. In the latter part of 1936 the monetary authorities, fearful that the credit structure was getting out of hand, cut sharply into surplus funds by raising reserve requirements. This move was followed in December by the gold sterilization program, and in the spring of 1937 reserve requirements were again raised."³ Although foreign trade amounts to but about 10% of our National Income, the excess gold within our structure minimizes export activity which is vital to some companies.

In view of government competition with private industry, the bondholder must increasingly vary his portfolio as to

¹ "Surplus Funds Dominate Bond Prices"--Barron's 7/11/38--1
² Williams, J. S.--"The Bond Bulletin"--The Magazine of Wall Street--1/13/40--422
³ "Surplus Funds Dominate Bond Prices"--Barron's 7/11/38--2
maturity, industry, and locality. Those overweighted with mortgages have publicly admitted their distress through the Banking Holiday of 1933. A brief glance at the erratic Labor movements within the decade emphasize the difficulty of the wage earner to meet regular installment payments of any description with the resulting loss and tragedy to the buyer and frozen assets to the lender.

"Indicating further the lack of incentive for idle funds to enter American Industry is the fact that from the end of 1929 to the end of 1933 the government bond holdings of the 26 largest legal reserve life insurance companies advanced from only about $300,000,000 to about $4,500,000,000. At December 31, 1932, the market value of bonds owned was 1.18 billions less than cost. On December 31, 1938 the market value of bonds owned by them was 360 millions less than cost." ..."In 1930, the average rate of return on bonds was 4.70%. It dropped every year thereafter and stood at 3.45% in 1938".1

Private financing originated to assist the small businesses to get funds; but greater use has been made of it by large corporations desiring to avoid the S. E. C. regulations on publicity. Taken by the 26 insurance companies referred to above, representing nearly a third of all new corporate bonds and notes issued during the five year period, 1935--39,

were: 2

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount</th>
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<tr>
<td>1932</td>
<td>$33,300,000</td>
</tr>
<tr>
<td>1933</td>
<td>16,783,000</td>
</tr>
<tr>
<td>1934</td>
<td>90,647,000</td>
</tr>
<tr>
<td>1935</td>
<td>$351,378,000</td>
</tr>
<tr>
<td>1936</td>
<td>327,792,000</td>
</tr>
<tr>
<td>1937</td>
<td>371,353,000</td>
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<tr>
<td>1938</td>
<td>659,508,000</td>
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2. Ibid
The full effect of this method of distributing securities may be seen only in retrospect, but its practice is disconcerting to the private, individual bond buyer.

This decade tragically emphasizes the results of over-enthusiastic, over-optimistic, and over-timed extension of capital. Records of tremendous losses are common knowledge, and the tone of recent reporters in explaining the causes for the great debacle of 1929 leave one wondering why, at the time, its impending magnitude could not have been cushioned. Yet, when one admits that over the years, labor’s share of gross income steadily increased with intensified production, it is not surprising, under the then prevailing regulations of the New York Stock Exchange, that even the bootblack was interested in the tape.

In spite of such leaders as New York Central dropping from its 1929 high of 256 to 8 in 1932, Radio from 114 to 2 1/2, Electric Bond & Share 567 to 5, and Auburn Automobile 514 to 29; it is equally exciting to follow them thru 1933:

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<th>1933</th>
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<tr>
<td>CN</td>
<td>14-----58 1/2</td>
<td>18 3/8--45 1/4</td>
<td>12 1/4--29 3/4</td>
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<tr>
<td>RC</td>
<td>9 -----12 1/2</td>
<td>4 1/2--9 1/8</td>
<td>4 -----13 3/8</td>
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<tr>
<td>EBS</td>
<td>9 7/8--41 5/8</td>
<td>6 --23 1/2</td>
<td>3 1/2--20 3/8</td>
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<tr>
<td>AAC</td>
<td>31-----84 3/4</td>
<td>16 1/2--57 3/8</td>
<td>15 -----45 1/2</td>
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<td>27 3/4--49 5/8</td>
<td>15 1/8--55 1/4</td>
<td>10 -----21 1/4</td>
</tr>
<tr>
<td>EBS</td>
<td>15 3/4--27 5/8</td>
<td>5 7/8--23 1/8</td>
<td>4 1/4--15 7/8</td>
</tr>
<tr>
<td>AAC</td>
<td>26 5/8--54 1/4</td>
<td>3 1/8--36 3/4</td>
<td>2 1/2--6 1/2</td>
</tr>
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</table>

A glance at the action of others is more encouraging:

1. Adjustable Stock Ratings--The Magazine of Wall Street Compilation
Monsanto  |  1929 |  1932  
Humble Oil |  43   |  12    
Minneapolis-Honeywell |  41   |  41    

|  1933   |  1934  |  1935  |
MTC  |  25----83  |  39----61 5/3  |  55----94 3/4  
HB   |  40----105 1/2 |  33 1/4--49 1/2  |  44----64  
MWH  |  13----36 3/8  |  36--65    |  58----150  

|  1936   |  1937  |  1938  |
MTC  |  79----103  |  71----107 1/2  |  67----110  
HB   |  57----80   |  54 7/8--87  |  56----72 5/8  
MWH  |  65----112  |  53----120  |  46 1/2--92  

***

Into these figures may be read many facts from statements since published. However, they are presented merely to show the power of some companies to grow while others decay.

The common stock holder is the risk bearer of business. Throughout his life he is a debtor to his company. In reorganization he must meet an assessment to pay the creditors if his company is to continue and possibly gain strength and its future relative share of prosperity. His returns depend not only upon the prosperity of his company, but upon the disposition of his directors in distributing the earnings.

From approximately 1200 stocks listed on the NYSE, he must decide first in which industry he wishes to participate, and then in which company of that industry. His knowledge of any industry is generally negligible, and by the time he understands one, some new industry arises from a chemist's test tube, or substitutes have been developed which seriously alter the future prospects of his choice.
Available for his reading and study are highly recognized daily financial papers, periodicals, and statistical services. With time available, his decisions may well vie with the forecasts of Investment Services, and his success be commensurate with his knowledge.

"The trend of government actions the world over, and particularly in the U. S., is undoubtedly in the direction of a managed economy. In investing, as in everything else, one has to deal with conditions as they exist. Taxes sharply penalize the rewards of diligence and shrewdness, the regulations of the Securities and Exchange Commission, too, have made impossible the quick fortunes of the past. Yet Wall Street is still the outstanding marketplace of the world—a free and open arena where, now that the abuses and deceptions of manipulation have been outlawed, no one can honestly claim that the cards are stacked against him." 1 "..."The stock-market merely registers and does not cause, what takes place in the realm of business and profits." 2

In the late stages of a bull market the distribution of stock "rights" by many companies is common practice. They serve as a means for the company to secure added capital, and at the same time tend to bring down the price of the stock within the range of the average investor's pocketbook, "thus creating a broader and better market". 3

"There is always a ready market for Rights, and the

1. Nelson, H. G.—"Commonsense Speculation"—Barron's 5/9/38—1
2. Ibid
holder should be certain to ascertain the value of all rights accruing to his interest and dispose of them, if not to be exercised, before date of lapsing. A simple formula for computing the value of rights is: 

\[ \text{Premium} \times \frac{\text{Ratio}}{1 + \text{Ratio}} \]

The premium represents the difference between the market price of one old share and the offering price of the new. The ratio represents the relationship of the number of new shares offered to the number held. Taking A. T. & T. offering for example, the difference between market and offering prices is $67 and the ratio is 1 for 3. Therefore:

\[ \frac{67 \times \frac{1}{3}}{1 \times \frac{1}{3}} = 16.75 \]

the value of the right accruing to each old share. "Precedent calls for a snapback in the price of the stock when the rights expire."

Related, in that they are an accessory to existing securities, are "warrants" which "frequently make their appearance in connection with and to enhance the attractiveness of senior issues and are exercisable only on presentation of the senior security. Their fluctuations will trace a pattern directly similar to the movement of the stock to which they entitle purchase." Since, the stock cannot be purchased until advanced from the date of issuance of the warrant, the investor may reason, especially in the case of a reorganized

2. "Rights"--The Magazine of Wall Street--1/13/40--p. 427
company: as it re-establishes a firm financial footing, the stock will reflect that earning power, and for him there would be greater profit prospects in the common stock than in his senior security. Speculators in the warrants only, with no intention of buying the stock, involve much less money than the purchase of the stock itself. Properly timed, such transactions can be highly profitable.

When substantial income is sought without the risk involved in common stock, one may decide upon preferred stock. Since preferred issues have no maturity date like a bond, changes in prices are more erratic than bonds. When a stalemate in the capital market no longer exists, prices of senior securities decline. As interest rates rise, holders of non-callable preferred stocks face a loss in capital. Accumulated dividends often become burdensome to the company and are paid off in stock rather than in cash. High grade callable preferred stocks in a period of prosperity may be replaced by lower dividend issues."

"Convertibles have been growing in favor during recent years because they offer some protection against both inflation and rising interest rates. A conversion feature will not prevent a preferred stock from declining sharply if conditions threaten the security of the dividend. In a period of business decline, the straight investment features of a convertible assume major importance. Safety becomes the paramount consideration. Convertibles represent an attempt to

1. Lawrence, Herbert--"How Sound Are Preferred Stocks"--Barron's 11/27/39--18
straddle the chasm between fixed income securities and equity shares. Obviously such an attempt involves a more complicated investment problem than would be the case if the investor were making a commitment in either a non-convertible bond or stock.

In buying convertibles, it is essential for the investor to determine whether he wants to place the greater emphasis on security or on price appreciation possibilities. If it is the latter, then the investor will do well to watch the turns of the market with virtually the same care as he would give to common stock investments, for it is generally true of all investments that those which go up the most in bull markets tend to decline most in bear markets." 1

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1. Lawrence, Herbert--"Convertible Preferred Stocks"--Barron's 12/4/39--p. 19
Brokerage Mechanics The New York Stock Exchange is simply a market place. Its members trade in securities on the floor of the Exchange, either as brokers for others, as is usually the case, or for their own account. In the latter transactions, however, members are governed by strictly enforced rules which insure the precedence of customers' orders over their own.

The Stock Exchange is a voluntary association of 1,375 members, the majority of whom are partners in some 630 brokerage and investment firms, which are known as "member firms". Its Constitution, signed by each member, is a contract binding him and his firm to abide by the rules of the Exchange whose aims, as stated by its Constitution, are: "To furnish exchange rooms and other facilities for the convenient transaction of their business by its members; to maintain high standards of commercial honor and integrity among its members, and to promote and inculcate just and equitable principles of trade and business."

Trading is conducted on the floor of the great hall of the Exchange which, being more than 100 feet wide, 133 feet long and 79 feet high, is one of the largest enclosed spaces in the world. Here terminate 2,000 private telephone lines connecting brokers on the floor with their offices in New York. They in turn are in communication by private wire systems with their 1,100 branch offices, their 130 member correspondents and their 4,200 non-member correspondents.
The Exchange owns and occupies the four buildings covering the block bounded by Broad, Wall, and New Streets and Exchange Place. In this property, together with other assets, each member has a 1-1375th interest.

The purchase price of seats is determined entirely by supply and demand and is paid to the retiring member, not to the Exchange itself. Dues, paid by members at the current rate of $1,000 a year are augmented by fees for the listing of securities, charges for the rental of facilities within its building, the sale of quotations, charges to members for the clearance and delivery of securities effected through the Stock Clearing Corporation, and other income to enable the Exchange to meet its payroll and other expenses.

Statistics indicate that about 15,000,000 Americans own securities directly. The number who own them indirectly is incalculable, but it must include the owners of the nation's 39,000,000 savings banks accounts and 63,000,000 insurance policies, because every bank and insurance company of consequence has a proportion of its assets invested in listed securities.

General partners in member firms have unlimited personal liability for all the acts and commitments of their firm, thereby contributing not only to financial stability but to prudent and conservative business methods.

Like all American securities markets the New York Stock

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1. So called from a palisade ordered constructed on the site in 1652 by Peter Stuyvesant, Governor of the Dutch colony of New Amsterdam, who feared invasion by the British. In popular usage it designates the financial district of New York City.
Exchange operates under the supervision of the Securities and Exchange Commission, created by an act of Congress in 1934. This law, designed to increase the legal responsibilities of the Exchange and its members and to afford investors additional protection in their dealings.

Each of the seventeen trading posts handle the market for fifty or sixty different stocks. The casual visitor to the Stock Exchange gallery is apt to be much impressed by the uproar of trading on the floor and by the mechanical appliances in use there but inadequately appreciative of the more important human mechanism. That bedlam which he sees below him is in reality created by the movements of hundreds of orderly but energetic individuals performing their work systematically and efficiently. It is through the highly specialized work of several different types of brokers that the securities market operates.

The membership of the Exchange can be divided roughly, into several different groups, each with a different function. Most numerous are the commission brokers. Then there is the 42 broker who makes use of his Exchange membership to assist commission brokers in executing their orders. He is most useful and prosperous in brisk markets when the commission broker's business is too large for him to transact alone. He imparts a flexibility and a reserve power to the facilities of the Exchange, enabling it to handle with efficiency great surges of business.
The **old-lot dealer** handles less than the trading unit of 100 shares. Also a dealer is the **floor trader** seeking a profit for himself. His usefulness lies in supplying the market with bids and offers of stock.

The **specialist** is both a broker and dealer in one or more securities traded in at a single post where he remains throughout the day. But he cannot act as broker and dealer in the same transaction. He is a "broker for brokers" and receives a commission for each order he executes as a broker, which is paid by the member who gave him the order. As a rule, limited orders at specified prices above or below the current market are handled by him. In trading or dealing the specialist must give precedence to the orders of his customers. He operates under many restrictions designed to maintain the highest ethical standards.

Approximately seventy members of the Exchange trade only in bonds as brokers or dealers.

The Exchange, some years ago, established, within the Exchange, its own training school--The Stock Exchange Institute--where employees of the Exchange and of member firms study the highly specialized work of the securities business.

The market structure now occupied by the Exchange was completed in 1922 to provide additional facilities to accommodate the sudden expansion of investment and speculative demand which followed the World War and reached its spectacular climax in 1929. A year earlier, the Exchange, in order to augment its floor trading area, had purchased two adjoining buildings, giving it control by ownership or long-term
lease of an entire city block.

The organization of the Stock Exchange today is the result of varied and practical experience dating back to 1792. During the intervening years of steady expansion and evolutionary process, there has grown up a great deal of tradition in connection with the institution which it is unnecessary to recite here. However, its code of ethics and its code of practices are of the highest order, and it is the constant endeavor of the management to see that these standards are rigidly maintained.

In 1867 the electric stock ticker was adopted to give speedier transmission and more reliable and complete publicity to prices.

The principal requirements for a listed security are:
that the company be a going concern having substantial assets and a satisfactory record of earnings; that the issue be sufficiently large to warrant listing and widely enough distributed to permit the maintenance of a free and open market; that the company agree to follow certain procedure regarding corporate practice, form of reports, etc., designed to protect the investor.

In 1829 the first train was moved by an American steam locomotive in this country. A year later the first railroad stock—that of the Mohawk and Hudson Railroad—was listed on the stock exchange. 1

"The 1,375 members of the New York Stock Exchange were classified by the SEC according to their primary functions, as of October 1, 1935. The divisions were as follows:

<table>
<thead>
<tr>
<th>Role</th>
<th>Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Commission Brokers</td>
<td>391</td>
</tr>
<tr>
<td>Floor Brokers (§2)</td>
<td>153</td>
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<tr>
<td>Floor Traders</td>
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<tr>
<td>Odd-Lot Dealers</td>
<td>25</td>
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<tr>
<td>Odd-Lot Brokers</td>
<td>115</td>
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<tr>
<td>Bond Brokers and Dealers</td>
<td>76</td>
</tr>
<tr>
<td>Specialists</td>
<td>348</td>
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<tr>
<td>Inactive Members</td>
<td>227</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1,375</strong></td>
</tr>
</tbody>
</table>

"As defined by William C. Van Antwerp, former governor of the Stock Exchange—anent the Floor Trader—"They do not accept orders; each man is in business for himself. They entertain no illusions, and they recognize no alliances with each other. Each one follows his own inclinations, and does not permit himself to be moved by tips, or rumors, or gossip, or sentiment. He is intent, resourceful, suspicious, vigilant, and ubiquitous. He is a bull one minute, a bear the next. He asks no quarter, and gives none."  

"From early days of the American Republic, the law regulating security markets has been characterized by gradual growth rather than abrupt change. With the enactment of the [Securities Exchange Act of 1932](https://www.sec.gov/rules/factsheets/actof1932.htm) on June 6, 1934, what here-tofore has been evolution has become revolution".

"Congress finally brought all of the country's stock exchanges under governmental regulation. The Securities and Exchange Commission was organized to administer this Act and

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1. Warshow, Robert Irving, op. cit., p. 22
2. Ibid—page 35
formulate rules and regulations to govern orderly and honest trading. This legislation marks the most important development in stock market practice in over a century."

"The Commission is composed of five men appointed by the President by and with the consent of the Senate. Not more than three are of the same political party. Each has no other vocation and does not participate in stock market transactions of the character which are subject to the regulation by the Commission. Their salary is $10,000 each yearly and they hold office for five years except the commissioners first appointed."

"The SECURITIES EXCHANGE ACT is designed primarily to regulate credit in security transactions, to limit speculation, to prevent unfair practices, and make public adequate information on securities publicly traded in, and to discourage the unfair use by insiders of information which is not made public."  

With "inadequate regulation of the nation's system of credit" given as the "cause of the excessive speculation such as prevailed in the boom years of 1923 and 1929", it is not surprising to find much emphasis in the Act upon margin trading.

"A broker is not a public servant. He is a private business man engaged in one of the most profitable and secure undertakings it is possible to find in our business organization.

1. Warshow, Robert Irving, op. cit., viii--Introduction  
3. Ibid--p. 11  
4. Ibid--p. 12
He takes absolutely no risk on customers' purchases or sales, being always fully secured by the customers' margins. He carries no inventory, has to take no depreciation losses like other businessmen, has no plant or machinery of consequence, and needs no special technical training. His profits come from commissions and interest charges. If he is a good businessman, as in any other line of business, he will try, wherever consistent with the prevailing ethics of his line, to get as much trading as possible, so that he may get more commissions. The personal probity of brokers naturally varies, just as there are honest and dishonest lawyers or doctors or butchers."

"Customers' men were often compensated by the operating syndicate for spreading news of a pool operating in a certain stock, a point which served usually to induce the customer to purchase. Section 19 of the ACT empowers the Securities Commission to regulate the manner and method of soliciting business by customers' men."  

By the ACT the broker is now restricted in his borrowing by Section 8. "In order to control the flow of credit at its fountainhead, brokers and dealers are not allowed to borrow in the ordinary course of business except from the Federal Reserve System, or non-member bank agreeing to the same laws as member banks and to the extent permitted by the Federal Reserve Board from other brokers or dealers in emergency cases. In this way the Board's control of credit for stock market

1. Warshow, Robert Irving, op. cit.--p. 30
2. Ibid--p.--47
Brokerage Mechanics

commitments is made complete." 1

Brokers are forbidden to permit aggregate indebtedness incurred in the ordinary course of their business to exceed twenty times their capital, exclusive of fixed assets and Exchange Membership. They are also forbidden to commingle securities of a customer in a common loan with securities of others, or to lend securities of a customer, without the written consent of the customer concerned. "Where the broker and dealer functions are combined in a single person, his own interests may conflict with the interests of those to whom he owes a fiduciary duty. This conflict may react to the disadvantage of his brokerage customers in a variety of ways." 2

"The Commission in a recent report states that "generally speaking, the rules were designed to eliminate excessive speculation on the part of exchange members, to delineate more clearly certain of the fiduciary obligations of a broker to his customer, and to restrict certain practices regarded as detrimental to the interests of the investing public." 3

"Under Regulation V, the Federal Reserve Board permits a bank to loan a broker or dealer 60% of the current market value of a stock registered on a national securities exchange, if the securities hypothecated for the loan are carried for the account of his customers. 4 There is nothing in the law to prevent the Federal Reserve Board from decreasing the loan

1. Meyer, Charles H., op. cit.--p. 14
2. Warshow, Robert Irving, op. cit., p. 74
3. Ibid--p. 152
4. Ibid--p. 52
permitted to five or even one per cent, thus eliminating margin purchases in effect." 1

"In cases of bankruptcy of brokerage firms it has frequently been found that the firms have borrowed from their banks on customers' securities more than what the customer owed." 2

"The first large syndicate in the U. S. formed by insiders for the purpose of stock speculation had for its basis the program of Alexander Hamilton to redeem the national debt in the form of interest-bearing public stock. This was during Washington's first administration." 3

"Millions were made by this pool in their speculative activity in government securities." 4

In the 50's, Cornelius Vanderbilt, Jay Gould, and Daniel Drew were associated in pool operations on a large scale and among them practically controlled the market. So long as they played fair with each other, they were consistently successful. But often they tried to make a double profit by secretly selling while the other pool members were buying. It was the result of one of these coups on the part of Drew and some other associates that Vanderbilt wrote:

Gentlemen: You have undertaken to cheat me. I will not sue you because the law takes too long. I will ruin you.

Sincerely yours,
Cornelius Vanderbilt 5

The famous Gold conspiracy engineered by Jay Gould in 1869 and designed to corner gold in the U. S. with the aid

1. Warshow, Robert Irving, op. cit., p. 53
3. Warshow, Robert Irving, op. cit., p 122
4. Ibid--p. 123
5. Ibid--p. 123
of persons close to the President is an instance of a daring pool that went wrong." 1

"In the boom period from 1922 to 1929, as many as a hundred pools sometimes operated at one time in different securities, mostly public favorites which had an active market." 2

"Of course, pool operators are not always successful. William C. Durant, one of the most powerful operators in the stock market has several times been in serious difficulty. In 1926 he was managing a small provisions market at Asbury Park, but once was the controlling factor in General Motors Company." 3

"When stocks are low and public demand dimmed, there are very few pools, for almost always they are dependent upon the accumulation of large groups of small traders who can be relied upon to buy, once the quotations are lifted far above the value of the stock manipulated. At the first sign of increasing market activity, the pool managers start work. After the lean years of 1931 and 1932, there was a stock market stir in the spring of 1933 when President Roosevelt entered upon his new program. The Senate Investigating Committee, in its stock market investigation, uncovered the details of many of these pools, and the testimony is as startling as it is enlightening. John T. Flynn traces in detail the pool organized early in 1933 to manipulate the stock of American Commercial Alcohol Corporation, and his

1. Warshow, Robert Irving, op. cit. -- p. 124
2. Ibid -- p. 124
3. Ibid -- p. 126
report is used as a basis for this summary. It should be borne in mind that besides the rise in stock prices, there was a special public interest in alcohol stocks on account of pending legislation to repeal the Prohibition Amendment."

"In 1933 the officers decided to raise funds through the sale of common stock. The logical method would have been to offer the new issue to present stockholders, particularly as the market in May 1933 was good for alcohol stocks, and the new financing would have received a ready response. The corporation decided on a very complicated scheme, however, instead of making an offering to stockholders. This plan was designed both to evade the law, as later indicated, and as a money-making scheme. Dummy corporations were set up to acquire the stock." 2

"From May 15 to the middle of July the market price of ACA rose from 21 to 89 7/8. Thereafter the price broke until it went back to $30 a share." 3

"E. F. Hutton & Company, the famous brokerage house, engineered a similar pool for the same company at another time. In spite of the fact that this well-known brokerage house was heavily interested in the stock, their market letters during the period of the pool consistently recommended purchases by customers. The testimony before the Senate Investigating Committee uncovered a mass of factual material regarding the activities of many other pools. The men testifying were under oath and a reading of the manuscript of these

1. Warshov, Robert Irving, op. cit.--p. 126
2. Ibid--p. 127
3. Ibid--p. 130
sessions will repay the student of the stock market manipulation."

"Naturally, the startling evidence unearthed in the investigations led Congress to insist in the new Securities Act provisions designed to limit, if not abolish, manipulative practices on the exchanges. Section 9 of the new law is specifically designed to eliminate certain practices common heretofore in the manipulative operations. Wash sales, matched orders, market rigging, dissemination of false information, paying or receiving a consideration for disseminating information, and issuing false or misleading statements, are expressly forbidden. Some of these points have heretofore been prohibited by internal exchange regulations, but very seldom enforced."  

"The prohibition of market rigging, that is, the buying and selling at the same time by pools for the purpose of creating an appearance of market activity and creating a following, is the most important provision, because it has always been found by pool managers so necessary a part of a pool operation."  

"The vicious practices of stock market pools in the past have affected every small trader. Daniel Drew once said that 'buying stocks in Wall Street, if you are not an insider, is like buying cows by candle-light'. The chances are against the small trader at best."  

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1. Warshow, Robert Irving, op. cit.—p. 130  
2. Ibid.—p. 130  
3. Ibid.—p. 131  
4. Ibid.—p. 132
"The knowledge of past pool operations is valuable; the knowledge of the present law is a further protection. It is to be hoped that the administration by the Securities Commission will be forceful and unwavering. Since criminal penalties are provided by the law in every case and civil penalties in addition in some instances, the particularly stringent provisions covering inside manipulation should prove effective."

"Information required by the ACT adds little if anything to listing requirements of the New York Stock Exchange other than the disclosure of the remuneration of officers, directors, and high salaried employees." The issuer of securities must keep information up to date, and file annual and quarterly reports, the former certified by independent accountants, if so required by the Commission. Every director or stockholder owning 10% of any class of stock is required to file with the exchange and with the Commission a report of his holdings. Any change in the same must be reported by the tenth of the following month. When a profit is made within six months of the time he buys it, or if he buys it back within six months of the time he sells it, he must turn over the profit to the company. Directors, officers, and 10% holders are forbidden to sell short the stock of their company.

Although the Commission is not empowered to interfere in the internal management of any corporation, it may require various reports from those corporations who invite the public

1. Warshow, Robert Irving, op. cit.--p. 132
to invest in their securities. Its power over exchange rules covers so broad a field of stock market technique that almost any part of the routine of the securities business could be changed at its instance." 1

"The uniformity of reports enables investors to make comparisons with other companies in the same line of business, and their frequency enables the intelligent security holder to keep in closer touch with his company's affairs than heretofore." 2

"To a substantial extent the law is experimental and its effects in operation are largely unpredictable." 3

"Stock market trading is a complicated business and a hazardous one. The reader can try only to assure himself of a decent percentage, and in order to secure this, he must take advantage by preparing himself with every weapon at his disposal. In the past, the large operators and insiders have been armed with machine guns and the small trader with toy pistols. The struggle has been unfair and their results disastrous. The securities act of 1934 should, by eliminating many of the unfair practices current in the last few years, give the small man a decent chance. It is to be hoped that the administration of this law will be as unyielding in its enforcement as the legislators have been in the enactment of the law. If they are, we can have reasonable assurance of a free and natural stock market, where intelligent conclusions will have a fair chance of being fulfilled." 4

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2. Warshow, Robert Irving, op. cit.--p. 16
4. Warshow, Robert Irving, op. cit.--p. 167
Equipped with these facts, the presence of a serious problem in their administration is obvious when superimposed on the shortest and sharpest decline in stock values in the history of the averages during the fall of 1937 in which, in spite of increased margin requirements and other regulations, millions of dollars were lost while fifteen million security holders were being 'protected' by the government supervision.

If the prospective investor seeking profit eliminates from his activity margin trading and short selling in favor of outright purchases, he yet entertains an illusion if therein he expects safety of principal. He has precluded two sources of loss, but if his 'timing' of purchases and sales is in error, his capital may wilt or freeze. As all writers of long experience emphasize--nothing is static; therefore, once one ventures into business, he at no time leaves his business without someone responsible in his place who is conscious of daily developments with the authority necessary to act upon the same.

The margin trader is intrigued by price changes, more than investment quality of various industries. He is most active in periods of low interest rates. He has been credited with and blamed for the 1929 rise and fall.

When one reviews the easy interest rates over the early 20's and the eagerness with which commercial banks accepted securities as bases for loans both to brokers and individuals, one might agree that the banks were truly the 'pawn brokers
of margin traders' and also better understand the flourishing investment banking institutions which bloomed in the latter 20's. The forming of bank affiliates to deal in securities not eligible for bank investment was common practice, but the Banking Act of 1933 divorced these securities affiliates from the commercial banks.

"The usual service of the commercial banks to business in supplying short-term credit vanished, as corporations could go directly to the security market for funds and with no interest charges. Just how much of the ensuing trouble was caused from over-investment in equipment or over-expansion of credit is still debated, but 'the use of securities as collateral during good times of booms represents a pyramiding of credit'."

"The portfolios of commercial banks during late years indicate to what a small extent the original dream of those who framed the Federal Reserve Act has been accomplished. On June 30, 1937, member banks had over $18 billion in investments and about $14 billion in loans. Over two-thirds of these investments were in government securities. Of the loans, about one-third were on securities, and nearly one-sixth were on real estate. Between 20% and 25% of the loans on securities were probably for business purposes and not for speculation. But only about 2% of the total loans and investments of all member banks were represented by acceptances and commercial

1. Simpson, Kemper--"The Margin Trader"--Harper & Brothers
New York, 1933--p. 83
2. Ibid--p. 80
3. Ibid--p. 93
paper bought in the open market. Finally, the 'all other loans', which comprise the bulk of the real commercial loans, have become a relatively unimportant asset."

"On October 4, 1929 brokers and dealers had loans from member banks of the Federal Reserve System of about $2.8 billion and from the other lenders of $6.4 billions. In addition, the banks were lending on securities of their customers other than brokers and dealers. In the Banking Act of 1933 loans for account of others were prohibited. In the Securities Exchange Act of 1934, the board was given power to increase the margin requirements for security speculators which it did in 1936. The commercial banks, however, have continued to supply by far the largest part of the credit extended margin traders."

"In 1935 and 1936 the Treasury's insistence on cheap money, prompted by its desire to sell government bonds at low interest rates, prevented the restrictive money policy customary during booms." "Few men of affairs foresaw that one of the greatest speculative booms was to be followed by one of the worst depressions. The fact that the cycle problem has become more acute may be due to increasing complications of our economic life. And among the complications which augment the amplitude of cyclical fluctuation the excesses of margin trading are certainly not the least important."  

1. Ibid--p. 74--Hearings before the Sub-Committee of the Committee on Banking and Currency of the United States Senate--1931
2. Ibid--p. 32
3. Ibid--p. 106
4. Ibid--p. 117
"Just what part Margin Trading had in the 1935-36 boom and the 1937 crash may be reflected in the following facts. The cash used to buy securities is largely in the form of bank deposits. When investors, margin traders, banks, investment trusts, and other corporations have larger bank deposits, they have more 'cash' with which to purchase securities. As evident, all the banks in the U. S. showed an increase in deposits of about $8 billion between 1935 and 1937. A part of this $8 billion increase was created by government deficit financing. These banks showed an increase of investments during that period of about $4 billion, most of it in government bonds. During the same period over $2 billion of gold flowed into the U. S. This gold inflow and the New Deal Silver Policy also served to increase commercial bank deposits. Thus, commercial bank deposits were increased for the most part by factors other than commercial loans." 1

"When it is considered that much of this cash shied away from bond markets where yields were kept low by Treasury policy and SEC laxity in registering refunding issues, it is easy to understand how it got into the stock market." 2

"Member banks' total loans on securities amounting to $4 billion in 1937 were probably just as excessive under the changed circumstances as member banks' loans on securities of over $10 billion at the end of 1929." 3

Although the regular installment buyer of merchandise

1. Ibid--p. 129
2. Ibid--p. 130
3. Ibid--p. 131
might think that buying stock on a borrowed money plan assures him of eventual ownership, he may find the payments irregular, untimely, and ruinous."¹ In view of the extensive losses suffered by many investors, the Securities Exchange Commission has given a great deal of attention to the matter of margin requirements, both as a protection to the investor against himself and the overzealous broker who encourages such trading in the hunt for commissions.² Instead of the 'shoestring' margins of the early stock market history varying from nothing to whatever was conducive to assured business, a margin requirement of 55% of the current market price of stock has been set.³

"The ACT authorizes the Board to provide different standards for purchasing as against carrying a security, and it is expected that the margin requirements, once a security is purchased, will not be quite as rigid as in the case of initial purchases. At the present time, there is nothing to prevent the broker, once the initial purchase is properly margined, from carrying the account as long as he desires, subject only to his own protection.⁴ Under the law certain securities are exempt from these margin provisions, and a bank or broker may make any loan he desires on these. These exempt securities are securities of the U. S. and state governments and their subdivisions and such other securities

1. Bernstein, Allen, M.--"Merchandising Your Investment--
   Greenberg Publisher, New York--1936--P. 15
2. Warshow, Robert Irving, op. cit., p. 49
4. Warshow, Robert Irving, op. cit., p. 55
as the Stock Exchange Committee later exempt from the provisions of the law."

"The broker, in borrowing from the bank on his customers' securities, usually pays the call loan rate, which is announced each day on the floor of the New York Stock Exchange, and appears on the ticker and on the financial pages of all the metropolitan newspapers. This rate has been recently 1%. In inspecting over 50 different brokers' statements at a time when the call loan rate was 1¾%, the writer found that the lowest interest rate charged was 3% and that several debited the customer with as high as 6% on small accounts." 2 "The differential between the bank rate and the brokers' rate is so large that it has proved one of the most important sources of income to brokers.

The small customer will do well to scrutinize carefully the interest charges on his account. Some investigation may be the means of an immediate saving. Upon investigation, the customer will find that some houses will offer him better interest rates than others, and a little shopping before opening his account may mean several hundred dollars a year saved. It must be kept in mind that no fixed rate for interest is set by the New York Stock Exchange or any other authority, and naturally, the broker will charge all he can get unless the customer protects himself beforehand." 3

"Until the SEC regulations, brokers freely loaned customers' securities to other brokers in connection with

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1. Warshow, Robert Irving, op. cit.--p. 55
2. Ibid--op. cit.--p. 67
3. Ibid--p. 69
short sale transactions. Such a practice tends to deflate
the stock which the margin holder bought for appreciation.
Written permission must now be given the broker for such use
of stocks, and since no split is made between the broker and
customer for what the broker receives on such business, the
customer will do well to refuse the permission.\(^1\)

It is difficult to find any writer who recommends margin
trading under any conditions, yet the average investor is
left in a quandary as to its weight in causing severe losses
through fast changing price movements such as were recorded
in the fall of 1937 under strict regulations, primarily a
'cash market'.

While trying to understand this phase of trading, the
remarks of J. George Frederick in Common Stocks and The
Average Man constitute good background:

"For the average man, margin trading in stocks is a
snare and a delusion. It should be said, however, that
margin trading is a perfectly legitimate operation. It
enlarges the operations for making profit and also enlarges
the chances of loss. Fundamentally it is a device for the
technical purposes of speculation; not long pull investment
speculation, but in and out trading. It is really a labor
saving device and convenience for those who are technicians
in speculation; and also for those men of wealth, with ex-
tensive credit, who may logically assume large risks."\(^2\)

1. Warshow, Robert Irving, op. cit.--p. 106
2. Ibid--page 264
"No good business man would dream of accepting all the money that any bank is perfectly eager to loan him; he must at all times keep his credit position sound." 1 "The bridge builder considers maximum strain and then builds with a margin of safety to spare." 2 "One of the greatest rules which has ever been hatched out of a Wall Street checkered career is 'have a fixed policy and stick to it'. A man who has a salary of less than $10,000 and a rather small capital should not indulge in margin trading. He should be content to buy a few well selected bargains outright as usual." 3

Although through the three main odd-lot dealers 4 one can be sure of the purchase or sale of his securities at from one-eighth to one-half point away from the current market, the history of such practice raises a flag of caution:

"It appears that over the period 1920--1938 as a whole the public has come out very badly. The average price at which stocks were sold by the public in the months of net selling is about 14% lower than the price at which they were bought in the months of net buying, and the present market valuation of the unliquidated balance is 10% lower than the average price at which it was bought. (Calculation from Standard Statistics Index of average prices of 419 stocks.) For 1925--1938 the

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1. Warshow, Robert Irving, op. cit--p. 265
2. Ibid--p. 268
4. Carlisle, Melleck & Company) DeCoppe and Doremus ) together do over 97% of Jacquelin and DeCoppe ) business
percentages are 28% and 23% respectively. The public bought
odd lots heavily in the boom years of 1928--1929 and just as
heavily in the bear market of 1930--1931.¹

"The activity in odd-lots increases as the prices
increase. The odd-lot dealers, for inventory position, buy
and sell in round lots daily, but under the present regulations,
they may make but one sale or purchase in round lots before
executing a customer's order, thus eliminating their influ-
ence on the price obtained for the customer's account, as the
customer's price is based on the 'last round lot sale' made."²

"An odd-lot transaction is certain of an execution
one-eighth of a point away from the next round-lot trade,
no matter how great may be the preponderance of odd lot or-
ders on the same side of the market. This certainty of ex-
ecution is part of what the trader pays for in the differen-
tial."³ "At Post 30, where all the odd lots are of less than
ten shares, the differential ranges from one-quarter point to
two points according to the price of the stock."⁴

The dealers provide an elaborate system of recording the
tape time and price of every round-lot trade so that the cus-
tomer may be assured that his order has been properly execu-
ted. A tabulation of the net profit for the three odd-lot
dealer firms from 1929--1938 emphasizes the importance of
volume of business to this group and helps to explain the
$1.12\frac{1}{2}$ average differential to the odd-lot customer:

¹. Ibid--p. 56
². Ibid--p. 36
³. Ibid--p. 138
⁴. Ibid--p. 140
## Odd-Lot Dealer--Net Profit

<table>
<thead>
<tr>
<th>Year</th>
<th>Per Share Traded</th>
<th>Per Odd-Lot Share Traded</th>
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<tbody>
<tr>
<td>1929</td>
<td>$.0451</td>
<td>$.0545</td>
</tr>
<tr>
<td>1930</td>
<td>.0236</td>
<td>.0279</td>
</tr>
<tr>
<td>1931</td>
<td>.0207</td>
<td>.0246</td>
</tr>
<tr>
<td>1932</td>
<td>.0262</td>
<td>.0307</td>
</tr>
<tr>
<td>1933</td>
<td>.0430</td>
<td>.0491</td>
</tr>
<tr>
<td>Five Year Average</td>
<td>.0334</td>
<td>.0395</td>
</tr>
<tr>
<td>1934</td>
<td>.0030 Deficit</td>
<td>.0035</td>
</tr>
<tr>
<td>1935</td>
<td>.0390</td>
<td>.0475</td>
</tr>
<tr>
<td>1936</td>
<td>.0392</td>
<td>.0470</td>
</tr>
<tr>
<td>1937</td>
<td>.0192</td>
<td>.0233</td>
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<td>1938</td>
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<td>.0290</td>
</tr>
<tr>
<td>Five Year Average</td>
<td>.0250</td>
<td>.0300</td>
</tr>
</tbody>
</table>

Somewhat similar to the stock market practice of **short selling** was the Biblical incident of Esau selling his inheritance, which he did not own, to his brother for a mess of pottage. In that incident immediate delivery was made, whereas promised delivery in the future must be assured in the stock market transaction of today. The principle is basically sound in terms of commodities for future delivery; but its practice in miscellaneous industries is enveloped in multiple risks and added costs.

As the issue to be sold is not available to the customer for the broker's use, the broker must--from the "loan crowd" which gathers on the floor of the Exchange after the market closing at 3 P. M. daily--borrow it. The costs of the borrowing are charged to the customer's account, and an additional Federal Tax is imposed on short selling. Any dividends

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1. Hardy, Charles O.--op. cit.--p. 163

2. Warshow, Robert Irving, op. cit.--p. 102
paid are sacrificed by the customer; and unless pre-arranged with the broker, interest at the call rate is not credited to the customer's account to, even in a small way, counteract the dividend loss.

Rule 16 in Section 7 of the SEA "represents the first attempt made to put any curb on the practice of 'short selling'. It "prohibits any member from effecting a short sale either for his own account or for the account of others at a price below the last sale price on the exchange." 1 The purpose of this regulation is to prevent the indiscriminate offering of stock for a short seller on a scale down, and thus create an appearance of unusual activity on the downside." 2

"Another specific regulation is in Section 16, which prohibits officers, directors and stockholders owning more than 10% of the stock of a corporation from selling the stock of their own corporation short." 3

"There is no question but that short-selling has been the medium for many bear raids, a factor in accelerating a decline, and a baneful influence in the depression period. How the evil effects can be avoided and the basic principle permitted is a problem which is difficult of solution and will undoubtedly be the subject of experiment by the Securities Exchange Commission administering the new Act and the Federal Reserve Board, to whom some of its powers have been delegated for administration." 4 "Legislation in the past in other

1. Warshow, Robert Irving, op. cit.--p. 157
2. Ibid--p. 158
3. Ibid--p. 107
4. Ibid--p. 108
countries has not been successful. In the United States no serious restrictions have ever been imposed up to 1934. As an emergency measure, particularly in a period of rapidly falling prices, when the market is vulnerable, restriction or supervision of short-selling seems to be a necessity. Certainly, the NYSE has not proved itself amenable to any adequate restrictions even in the most extreme periods, and some outside agency seems required to take measures when needed, even if these be temporary in period of time and limiting in effect." 1

"Short selling for the small trader can only be recommended when used in selling stocks actually owned and as a convenience until stocks can be secured for delivery, or as a hedge against other securities held. It may serve as an insurance measure until he can fully decide as to the course events will take. The sacrifice of commissions and the other charges may be warranted in such hedging, as an insurance premium, by a feeling of greater stability in a period of changing values." 2

When the investor realizes that short selling generates a 'margin account', and that unless all margin account customers by written request disallow their brokers to loan stock held on margin, forces are at work to defeat his plan, greater caution may be exercised in the use of this feature in trading.

1. Warshow, Robert Irving--op. cit.--p. 109
2. Ibid--p. 112
"The Securities Commission defines a put as 'an option in favor of the holder of the put to require the maker within a specified time to purchase and pay for a specified security at a stipulated price'. The usual charge is $37.50 for three days and $137.50 for thirty days. If the customer accepts the 30 day option, he will pay the specialist $137.50 and receive a memorandum receipt which will empower him to sell to the specialist the 100 shares at any time within the option period. If, within thirty days, the stock should go up or not down sufficiently, the customer will lose his option fee and the transaction is closed at the end of the stated period."

In issues that have had a substantial rise in the past ten days, activity for puts implies that stockholders are seeking to protect their long positions.

"A call operates on the same principle, but the option privilege entails the purchase of stock, rather than the sale, as in the case of a put. The fees are the same, and the purchaser of the call has the option of buying the stock at the agreed price and within the stated period."  "A $2 service charge for every put or call transaction handled through a broker is charged. If the put or call is not exercised, the loss is limited to the initial charges. If, however, the option privilege becomes of value within the period, the customer, in order to take advantage of his option privilege, must both sell and buy the stock and pay the regular brokerage commission and

1. Warshow, Robert Irving, op cit.--p. 136
2. Barron's--"The Option Market"--9/18/39--p. 12
3. Warshow, Robert Irving, op. cit., p. 106
taxes in addition on both operations. If the quotation of
the option is five points from the market, the customer should
figure seven points before it becomes profitable to close the
transaction." 1

"Most of the time, purchases of puts and calls merely
expire by limitation and with it the original investment.
These are the longshots of the trading plungers." 2 "Puts and
calls were purchased very widely by small traders in the boom
period and, recently, with active markets and wider fluctua-
tions, are coming into vogue once more. The apparent advantage,
as against purchasing a stock on margin appeared in the fact
that the liability of the customer was limited to the initial
charge, and the carrying of a sizeable amount of stock for a
period entailed a comparatively small amount of capital. This
advantage is more apparent than real." 3

"The percentage against the trader is so large that the
chance of profit on this type of transaction is always a long
shot. Trading in puts and calls is a desperate form of spec-
ulation for the small trader and is in ninety cases out of
a hundred ill-advised and foolhardy." 4

"The mass of put and call trading is in the nature of
a racket. Some of it is legitimate, arising from the wish
of holders of stock to hedge by selling options. Most of it is
artificial and the small trader will do well to avoid trying

1. Warshow, Robert Irving, op. cit., p--136
2. Ibid--p. 138
3. Ibid--p. 139
4. Ibid--p. 139
to hit these long-shots by staying close to the legitimate and natural method of buying either outright or on safe margin."

"Spreads and Straddles are variations of put and call options. They are option purchases of puts and calls combined, of the same stock, and purchased at the same time. A spread is an option to buy and sell the same quantity of the same stock within a stated period, both options being usually given for a similar number of points away from the market price. A straddle is an option entitling the holder to either buy or sell, within a given period, a certain stock at a fixed price, the market price, or a price away from the market. These are complicated devices of speculators, expensive, and are very seldom desirable forms of options for the small trader."  

"When straddles are in fair demand, they reflect the market uncertainty on the part of buyers who want protection in the case that the market breaks out of the current rut on either side."  

Since the specialist hopes to keep the $137.50, and since he is in a position to know the outstanding orders 'Good Until Cancelled' in the various issues, the price at which he is willing to sell either puts or calls represents a hard bargain. The figures published on the Option Market may well be included in forming one's opinion of the general market, as expanded offerings of puts may indicate a bullish outlook,

1. Warshow, Robert Irving, op. cit.--p. 141; also The Magazine of Wall Street--"For Profit & Income--Calls as a Hedge"--12/17/38--p. 268  
2. Ibid--p. 138  
while an active demand for puts may represent insurance against long positions in stocks as indicated by 'The Option Market Column' in Barron's of September 28, 1939.

The Securities Exchange Commission defines a stop-loss order as 'An order to buy or sell a stated amount of a security at a market price if and when a transaction occurs at a designated price. The purpose of such an order may be to limit the loss on an open commitment; to safeguard a profit on an open commitment; or to insure the making of a new commitment when a specified price level is reached.'

"It is also used by a customer who cannot meet a call for margin, but who wishes to hold the stock as long as possible. The stop-loss order in that case is placed at the lowest point the broker will allow. A sharp decline, even if only of a few days duration, often swept hundreds of margin accounts away. At a time like this, specialists and floor traders would go gunning for stop-loss orders in order to accentuate the decline and force weak stock into their hands. Where a decline was obviously due to such a technical condition, floor traders were quick to act to garner in easy profits at the expense of the small margin traders."

The latest schedule of commission rates adopted by the New York Stock Exchange effective January 3, 1938 is as follows:

"On stocks selling at 50¢ per share and above, the commission rate per share shall be not less than the following:

1. Warshow, Robert Irving, op. cit., p. 40
2. Ibid—p. 41; also Booklet—"Trading Methods"—Chisholm & Chapman
Price per Share | Rate per Share (100-unit) | Rate per Share (10-unit)
---|---|---
50¢ and above but under $1 | 2 | 3
1 | 3 | 6
2 | 4 | 7
3 | 5 | 8
4 | 6 | 9
5 | 7 | 10
6 | 8 | 11
7 | 9 | 12
8 | 10 | 13
9 | 10 | 14
10 (Base Rate) | The 13½ base rate plus 1¢ for each $10 of the price per share | The 14¢ plus rate for each $10 of the price per share for (10 and above)

On stocks selling below fifty cents per share—special schedule.

Five dollar minimum commission except:
1. To banks, brokers, and all dealers
2. On transactions involving an amount less than $200
3. On concurrent multiple orders executed on the same day

In addition to the above rates, the New York Stock Exchange has made, effective January 3, 1938, a service charge which applies to inactive accounts carried by a member firm. This charge cannot be stated in a few words, but in a general way, it amounts to a minimum of $2.00 per month on an account, which at the close of business on the last business day of the month, has a debit balance of $1,000 or less, or no debit or credit balance, or a credit balance of $2,500 or less, provided during such calendar month the account does not have transactions in securities or commodities on which the total commissions are at least $3.00. The charge on such accounts may go above $2.00 if many securities are carried in the account. There is a pro-

1. Jackson & Curtis
vision in this ruling so that in the ordinary case where a cash purchase is made and the security is in our office over the end of one month and taken out before the end of the next month, there would be no charge.1

In addition to these commission charges, one must figure on the stock transfer tax which varies greatly between states, it being much less on the Boston Exchange transactions than on the New York transactions. Not to be forgotten are the state and federal taxes on both dividends and capital gains. As stated elsewhere in the section on Investment Services, the average total cost approximates 3% of the funds employed. The interest charges on margin accounts together with safety deposit rental costs also reduce the net gain in trading.

Business Barometers:  **Business Activity**—Available to the investor are various barometers or indexes to business activity, past, present, and future. As various publications subdivide American industry into many groups, a study of each reveals important relationships between them. The fact that directors of corporations cannot show a continuous profit in their particular field multiplies the investor's problem—to preserve and accumulate capital. The investor, however, does have the advantage of being able to select, for whatever length of time he chooses, participation in the various industries. In no course which he ever studied had he so great a challenge or satisfaction in successful completion. He becomes an integral part of the course 'Applied Economics' which has limitless requirements for mere passing, and a lifetime may prove too short for honors.

Periods of prosperity are based upon the expansion of the producers' goods group of industries which represent new capital created for long-term use such as steel products, building and construction. Orders in these lines set in motion activity in supplying fields. The time needed by each line to fill the orders varies; therefore, the business cycle for each is not exhausted simultaneously.

"Followers of the heavy goods industries have had little but disappointment for almost a decade despite all kinds of logical proof that "sooner or later" the needs of this type left unsatisfied during the depression must be filled and must cause a boom in producers' goods. It is characteristic of
durable goods companies to swing in wide cycles, exhibiting very large earning power in active periods and frequently running into red figures during slumps; paying good dividends for a few consecutive years, then omitting payments entirely when business falls off. This cycle has always been accepted as a normal thing and the prices of individual issues follow business hopes and fears to far greater extremes than do those in the stable industries."

"The most valued single barometric item is steel scrap, the price of which is available in any metropolitan newspaper. A sudden drop in steel scrap is usually the forerunner of a let-down in steel operation. Almost as important as steel scrap to business and security market calculations is the price of copper. It is the raw material of the electric age in which we live."  

The investor constantly keeps in lead position the earnings of those industries in which he is interested. The productive capacity of the industry as a whole is the introduction to the analysis. The increased use of light, alloyed steel in recent years has enhanced the prospects of makers of the same. "Producers of alloys for steel manufacture have established themselves in recent years as indispensable units in the system which turns out the instruments of modern industrial production. They also are essential to the manufacture of many finished products. This dependence of the steel

1. White, Cyrus V.--"Securities To Hold Today for Tomorrow's Profit"--The Magazine of Wall Street 6/17/39--223
industry on these companies for supplies of tungsten, molybdenum, chrome, vanadium, nickel and other ferro-alloys has enabled concerns such as International Nickel Co. of Canada, Climax-Molybdenum Co., Vanadium Corp. of American and Molybdenum Corporation of America to establish good earning power and in many cases to grant good dividends."

"But modern metallurgical progress, backed by aggressive research, continues to change the values of some alloys as compared with others; and thus the relative importance of particular companies in the steel alloy field is likewise subject to change. Examination of these trends from time to time is necessary in evaluating the probable future earning power of the alloy concerns in question."

"Vanadium metal had a period of dominance in several fields during the late 1920's but it was lost in the early 1930's as molybdenum and other cheaper alloys entered the field. Molybdenum also has displaced tungsten to some extent as a tool steel alloy. Crucible Steel Company makes about one-half the nation's tool steel. Ferro-Chrome sold by Vanadium Corp. is an important alloy for quality steel. Foreign influences affect all four companies to an extent, but Climax and Nickel the most."

Supplementing figures on iron ore consumption, percent of pig iron furnaces in blast, pig iron production, and steel ingot production, such periodicals as Steel and Iron Age and reports from the American Iron and Steel Institute furnish

1. Cooke, R. F.--"What Alloy Producers are Earning"--Barron's 8/19/39--9
2. Ibid--p. 9
valuable data.

In spite of the fact that there has been a "70% gain in the electricity consumed by the various average residential customers between 1929--1938", the production figures alone are but the prologue to tragedy for many public utility security owners in this period owing to the Public Utility Act of 1935. The figures published by the Edison Electric Institute do however reflect the great secular growth in the use of electricity and assist the investor in making his decisions among suppliers of industrial or residential power, electrical equipments, or even chemicals, as the latter take their place in refrigerators and air-conditioning equipment, and plastic moldings.

Although electric output in kilowatts "reflects the general rate of activity in many industries it serves, and to a degree, the level of prosperity of its domestic customers", as an indicator of utility net earnings, electric power production is not always satisfactory. In periods of pressure on rates and of rising operating costs and taxes, net profits can fall even though output in terms of kilowatt hours holds up well. Assuming no change in rates, a decline in output due to lessened industrial activity does not necessarily mean a corresponding decrease in utility gross revenues, since industrial power is sold at relatively low rates. Conversely, rising industrial demand for power in a recovery period does

1. Lawrence, Herbert--"Vigorous Growth of Electrical Industry" Barron's 6/5/39--7
2. Compiled as to Source
3. Wooten, James W. Jr., op. cit., p. 56
not mean the same percentage gain in gross. A goodly portion of such additional revenues, however, may be carried through to net profit, if no new facilities are required to take care of the business."

"Long considered an accurate measure of the state of business are freight carloadings. However, because of the competition from other forms of transportation, the tendency has been for carloadings to advance during a period of improved business at a rate less than that of business as a whole, and to decline to a proportionately greater extent during periods of depression. 1937 showed a gain over 1932 of 41.3% while industrial production in 1937 averaged a 72% advance over 1932."

"However, in spite of this variance, and the fact that freight cars have a larger capacity than they did in 1929, carloadings are among the indices most generally followed by the public and for this reason alone, they have a substantial influence upon the sentiment toward market prices. Seasonal trends are reported and are comparable with the same period the year previous."

All financial papers carry this information—some daily, some weekly, and others monthly. The thirteen Regional Shippers' Advisory Boards of the Association of American Railroads furnish it subdivided under 29 important commodities.

"The miscellaneous freight reflects the movement of heavier

1. Electric Power Production—Behind the Figures—Barron's—5/2/38--11
2. Wooster, James W. Jr., op. cit., p. 51
3. Ibid—p. 51
industrial demand for these raw materials which is significant from an industrial point of view."

Carloadings figures appear in Engineering News Record on Friday of each week, in Railway Age monthly, in The Wall Street Journal on Monday weekly, and in the Magazine of Wall Street bi-monthly.

As one learns more about the sources of revenue by railroads in which he may be interested, the carloadings become more vital in his estimate of their worth.

When, as in Barron's, the business failures for the week are given as a single number, little weight can be placed upon them by the reader who is left wondering how much money was involved, what type of business predominated, and the general source of original capital. "Over the eight year period between 1929 and 1937 some 82 million dollars of principal were charged off as bad debts, and an additional sixty-six million dollars of charges were uncollected. Between the two, the personal finance companies of the country sustained a loss of one hundred and forty-eight million dollars." As serious as these figures appear, conclusions drawn from these facts, if available, might be different: total loans from combined sources, total business done, and total loss from bankruptcies.

Fundamental weaknesses in the Bankruptcy Act, however, seem evident. "With one-fifth of the population of New York, Alabama, in 1931, had 80% more wage-earner bankruptcies.

1. Barron's--August 21, 1939
2. Neifeld, M. R., Ph. D.--"Personal Finance Comes of Age"
   Harper & Bros. Publishers
   New York City 1939--p. 178
Alarmed at the tremendous loss to creditors from the rising tide of bankruptcies, which seemed to be due to leniency in provisions of the Bankruptcy Act, commercial credit and financial interests sought to plug up statutory loopholes. A committee of eminent lawyers under the chairmanship of Colonel William J. Donovan made an investigation in New York for federal Judge Thatcher. Extensive study of the Bankruptcy Act, enacted July 1, 1898 brought the committee to the conclusion that rapid and far-reaching economic changes had made the inadequacies very apparent and that slow-moving procedural machinery, the breakdown of creditor control, the large domination of administration by attorneys had opened the way to bankruptcy frauds. The Donovan report stimulated the Department of Justice to make a nationwide study and as a result, extensive amendments in the law were recommended to Congress in 1932 by the Attorney General of the U. S. These proposals were intended to restore the sanctity of contract by tightening the application of the Bankruptcy Act so that debtors would not have easy access to this means of repudiating their obligations. The details of the new statute on the Bankruptcy Act of June 22, 1933 were the result of facts gathered over six years by outstanding lawyers, accountants, bankers, legislators, economists, business men, judges, referees, text-writers, all schooled in bankruptcy law and procedure.  

Related to business failures are those traceable to brokers' loans which "still furnish one of the surest indicators

1. Ibid--p. 139
of the character of buying entering the market--their message is always significant".  

From the peak in 1929 to the spring of 1932, brokers' loans had been reduced 93%, and were approximately equal to the present figure; but in the following weeks that total was again cut in half.  

The added protection to the investor from the loaning power of brokers being reduced by new margin requirements is challenged by many.  "Brokers' loans reached a peak of $8,500,000,000 in 1929 and declined to less than $400,000,000 in 1932."  

Any attempt to try to explain managed currency and its effect on interest rates is futile because of the complexity of its nature; however, the ordinary investor can profit by putting some of the facts together. The well written pamphlet by Charles R. Whittlesey--"Banking and the New Deal" does throw light upon the call money rates over the decade. Reflecting upon these figures from 1924, Babson writes:

"In 1924 money was available at 2%; while at the height of the stock market boom in 1929, call money loaned up to 20%. With the collapse of the stock market boom, the demand steadily fell off again and in 1932 call money was available around 1 1/2%."  

One sees an inherent weakness in the Federal Reserve System which was designed to control speculation--"To afford

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1. Brokers' Loans--Magazine of Wall Street--11/5/36--61  
2. Brokers' Loans--Magazine of Wall Street--5/7/36--72  
5. Ibid--Babson, R. W.--p. 7
seasonal and emergency elasticity by providing for the issue of currency or the extension of bank credit against discounted commercial paper." 1 "The amount of discountable commercial paper is influenced, obviously, by the price of the goods against which the paper is drawn. If their price is rising, an increasing quantity of commercial paper can be issued against them and this permits the issue of an increasing amount of circulating medium. The tendency for prices to rise is, therefore, not checked as it would be if the quantity of circulating medium were inelastic, but instead feeds upon itself. In good times, borrowers will probably be willing to expand credit at a rate in excess of the volume of business, and bankers will almost certainly be willing to have them do so. In bad times the opposite holds true." 2

Although business indexes have recorded marked improvement since 1932, "call loans currently earn but 1 3/4%." 3 "The easy money policy sponsored by the Government and Federal Reserve System has recently come in for some well deserved criticism from responsible financial quarters. It has been validly pointed out that low interest rates will, alone, offer no inducement to undertake capital expenditures, while at the same time they act to discourage savings and individual thrift." 4

1. Whittlesey, Charles R., op. cit., p. 3
2. Ibid--p. 4
4. Interest Rates--The Magazine of Wall Street--1/29/38--524
In a study of Interest Rates and Stock Speculation, Richard N. Owens and Charles Hardy found repeated lack of correlation between money market and the stock market. 1 "High money rates were no barrier to climbing stocks in 1907 and 1929; ludicrous money ease was no dam to the liquidation of 1937. A factor of no fundamental worth, but one which has to be reckoned with on many occasions, is speculative psychology. The astute investor must guard against the infection of speculative psychology." 2

Regardless of from what angle the investment problem is attacked, the investor gets back to the problem of new financing. When business was at its peak in 1928--1929, "new corporate issues were pouring forth at the rate of more than $500,000,000 a month and hit a post-depression high late in 1936, the year in which the bonus payment pushed the Government deficit to a record level." 3 The dearth of such financing is reflected in the earnings of the leading engraving and security printing company--American Bank Note--with the following price fluctuations:

<table>
<thead>
<tr>
<th>Year</th>
<th>Earnings</th>
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<tbody>
<tr>
<td>1934--11 3/8--25 3/8</td>
<td>86 Deficit</td>
</tr>
<tr>
<td>1935--13 3/8--47 3/8</td>
<td>1.36</td>
</tr>
<tr>
<td>1936--36 --55 3/8</td>
<td>1.24</td>
</tr>
<tr>
<td>1937--10 --41 3/8</td>
<td>1.07</td>
</tr>
<tr>
<td>1938--10 --23 1/8</td>
<td>.35 Deficit</td>
</tr>
</tbody>
</table>

Increases in new financing directly describe the confidence in the future expressed by American Industry.

Inventory accumulation in view of profits aligns itself.

2. Ibid--Barron's 5/30/38--13
with Commodity Price Indices. The best known based upon a large number of representative commodities is the Bureau of Labor Statistics index of wholesale commodities which is compiled from over 800 quotations. \(^1\) "A notable aspect of the 1923-1929 prosperity was the relative stability of the commodity price structure and the balanced price relationships between such major commodity groups as farm products, raw materials, semi-finished goods, and finished goods." \(^2\)

"The goal of the Roosevelt Administration has been and still is to restore the general price level to approximately what it was in 1926 and likewise to restore as far as possible the 1926 parities between the more important commodity groups. Obviously, the difficulties confronting our price planners are enormous. Prices of many basic commodities—wheat, cotton, rubber, and copper, to mention but a few—are subject to a multiplicity of supply-demand factors operating both nationally and internationally. Monetary credit manipulation has been demonstrated to be a most imperfect instrument for regulation of the general price level and is, of course, wholly useless as a weapon directed against price disparities. That is why the Administration has shied away from the monetary approach to price control. Early last year when it was thought that some prices were getting too far "out of line," notably that of copper, the President tried to talk them down. He succeeded to a disastrous extent. In

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3. Ibid--572
knocking the psychological props out from under the international speculation in raw materials then in progress, he contributed materially to the following deflation of most all prices."

"That prices of most manufactured goods are now out of line with both industrial raw materials and farm commodities is due largely to the economically unjustified and over-fast raising of hourly wage rates in key industries late in 1936 and during the forepart of 1937. Upon the raw materials and consumers' durable goods, the impact of depression falls hardest and fastest. When business men believe, for whatever reason, that their outlook for sales and profits has become unfavorable, they curtail or halt buying of raw material, semi-finished, and finished goods virtually over night." 1

"Best of the commodity futures indexes is the Dow-Jones index which includes prices of commodities in an adequate number of active raw material markets. Refinement of the study of commodity prices in their bearing on business earning power and thus, in turn, on the stock market, may be had by recourse to a sensitive spot commodity price index." 2

"Moody's Daily Commodity Index is one of the most sensitive being composed of spot prices for volatile commodities, and rapid changes therein are upsetting to business equilibrium." 3

Even though 1929--1933 was marked by one of the most drastic periods of deflation ever recorded in commodity

2. Nelson, H. G.--"Commonsense Speculation"--Barron's
prices, carrying wholesale prices 30% below the July 1929 level, current research into the earnings of various companies reveals profits during the ensuing period of readjustment—"which taught business that it can make a profit at low prices when it has conducted the necessary housecleaning." 2

"Retail food prices declined, on the average, about 35% between the middle of 1929 and 1932, and general living costs were 12% below the levels of November 1929. Hence a flood of wage cuts was released during the last half of 1931 which action extended into 1932, when general wage levels were liquidated on a basis of approximately 20% below the peak of 1929." 3

The new concept of cash and credit in the early 20's provided fertile ground for the personal finance companies' activities, resulting in the average American family enjoying its highest standard of living ever attained. The abyss into which many fell is not evidence of national recession. "The potentiality for economic expansion in this country is enormous, prophets of 'stagnation because of economic maturity' to the contrary notwithstanding. To hold that our living standard has reached its maximum while more than 40% of the families in this country have annual incomes less than $1,000 and while 79% of all families have incomes under $2,000 is to confess that we do not know how to use the world's most abundant pool of productive resources--plentiful raw materials,

1. Babson, Roger W.--Washington And The Depression--p. 3
2. Ibid--p. 3
3. Ibid--p. 11
efficient factories, intelligent and energetic labor, resourceful technicians and managers, excellent transportation, billions of idle capital."

Difficult as the proper weighting of each of the foregoing barometers of business may be in the investor's current problem, recognition of their general acceptance and awareness of their general position will help him to justify decisions for action.

1. Mathis, George--"Standard of Living"--The Magazine of Wall Street--1/13/40--393
Te c hni c

H u man

R e a ct ions

t o

G ood
a n d
B ad

N e w s

F O R E I G N

r a tes a r e d i f f i c u l t t o t r a c e h e r e f o r t h e i r i m p o r t. H o w e v e r,
in a ny c r i s i s o f n o t e, s p e c u l a t i o n s v a r y i n i n t e n s i t y f r o m
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w r i t e r s w h o s e p h i l o s o p h y h e s u p p o r t s, a n d, f r o m t h e m, h o p e
t o g e t t h e p i c t u r e a s f r e e f r o m b i a s a n d p r o p a g a n d a a s p o s s i b l e.
A t t h e s a m e t i m e, h e m u s t s u p e r i m p o s e t h e g e n e r a l s t r e n g t h o r
w e a k n e s s o f t h e m a r k e t a t t h e t i m e a p o n t h e f o r e i g n s i t u a t i o n.
W h o l e s a l e c o n f i s c a t i o n o f A m e r i c a n o w n e d p r o p e r t y, f o r i n-
stance, i n f o r e i g n c o u n t r i e s m i g h t r e a d i l y s e t o f f a l i q u i d a-
t i n g p r e s s u r e, w h i c h, o f i t s o w n m o m e n t u m m i g h t l e a d t o a
s e r i o u s l y o v e r - s o l d c o n d i t i o n; a n d r e s u l t i n h e a v y l o s s e s.
W r i t e r s g e n e r a l l y a g r e e t h a t p r i c e s f l u c t u a t e m o r e i n a n t i c i-
p a t i o n o f a f a c t t h a n u p o n t h e r e a l i z a t i o n o f t h e s a m e.

E a r n i n g s

T h i s i s t h e r u l e r a t h e r t h a n t h e e x c e p t i o n
i n t h e c a s e o f e a r n i n g s a n d d i v i d e n d s.

S i n c e, i m m e d i a t e l y p r e c e d i n g t h e d e c l a r a t i o n o f d i v i d e n d s,
they r e p r e s e n t p r o f i t s, t h e p e r s h a r e i n t e r e s t i n t h e c o m p a n y
b a l a n c e s h e e t i s g r e a t e r t h a n a f t e r t h e i r t u r n i n g i n t o a
a d d e d l i a b i l i t y. I f, w i t h i n a r e a s o n a b l e t i m e, h o w e v e r,
the p r i c e r e c e s s i o n i s n o t r e g a i n e d, o n e m a y q u e s t i o n t h e
j u d i c i o u s n e s s o f t h e p o l i c y. W h e n, a s i n t h e p a s t f e w y e a r s,
l i t t l e p u b l i c p a r t i c i p a t i o n f o l l o w s t h e a n n o u n c e m e n t o f
i m p r o v e d e a r n i n g s, t h e i n v e s t o r i s b e s e t w i t h t h e p r o b l e m o f
finding out what factor must be altered to result in a more
natural response. Every action he takes has its price or
reward. Can he afford to subscribe to such sentiment as
this, for example:

"Once we took it for granted not only that business
was good, but that it would permanently stay good. That was
in the days of the New Era; the Victory over the Business
Cycle; the Chicken in Every Pot; the Two Cars in Every
Garage, etc. Now, after some years of experience with the
New Deal, the more abundant life, security for everybody
and the redistribution of everything, we are going in in a
big way for the opposite illusion—the illusion that any-
thing more than a short-lived business recovery would be
abnormal and therefore improbable."

On should he equip himself with a graphic service such
as Investogaphs, Inc. or Securities Research Corporation
which emphasize relationships of price to earnings over a
long period and select securities which look promising
based upon the more academic methods of computation?

"Stock prices in 1929 were more than 100% higher than
in 1926, yet corporation earnings were up only 5%. "The
rule of thumb used to be that a stock is reasonably priced
at ten times its earning power. Of late years, the sensa-
tional growth of certain industries, notably chemical and

1. Mathis, George W.--"Examining the Base for Sustained
Recovery"—The Magazine of Wall Street—
1/13/40--392
2. A Booklet—"A Practical Approach to Profitable Investment"
Investogaphs, Inc. 1938—p. 9
aviation, has resulted in a yardstick materially longer than the old fashioned ten to one. As long ago as 1928 John J. Raskob, then chairman of the finance committee of General Motors Corporation, publicly went on record that stocks of the caliber of General Motors should sell for '15 times earnings'. No hard and fast rule can be set down. Probably somewhere around 15 to 1 is a sound basis for a take-off for a sustained flight."

Showing similar sentiment are the following figures taken from the Financial World:

"25 Leaders Measured by Price Earnings Ratio"

<table>
<thead>
<tr>
<th>Group Average--1926--1929</th>
<th>14.7</th>
</tr>
</thead>
<tbody>
<tr>
<td>1935--high</td>
<td>20.2</td>
</tr>
<tr>
<td>1936--high</td>
<td>19.0</td>
</tr>
<tr>
<td>Recent Ratio--------------</td>
<td>14.2</td>
</tr>
</tbody>
</table>

"What is reasonable capitalization of earning power nowadays is probably the most moot point of discussion in Wall Street. The 'biggest and best' issues are here (in the late part of spring 1938) selling in many cases for from 30 to 40 times estimated annual earnings. Only the utilities, which are commanding 11 to 12 times earnings ratios, appear reasonably priced. Time alone will tell whether some new and latent influence accounts for the apparently unwarranted price level of the so-called 'blue chip' industrial issues. Certain industries, because of their in-and-out results, namely, the constant recurrence of losses

2. "Taking the Measure of Stock Prices Now" Financial World--9/22/37--p. 11
after profits, command a much lower ratio. For that reason sugars, leathers, rubbers, automobile accessories, and the like are not susceptible to the application of the 'times earnings' check. Many investors have been lured to ruin by the superficial appeal of a five or six to one earnings ratio which suddenly vanished with the advent of hard times."

In anticipation of tax-forced dividends from a great many corporations through the operation of the Revenue Act of 1936, many stocks were in demand; but "the investor who is in receipt of the additional distribution should appraise the action in its longer term perspective. In many instances the money paid out to stockholders could be used to better advantage in the business, and thus what amounts to a return of capital is not an unmixed blessing in the manner in which the equity is affected. It should be also noted that a higher dividend basis in the current period, giving effect to any extras, does not establish a basis for coming years, since it will undoubtedly be a part of corporate policy to predicate dividend action upon the earnings results in any one year, and past experience will only be a matter of history. And although there may be some market price stimulation afforded through favorable dividend action, the fundamentals of investment policy which reckon with prospective earnings trends as well as with current achievement have not been set aside because of modifications of sound business judgment through short-sighted tax laws."  

1. Nelson, H. G.--"Commonsense Speculation"  
   Barron's 5/20/38--p. 9  
The temporary price changes in securities attributable to statements made by holders of influential political positions are of little consequence to the long term investors. If the fundamental factors for profit remain, increased earnings can be anticipated with relative price appreciation.

"The earnings statements covering full 1936 operations furnished eloquent testimony to the fact that--despite very large increases in taxes and other expenses--American business has not been experiencing "profitless prosperity." 1

"While this is a condition that cannot continue indefinitely, the end appears to be a considerable distance in the future." 2

**Merger**

"Not only is it true that mergers are usually made effective during a major bull market, but it is also true that stocks of companies about to merge (or which the public believes about to merge) are usually the spectacular favorites in such a market." In short, the whole atmosphere of mystery and the prospect of uncertain developments make an irresistible appeal to those having gambling instincts. Speculators or traders may well buy just prior to the time of merger, but as investment or as long pull speculation, that is rarely a wise time to buy. In most cases the temporary disadvantages are eventually overcome and then the more permanent advantages of mass financing, buying, production, and selling begin to show their effect. In the majority of mergers observed or studied historically, the

1. "The Trend of Things"--The Financial World--4/21/37--p. 4
2. Ibid--p. 4
turning point appears to have come somewhere between the third and seventh year of the new company's life. 1

One popular sample during January 1937 was that of Nash-Kelvinator. 2 Promptly after appearing at about 17, the new stock quickly rose to between 24 and 25; but could be bought at the end of 1938 at around 3.

Reorganizations In contrast to mergers, reorganizations are numerous in periods of depression. Earnings are inadequate to meet the fixed charges on outstanding obligations, and "fixed charges can only be reduced in two ways, either by paying off the indebtedness, which is generally impracticable, or by arbitrarily changing the nature of the indebtedness to make at least part of it bear contingent charges." 3 Many corporations in the past decade have taken advantage of the low money rates to reduce their funded indebtedness, though not being formally reorganized through any court procedure. Holders of callable bonds were in possession of free funds for re-investment with only fields of reduced income available to them. The mechanical reorganization of any company does not insure a steady improvement for the same as selected instances reveal, for example: Radio-Keith-Orpheum, Reo Motors, and McKesson & Robbins.

1. Vance, Ray--"Investment Policies That Pay"
   Barron's--New York City, 1930--p. 8
2. Clifford, J. C.--"Nash-Kelvinator--A Soundly Conceived Merger"--The Magazine of Wall Street
   12/5/36--p. 228
"Beginning in June 1934, applications began to be recorded under the famous "77B" section of the Bankruptcy Act. Month after month, a considerable number of firms, chiefly large ones, have taken advantage of this opportunity to readjust their indebtedness and capital structures without incurring the expense and disruption of regular bankruptcy proceedings." 1 Such savings tend to be applied toward payment of bank loans and commercial creditors. 2

"Although this form of adjustment is far preferable to bankruptcy for both debtor and creditor, it still spells loss for creditors in the scaling down of indebtedness or the interest rate on obligations." 3

On May 22, 1937 about 30% of the country's railroad mileage was in receivership involving about 3 1/4 billion of securities. 4 Both economic and political factors contributed to their predicament. The drastic loss of revenue during the depression years together with unsatisfactory freight rates set the background. Government control over wages and operating policies limit earnings. The Railroad Income Account for 1929--1939 shows the following % of Return Before Fixed Charges: 1929--4.84, 1932--1.25, 1938--1.43. 5 Yet, "as measured by ratio of operating income to gross revenues, the

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1. "Failures and the Course of Business"—United Business Service--5/22/37--p. 204
2. "A Sharp Rise in Bankruptcies"—United Business Service--2/12/38--p. 54
3. Same as #2
5. New York Herald Tribune--1/2/40--p. 39
efficiency of the railroads has increased some 30% during the past six years; and some roads are getting double the operating income from a given level of gross that they formerly obtained."

"Some of the more important roads in receivership have been able to maintain equipment and buy new rolling stock to a greater extent than a solvent road barely covering fixed charges. The solvent road's income must go toward paying bond interest, but the bondholder of the receivership road is in the same category as the 'forgotten man'."

Locomotives constitute approximately one-tenth of all railroad investment and nearly one-third of operating expense is applied to the repair and operation of this one-tenth of investment.

"Considerable difficulty has been experienced in constructing suitable reorganization plans under Section 77 of the Bankruptcy Act. The I. C. C. has publicly deplored the delay and recently refused to grant time extensions. The R. F. C. has also manifested the hope that reorganizations would be hastened." "Confidence in the financial outlook for the railroads has become badly impaired, and Congress by its dilatory tactics in connection with proposed railroad relief legislation is responsible for undermining sentiment

1. Fulton, Pierce--"Why the Rails Are Coming Back"--The Magazine of Wall Street--6/19/37--285
2. Dodge, Frederick K--"Speculative Possibilities in Rail Equipment Stocks--The Magazine of Wall Street--1/15/38--432
3. Same as #2--p. 433
further.”

However, as the whole history of American railroads is one of receivership and reorganization, the investor of this decade might well afford to analyze defaulted rail bonds for income and appreciation. "In my judgment, based on the background of a third of a century of intimate acquaintance with rail problems they stand now on the threshold of their greatest period of usefulness and of prosperity. The railroads are our most dependable and efficient means of transport. Their modernization, from whatever point of view you choose, is second in importance only to the modernization of our Army and Navy. The average rail locomotive is of the model of the last World War." 2

As assuring as this sounds, intense, contrary opinion only confuses the prospects both of rails and rail equipments: "So far as basic railroad factors are concerned, the trouble is by no means solely political regulation or excessive debt or rising costs of wages and taxes or motor and water carrier competition. Probably the most significant single economic factor is the long-term shrinkage in freight traffic. This is not a matter of less goods being produced, but of goods being moved shorter distances than formerly, due to the growing decentralization of industry over the past generation. In other words, in relation to industrial production and to national income, there has been a decline in

2. Elgen, Riley—"Rails Losing Fight Against Automobiles"—Barron's 12/11/39—p. 4
total freight movement for some years. ...For most roads, it looks like a losing long-term fight against economics and politics."

** Strikes ** The investor, conscious of increased commodity prices, might have anticipated threatening activities of labor after the NRA was ejected upon industry in 1933 with its cumulative complications and final repeal. With general information before him on the Average Wage Costs by Industries, such as frequently is published in financial literature, he might have even selected those industries to lead the "strike" menace; but, the developments of 1937 presented no parallel in American history. Legal rights of property owners were openly defied by labor and sanctioned by the Administration. In that year alone "striking workers deprived themselves and their families of more than $155 million in wages" 2, and the four preceding years averaged a toll of about $60 million. "Labor won about 26% of its 707 strikes in 1926 and made partial gain in 25% more; and things remained at about this level through 1932. But in 1933, bolstered by NRA, 37% of labor's strikes resulted in victories, and in 1936 the victories reached what is probably an all time high of 46%, another 24% of the strikes involving partial gains. If these mounting percentages are applied to the rising sum of strikes, the effect is startling." 3

"The fact that half of the 1936 strikes were fought for a principle, collective bargaining, with the trend continuing into the stormy spring and summer 1937 is of such significance that those who follow labor closely are inclined to doubt the comfortable theory that the current wave of strikes is just a normal post-depression phenomenon." 1 Through the Wagner Labor Act, labor is in a position to consolidate and even its new gains. However, if as stated in "Don't Kill the Goose" 2 'the A. F. of L. and C. I. O. combined have less than 1/5 of all the workers', the present investor will yet reserve a place for facts on the directors and managers of American industry.

War Regardless of on which side one's sympathy rested when the World War terminated in 1918, the League of Nations, following the Versailles Treaty, commanded respect. Although the fighting ceased, much bitterness and revenge remained. How much of the foreign invasions, confiscation of property, and control of industries and channels of commerce in the past decade are traceable to the terms of the treaty provoke much speculation. Japan in China, Italy in Ethiopia, Germany in Czechoslovakia each brought daily headlines to our press in their turn. Conflicting interpretations were visible in our security prices. Neither France nor Great Britain could afford a war; the greatest unifying force of the league vanished. The sanctity of treaties was confined to paper.

2. Goslin, Ryllis & Omar--"Don't Kill the Goose"--Harper & Bros. 1939
Broken promises were fertile fields for mutual distrust, but the lack of intensive battles in the various seizures kept many prospective investors on the side lines, so far as supporting war issues was concerned. Bonds were still high during the last quarter of 1938, an inflationary trend established by deficit financing existed, and the rumblings of war through the foreign clouds presented a closing picture for the investor's appreciation.

In September 1938 when Germany occupied the Sudeten area, the Dow-Jones industrial shares broke, to 129.91 from 143.08, a loss of 9.2% in less than three weeks. At the same time, the barometric London industrial share average went to 91.2 from 103.3 or a decline of 11.7%.

**Political Measures**

Tremendous individual losses and stagnation of industrial production worked cumulatively to develop a complete fear psychosis in 1932. Restoration of purchasing power was imperative. With the Roosevelt landslide as complete support, New Deal policies were magically designed and effected "to make capitalism work".

"No New Deal measure reveals more unmistakably the New Deal purpose to make capitalism work by tinkering within the system than the National Industrial Recovery Act--NRA. The object of the NRA was to enlighten the unenlightenment of the capitalists in the matter of the creation of purchasing power

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1. Nelson, H. G.--"Commonsense Speculation"--Barron's 8/14/39--p. 2
2. "The New Deal"--Fortune--February 1938--p. 150
and to enable manufacturers by combination and compulsion to raise wages, to eliminate unfair competitive methods, and stabilize price levels. The whole theory of the act was the opposite of the theory of business regulation laid down as far back as the Clayton and the Sherman Act. Practices previously forbidden as giving manufacturers unsocial advantages were now encouraged under governmental regulation. The so-called automatic controls were no longer trusted. Government itself took them over, and took over not only the capitalist problems but the capitalist themselves."

Multiple complications resulted and the NRA was ruled unconstitutional. Although officially dead, the Blue Eagle's feathers can be detected in subsequent legislation; such as the Wagner Act and the National Labor Relations Board. Government in business did not begin with the New Deal, as evidenced by "The ten departments and 87 different independent agencies" in effect during the Hoover administration; yet "it should never be forgotten" by the investor "that the President himself is by upbringing a T. R. Progressive and monopoly baiter and that his political education was an education acquired in the New York state wars against the public utilities. The broad economic structure of the New Deal was the work not so much of the President as of his more intellectualist advisers. A considerable part of business's mistrust of the New Deal olive branch is attributable to the fact that

the olive branch has been offered—whenever it was offered—by a man who held it like a club."

It is worth notice in passing that the AAA, quite as much as the NRA, was an attempt to make the capitalist system work. The outstanding agricultural phenomenon of the decade before the New Deal was the failure of falling prices to adjust production to the capacities of the market. Consequently the AAA was set up to create "artificially" the scarcity of supply relative to demand, which capitalist theory calls for. Farmers were enlightened as to their self-interest by means of bounties for acreage limitation, and cooperative action was assured by governmental supervision.

Since the investor is not so much interested in how much people have, but how they will spend it, he might well weigh the amount of business to be generated by the Rural Electrification Administration and the Electric Home and Farm Authority, which were set up to steer the power companies and the electrical appliance people into the rural market they had not developed for themselves. And the whole housing program was designed with the principal purpose of getting the building industry and its related financial institutions out of the ditch. The Home Owners Loan Corporation put props under the mortgage system and the Housing Act of 1934 insured banks, mortgage companies and the like against losses on building loans. Other significant measures of this same kind were

2. The same as #1
3. The Same as #1
the act setting up the Federal Deposit Corporation, which
gave the country's banking system a leg up to the extent of
insuring almost $48 billions of deposits; and the Emergency
Railroad Transportation Act of 1933, setting up a Coördinator
of Transportation to help the railroads eliminate unnecessary
expense and duplication of services." 2

"The Social Security Act of 1935 and the Railroad
Retirement Act of 1936 attacked the same general problem--
to increase effective purchasing power--in a different way.
Their purpose was to stabilize American society by adopting
in this country measures which had long since been adopted
in every important capitalist country of Europe." 3

"The principal exceptions to the general New Deal pol-
icy of making capitalism work from within were the acts
regulating the stock exchanges. The Securities Act of 1933--
the so-called truth in securities act--was a police measure
requiring the filing of information about securities issues.
And the Securities Exchange Act of 1934 establishing the SEC,
was a measure regulating the exchanges. They were aimed at
the better functioning of the capitalist system at its most
sensitive nerve center." 4

In summary--The mass of figures printed about each of
the governmental agencies is confusing, often alarming in
size. The investor, interested in profit must travel the

3. Same as #2--p. 160
4. Same as #2--p. 162
lane which neither overemphasizes their power to curtail industry nor fails to appreciate their effect on increased efficiency. Specialists in many fields collect maximum returns, but, in the field of investments, the average investor cannot afford to be a specialist if he is to capitalize on the human reactions to the news.
Security Analysis  From the mass of information, or rather 'material', published in the field of investments, even a disinterested party might reasonably assume that, from it, a profitable policy could be deduced. However, autobiographies of the country's wealthiest men are rare, and were the financial status of many writers published, it might truthfully acknowledge their sales ability rather than their investment formulae as their prime asset.

Adding to the following section on Investment Service records, one of the more recent investigations into the success of investment forecasting by Alfred Cowles, 3rd will serve to preface this section and emphasize the importance of being able to 'make up one's own mind' about values and prospects:

"Sixteen financial services, in making some 7500 recommendations of individual common stocks for investments during the period from January 1, 1928--July 1, 1932, compiled an average record that was worse than that of the average common stock by 1.43% annually. Statistical tests of the best available individual records failed to demonstrate that they exhibited skill and indicated that they more probably were results of chance. Twenty fire insurance companies making a similar selection of securities during the years 1928 to 1931 inclusive, achieved an average record 1.20% annually worse than that of the general run of stocks. The best of these records, since it is not very much more impressive than the record of the most successful of the sixteen
financial services, fails to exhibit definitely the existence of any skill in investment."

"William Peter Hamilton, editor of the Wall Street Journal publishing forecasts of the stock market based on the Dow Theory over a period of twenty-six years, from 1904 to 1929, inclusive, achieved a result better than what would ordinarily be regarded as a normal investment return, but poorer than the result of a continuous outright investment in representative common stocks for this period. On ninety occasions he announced changes in the outlook for the market. Forty-five were successful predictions and forty-five were unsuccessful."

"Twenty-four financial publications engaged in forecasting the stock market during the four and one-half years from January 1, 1928 to June 1, 1932 failed as a group by 4% per annum to achieve a result as good as the average of all purely random performances. A review of the various statistical tests, applied to the records for this period, of these twenty-four forecasters, indicates that the most successful records are little, if any, better than what might be expected to result from pure chance. There is some evidence, on the other hand to indicate that the least successful records are worse than what could be reasonably attributed to chance."

"It seems to be reasonably well established, at the

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1. Burtchett, Floyd F. Ph. D--"Investments and Investment Policy"--Longmans, Green and Co.--New York 1933--Footnote--P. 42
present time, that a substantial proportion of those who pose as investment counselors are quacks of one sort of another."

Therefore, deciding to work out his own salvation, the investor finds available to him among the leading dailies, THE WALL STREET JOURNAL, and the NEW YORK JOURNAL OF COMMERCE. "Both make every effort to follow all developments closely. Members of the staffs attend all public corporate meetings, as well as interview officers of all the national corporations at regular intervals. Over a long period of years, their information has been found to be unbiased and unprejudiced. In other cities there are local journals of merit, but the newspapers mentioned are national in scope and can be depended upon for accurate and complete financial information." 2

"In the field of financial magazines, the COMMERCIAL AND FINANCIAL CHRONICLE, 3 which is factual and not opinionative, BARRON'S, a weekly issued from Boston by the owners of The Wall Street Journal, and the ANNALIST, published by THE NEW YORK TIMES are the best known and recognized. Others include The FINANCIAL WORLD, COMMERCE AND FINANCE, THE BOND BUYER, and FORBES MAGAZINE—all weeklies, and THE MAGAZINE OF WALL STREET, a semi-monthly publication.

In each industry, there are trade magazines which treat in detail the developments in that industry. Magazines such

1. Burtchett, Floyd F., op. cit.—p. 42
2. Warshow, Robert Irving, op. cit.—p. 163
3. The Economist (London) is practically a counterpart of The Commercial and Financial Chronicle, but is somewhat more cosmopolitan in its viewpoint and in its contents.—Burtchett, Floyd F., op. cit.—p. 42
as THE IRON AGE, THE OIL AND GAS JOURNAL, THE RAILWAY AGE,
ENGINEERING AND MINING JOURNAL, PUBLIC UTILITIES FORTNIGHTLY,
MODERN PLASTICS, NATIONAL PETROLEUM NEWS, ELECTRICAL WORLD,
and TEXTILE WORLD supply detailed statistics and trade news of real value. For the investor or trader interested at any
time in a specific industry, the trade journal should be
read carefully."

From one's broker may be procured booklets containing
current price and investment data on listed securities, and
available for customer's use are the nationally recognized
investment services: Standard Statistics, Moody's, Fitch's,
and Poor's. "The ratings are interesting and are widely
used in the field, but the investment analyst uses them
largely as a check against his own estimate."

A long list of Government bulletins is available from
the Superintendent of Public Documents, Washington, D. C.
at nominal cost. The radical conflict between government
statistics and those collected from private sources, espe-
cially upon matters of unemployment, wages, relief, etc.
in recent years is insufficient reason for excluding them
from consideration.

Special types of Investment Letters such as the Harlan
Allen Economic Letter, the Kiplinger News Letter, Whaley
Eaton Domestic and Foreign Service "undertake to keep the
investor informed on developments in political affairs and
current economic trends as reflected in public psychology

1. Warshow, Robert Irving--op. cit., p. 163
2. Jordan, David I--op. cit., p. 362
and opinion. Of recent years, political maneuvers have been exceedingly important and knowledge of the way political sentiment is changing has proven invaluable, both to the investor and to the speculator."  

The most significant Business Bulletins by banks include: NATIONAL CITY BANK BULLETIN, CHASE ECONOMIC BULLETIN, CLEVELAND TRUST COMPANY BULLETIN, THE FEDERAL RESERVE BULLETIN. They are "extremely valuable for the data and items of comment upon money, credit and banking conditions in the country. Among foreign banks, the Bulletins of the MIDLAND BANK OF LONDON will be most useful to the American investors."  

Listed among the most active Universities Bureaus of Business Research publishing periodic letters are: University of Michigan, Harvard University, University of Illinois, University of Chicago, and the University of Minnesota.  

All investment services such as Babson's Statistical Organization, Brookmire's Economic Service, United Business Service, Alexander Hamilton Institute, Colonel Leonard P. Ayers, and others supplying to the investor and trader information and advice relegate them to the speculative realm and should be read as such.  

Supplementing these are excellent articles in the Fortune Magazine, and others in such magazines as The Review of Reviews, The World's Work, the Reader's Digest, and the financial section of the Saturday Evening Post.

1. Burtchett, Floyd F--op. cit.--p. 591  
2. Ibid--591
Bond and Stock Ratings together with Industrial, Rail, and Utility Averages temporarily conclude the sources of information available to the student of investment. From decisions, right or wrong, based upon this background will evolve a challenging, if not completely adequate, investment policy for any individual.
Investment Services Although there are many purchasers and sellers of stocks on the New York Stock Exchange, thousands must know little about business. The money which is spent for 'aid' in directing choices finally made is staggering. Practically no Investment Service charges less than $50 per year, and each publishes endless pages of "Letters of Appreciation" from its clients. United Business Service alone has over 8,000 subscribers including among them, according to a folder from them, "leading business executives, bankers, brokers, members of the NYSE, and individual investors in every state in the Union and in 28 foreign countries from Cuba to Japan". And going on, the folder adds, "More individual investors subscribe to UBS than to any other financial advisory service in the country." Many companies are on their lists as continuous subscribers for ten and fifteen years. When, within the period 1929--1938 covered by this thesis, the one United Opinion Service which "receives, analyzes, checks, and weighs--according to the accuracy in the past, other services--facts and forecasts from all reliable sources throughout the country (Alexander Hamilton, Babson, Brookmire, Colonel Ayres, Poor's, American Institute for Economic Research, Cram's, Harlan Allen, Gibson) prints no warning of the pending collapse in the early fall of 1937 and continues to advise buying many stocks at, in their opinion "well deflated levels", which within a week of the notation, are on their speedy way to half the figure named, the charge for their service is a major problem to any investor.

1. United Business Service Folder--February 1, 1938
As a subscriber to UBS for two and a half years, I have been able to check over their recommendations at random, and find in many cases, had the investor bought particular issues, he could figure on an average appreciation of between 10 and 30% in price, which would net him, after commissions and taxes which average together about 10%, a net profit of about 15%--and that with lucky selections.

It would be unfair to the Service to make any final statements upon its accuracy of prediction without tracing its individual recommendations through the whole of its career. Such would be costly--for 13 years Bulletins approximating $900--and the results once tabulated of little significance; for doubtless the personnel over that period has not been permanent; and, for the active life of the present investor, even if they remained for twenty years to "assist" him in his problems, little insurance could be assured him.

In carefully going over the correspondence from about twenty Investment Services which I have accumulated over three years, I particularly left the United Business Service until last, thinking that, since it was a United Opinion of the leading authorities, in it I would find an investment companion. We have little in common. My note of commendation goes to the Sales Manager for so subtly expanding his supporters.

For the information of those who know nothing of the company, the following facts are interesting:

The company was organized in 1920, and has for its slogan, "A Man's Judgment is No Better than His Information". At no time has it cut its prices, to my knowledge, to increase its
subscriber patronage as many others have: Investors
Research Bureau, Inc., Syracuse, N. Y. cut its price from
$45 to $25 after trying four months to get a subscription;
Wetsel Market Bureau, Inc., N. Y. City cut their proposition
from $60 to $35; and Dudley Kimball, Parsippany, N. J. from
$60 to $30.

The UBS Weekly Bulletin arrives in the mail on Monday
and includes four main sections:

1. Summary of Current Business and Investment Situation
   Favorable and Unfavorable Conditions Affecting
   Business and Investment Conditions with
definite forecasts

2. Sales and Credit Forecasts--by states and cities
   showing why prosperity will increase in
   certain sections and decrease in others

3. Commodity Price Forecasts
   Specific data on price fluctuation of
   80 basic commodities

4. Investment and Speculation Forecasts
   What to Buy, When to Buy, and When to Sell

All subscribers have the usual consultation privilege
and are always welcome to visit the 210 Newbury Street
Building in Boston.

The company admits that of all the technical market
forecasting methods available, five possess unusual merit.
The UNITED OPINION is applied with these five to arrive at
the Composite Result--Their Weekly Bulletin--which, accord-
ing to them is "far more accurate than the judgment of one
authority could possibly be." "Any one of these individuals
may be right or wrong in his deduction from the established
facts, but the majority report will undoubtedly prove to be
85% accurate in the future, as it has been in the past."

If the investor could take part in 85% of the recommendations, his results might be comparatively improved; but from the myriad of choices, his limited funds may find their way into plain streets that are not paved with gold.

Each service has a slightly different approach to the whole problem of forecasting, but after each has presented its conclusions, it takes no responsibility for your actions upon them.

From the tone of the correspondence from different services, their maturity can be felt. The fact that some are more highly advertised than others does not necessarily make them the more reliable. Working in the favor of all such publications since the World War is the increasing number of older people from which to maintain and increase their subscriptions.

Each company assures the investor that its staff is composed of experts, yet it would be difficult to find any uniformity of requirements in Finance in the Graduate Schools of Business over the country; therefore, the average man trying to make the most of his savings is confronted with a choice more serious in its repercussions than that of selecting the family doctor, dentist, lawyer, or painter.

It has been said by one service, Dudley Kimball--"The Kimball's Commentary", in explaining its virtues that 50% of the service fees of most agencies went into adver-
tising; and from the amount of mail which trails a single inquiry or request for a Bulletin, that seems probable. Considering the amount of clerical assistance necessary and the luxurious offices maintained by many, a broad circulation is compulsory for continuance. If these are fair statements, the average, intelligent investor can well wonder how expert counsel in all branches of finance can be afforded by each establishment.

Since 1904 Roger Babson has been in this field. His name is internationally known, and although not the only one correctly predicting the 1929 debacle, because of good publicity, for that he will always be remembered. It has been a powerful magnet for many to join him.

His service is one of the most expensive—$120 yearly, operating under the conservative motto—"Devoted to Protecting Capital and Increasing Income". He does not operate alone, but recognizes the results of some twenty of the most ably managed institutional funds in America and periodically compares their portfolios with his supervised list of 50 Stocks and 50 Bonds. 1

Babson's Reports are based on the fundamental law of Action and Reaction...and aim to supply you with the necessary courage and independence to say "No" at times when stock prices are high and investors are optimistic. "On the average of once every seven years American industry suffers a severe relapse, only to subsequently rebound to new peaks of achieve-

1. Booklet—undated—Babson's Reports Can Help YOU Obtain Protection of Principal, Increased Income, Profits
ment and prosperity. Thus, five times in the average business man's lifetime, farsighted investors are presented with an attractive opportunity to buy and hold sound securities of American corporations and to profit by the RISE WHICH ALWAYS FOLLOWS!" At no time is one subscribing to his service to operate under a margin agreement.

It is not surprising to find many services keying their reports to their interpretation of the Dow-Jones Theory which originally was not a 'theory' at all but simply the commonsense editorial observations of the late Charles H. Dow in the Wall Street Journal. Dow continually emphasized the point that an understanding of the stock price movements was invaluable because it afforded the most comprehensive and up to the minute gauge of what business men and investors as a whole thought of the future of business.

One of the outstanding writers in this field is Robert Rhea, author of "The Dow Theory", a text-book. It is significant to note that he never delegates the writing of his forecasts or discussions to others. His subscribers are notified if he is incapacitated or on a vacation. Since 1918 he has been confined to his bed most of the time. Not until after his book was printed in 1932 did he receive any compensation for his forecasting, but he was besieged with so many requests for his interpretation of events that he established one and accompanying it is the auditor's report of O. M. Williams covering the period of 12/31/28--3/25/38

stating, "For total transactions involving 601,612 shares, a gain of $436.19 was realized for each $100 of loss."

Dividends were not credited, but commissions and taxes were charged.

The price of the service is $40 yearly and mailings are sent out at approximately 10-day intervals. These letters are but the grammar school phase of learning Dow's theory, according to Rhea. To help others understand the theory, he has written, "The Stock Market Barometer" and makes available to students the past letters of his service from November 1928 through 1938 at $5.00.

In the subscriber's contract with some services one has the privilege of cancelling his contract at any time and is refunded the balance of his subscription price. Gaylord and Wood, publishers of The Dow Theory Barometer, limit the privilege of cancelling to two months after the order. As indicated by the name of the letter, this service considers itself of the orthodox school of Dow theorists. They believe that as soon as anyone starts to inject his own ideas into the Dow-Theory as described by Dow and Hamilton, he has a foreign policy which is warped and unreliable.

According to a letter of 12/31/38 in referring to the existence of the Dow Theory and its interpretation for forty years, "only 23% of the advance or decline was missed on the average, and this arose from requiring confirmation by both the Industrials and Rails before deciding that the Primary trend had changed and that therefore a primary reversal of
the business curve was at hand. Confirmation is valuable insurance against mistakes."

"If the Dow Theory has missed 23% of the total, how many business executives have missed 75% or even 100% of a trend...how many caught 9/7/37 on which date a major bear market signal was given?"

"Our clients sold their stocks at near-peak levels, and had their funds in cash during the severe breaks in the Fall of 1937 and the Spring of 1938. They were able to buy back their stocks at a fraction of the prices for which they sold them." 1

Since in this business of forecasting, the accuracy of prediction gains weight with the length of life of the company; any student of finance not seeing the date of establishment on correspondence might gain by finding that out. For a company such as Investment Letter, Inc. to state that its organization is the "outgrowth of a responsible group privately wishing to assist themselves and associates in investment of their own funds" leaves the prospective investor wondering why they would not accept the research of 'experts in the field' and remain in their regular positions. It happens that the head of this company is Charles J. Collins, former member of the NYSE and a "nationally recognized authority upon the Dow Theory" who has written a book "Fortune's Before You". If one found that such a business were established during a period when many brokerage firms had to liquidate because of

1. Letter--Gaylord and Wood 7/12/38
sharp reduction in trading, would it be fair to think it was operating from a 'back yard' approach to show once again the advantage of ringing its former front door bell? Or should one simply accept the fact that people change their positions to improve their own situation?

This service, as the others based on the Dow Theory, is conservative in style, has good graphs and company reports, including both investment and speculative issues. The cost is $50 yearly for weekly market letter, quarterly market leader list, earnings bulletin, and bond letter.

"That the service meets investors' needs is best indicated by the high rate at which subscriptions are renewed at expiration". (From its own publicity)

Among other services admitting the use of the Dow Theory is one which does not "expand" it as some, but "speeds it up" offering "original work.... not second-hand and questionable interpretation". Dudley Kimball is the author and has written a book "Investment Under the Dow Theory" to supplement "The Kimball's Commentary", his weekly letter at $60 a year started in March 1935. Although he admits "Just as Hamilton improved somewhat on the insight of Dow, so Rhea and Collins have improved somewhat on Hamilton's approach, particularly in adjusting the Theory to the needs of the trader as differentiated from the needs of the forecaster of business", he has designed the "Microscope Method, and Method 44" as his contribution to theirs for his subscribers. One gathers from correspondence which is swift in style, buried in detail,
and full of advertising all the books which he has written, that all methods and theories were awaiting his birth for his re-arrangement of the same.

In name only can the A. A. Signal Card and Investment Service of Anderson, Allen & Company be removed from the Dow Theory. The limiting of the Service to 100 stocks including all in the Averages is adapting the life insurance company actuary principle to the price movements and limiting risk losses from prediction. Its cost is $50 yearly, and for Institutional Investors' Service the range is $1,200--$1,500.

The publicity accompanying T. E. Rassieur, Trend Interpretation Service, attributes success to the Mathematical Computation of Trends. It "does not duplicate or overlap that of any other organization or system...truly unique." It was inaugurated in 1932 and Mr. Rassieur has "checked his formula back to 1922, to make certain that it would give reliable results under all types of market conditions". "My method of forecasting must naturally be and remain a secret formula. If I divulge my method, no laws protect me against losing my sole 'stock in trade'." The yearly cost is $50, and his book is "Trend Interpretation". Dun & Bradstreet is given as a reference and their reference would be interesting to secure.

This, together with the fact that their advertising copy is accepted by such leading magazines, newspapers, and other conservative publications such as: The Analyst, Forbes Magazine, Magazine of Wall Street, New York Times, Chicago Tribune, St. Louis Globe-Democrat, is presented to assure prospective
subscribers of their security under his advisement. His style is much too exclusive, inclusive; at time, belligerant and defiant to be convincing.

Another service——Stock Trend Service, Inc. relies upon Factor X for its accuracy. "This factor was discovered several years ago after all other recognized theories of stock market forecasting dismally failed to prevent the loss of millions of dollars of investor's money from 1929 through the great bear market. We felt that there must be a flaw in their technique and we set out to discover it, but resolved never to divulge to anyone this information until we had put it to every known test against every kind of market condition for 74 years—or back to 1861. During this period Factor X established an enviable record for accuracy."

This background plus the recognition of some virtue in the Dow Theory and "fundamental, statistical, technical, and planetary cycle studies" result in their Advanced Cycle Theory at $24 a year for two weekly bulletins, or $50 for Personal Service. Their book, "Ten Years Ahead" (to 1948). The gaudiness of their stationery, the volume of their correspondence, the cheapness of their supplies, and their partial reliance on the sun spots would defer the subscription of many from their service.

In the $100 a year class, among those reviewed, are (1) Statistical Reporting Corporation which furnishes the S/D (Supply-Demand) Reports—a complete service for traders and investors. The rated economic positions and price expec-
tancies for 269 stocks are represented every week. The ser-
vice separately serves the Long and Medium Term investors as
well as the Intermediate and Swing Traders. It is the purpose
of S/D Reports to furnish all data essential for Investors and
Traders to supervise their own accounts. Associated with
the Organization is an Investment Management Company if de-
sired by a client.

Emphasis is placed upon the use of the latest report.
A careful explanation is given of the terms and symbols used
in their presentation of the facts, but to those who prefer
the story of the companies told in charts, this service is
deficient.

(2) Investographics, Inc. is the most complete Graphic
service covering information on 250 companies and costs $100
per year. An intelligent use of their service should quickly
cover the cost of the subscription.

(3) Investment and Business Forecast of the Magazine of
Wall Street. The Forecast has a record of 20 years success-
ful service, 1917--1937. In regard to the capital needed to
use their service effectively they report:

$1,200 can readily follow the Trading Advices or
Bargain Indicator on a ten share basis on
approximately a 60% margin, while $600 is
sufficient for our Unusual Opportunities.

$3,000 should suffice for all three active departments.
The full amount is not needed in the beginning
but eventually it may be necessary.

In regard to its Personal Consultation Privileges, it states

1. Investographics, Inc., 31 Gibbs Street, Rochester, N. Y.
in its publicity: "This service cannot be obtained elsewhere. It has taken thirty years to build up and train our staff of business and investment experts and has cost several million dollars. Only our large subscription list makes cooperation like this possible."

(4) Poor's Complete Stock Supervisory Service is $125 yearly, but one can subscribe to their Industry and Investment Surveys at $65 a year. The keystone of the Poor's plan of security selection is the "industry approach method", which rests upon the well-known principle of business success that even a weak company can make money in a flourishing industry, while a stronger company in a depressed industry may be unable to rise above the handicaps imposed upon it by outside influences. It is therefore of primary importance to know the position of the industry in which you have invested or contemplate investing. They conduct continuous research in 62 industry groups with correlated studies of 1689 leading stocks.

The fact that the Poor's Publishing Company has existed since 1860 adds prestige to their reports among many, and their publicity accordingly carries very little boasting about its predictions.

The Index of Gain Power designed in 1931 applied to the Tillman Short-Swing Principle resulted in the Tillman Survey Service. This company was inaugurated in 1923 and charges $80 yearly for its service. "It is, of course, unfortunate that other services cannot use this formula, but
it is the product of our own laboratories and can be used only by us", they remind us in their booklet "Four Famous Forecasting Factors" in 1935.

Two services which are primarily teachers and market technicians are the Seamans-Blake, Inc. and H. M. Gartley Review.

Seamans-Blake, Inc. admits the use of the Dow Theory, but publishes with each number of its weekly Survey an Article--"Avoiding the Pitfalls of the Dow Theory". It is the publisher of the popular book "Seven Pillars of Stock Market Success" and "60 Rules for the Trader". Its publicity says that "every Seventh Reader has joined our big family---there must be a reason for this amazing progress." The tuition for the course, "Stock Market Trading", is $125.

In a booklet, "Profits in the Stock Market", H. M. Gartley says, "The Stock Market is a Competitive Enterprise. Its behavior is not a symbol of mystery but a symbol of Skill; of Knowledge. It is not owned and operated by despots, but it obeys the simple laws of Supply and Demand, and it yields its supply to those who bid the highest price for it. There is no way to out-guess, out-fool, or out-wit it. There is a way to analyze it. Not through the Trap Door of Chance, but through the Front Door of Knowledge. Remember, it is the weakness in the many that makes leadership for the few. And it is the weakness in the many that should make profits for you." "Profits flow to the man who knows HOW because he has taken the pains to learn."
The price of the Gartley Weekly Stock Market Review is $25 a year, and together with the New Gartley Course of Stock Market Instruction, $39.50.

The only study that has been made on Forecasts which in any way resembles what I had hoped to find for the period covered by this thesis is one covering the eleven year period since the World War done by Garfield V. Cox, Professor of Business Economics in the School of Commerce and Administration of the University of Chicago called, "An Appraisal of American Business Forecasts".

His conclusions are based upon a detailed study rendering to each prediction scores for accuracy and definiteness of statement. The judgments of the author were compared with eleven graduate students at the University of Chicago who applied the same test to the same quotations for the ten years, November 1918—October 1928. Excerpts are as follows:

The services as a whole show no secular improvement in either definiteness or correctness.  

"The results do support the expectation that the services will be right considerably oftener than they will be wrong, and that, in the long run, dependence upon the advice of one or more of them would prove much better than dependence upon luck."  

The adequacy of forecast reflected the service's anticipation of the direction taken by the index, correctness in forecasting the amplitude of the movement, and its accuracy

2. Ibid--p. 28
in predicting the time at which the advance or decline began.  

The services do a better job of predicting the upturns. In predicting major turning points—in regard to Babson—"its record is seriously weakened by the fact that for seven turns out of eight, it falls in the 'slightly helpful' class rather than in the 'definitely helpful' one."  

The Harvard business curve which failed to indicate the recession in 1923--24 was disposed of for some time to minimize the significance of the run which had occurred.  

These forecasters bear witness only to the belief that a specialist in the study of business fluctuations will, over a term of years, prove a more successful forecaster than a novice.  

The Barometer Letters of Babson's are typically brief and given over to conclusions much more than to reasons therefor.  

The theory which seems to be most influential in shaping the character of Moody's forecasting analyses is that the course taken by business activity is determined by business men's anticipations of profits....accords with the views of a number of the most eminent students of business cycles. The service has never explained its analytic technique in a manner sufficiently definite to render adequate appraisal possible.  

1. Ibid—p. 34  
2. Ibid—p. 42  
3. Ibid—p. 44  
4. Ibid—p. 59  
5. Ibid—p. 65  
6. Ibid—p. 67
Conclusions: Methods of analysis are changed from time to time, and sometimes even the underlying theories. And, what may be even more important, changes occur in forecast-ing personnel. Warning of trouble ahead, if given, is likely to be more delicately phrased than is an assurance of con-tinued or increasing prosperity. 1

By neither of the tests applied in this study is there evidence that the services in general are improving in the adequacy of their forecasts. 2

A recurrent mistake of certain services has been the expectation of too great or too prompt effects from conditions of credit supply. 3

"The writer does not mean, however, to minimize the accomplishments of the services. We should not forget that as a group they are found to have been definitely more right than wrong in every year but one. That they have shown no trend toward improvement does not mean that their work is valueless, nor does it establish that their efforts may not yet bear fruit in better forecasts than they have thus far been able to make. A decade is a short time in which to test the development of so complicated an art as business forecasting and the test itself makes no claim to precision. Let those who can do better than the services." 4

1. Ibid--p. 72
2. Ibid--p. 73
3. Ibid--p. 73
4. Ibid--p. 75
Charts Since no financial page can be read without seeing something about the "averages", the amateur must try to understand them. No better source of information is available for their history and action through 1929 than "The Stock Market Barometer" by William P. Hamilton, and supplementing this, "The Dow Theory" by Robert Rhea which is an explanation of its development and an attempt to define its usefulness as an aid in speculation by excerpts from editorials from January 29, 1906 through December 10, 1929.

The Dow-Jones Averages are made up of 30 essentially speculative industrials, 20 rails, and 10 utilities. Just as a barometer "predicts bad weather, without a present cloud in the sky", so have the "averages" over their career forecast changes in the primary trends in the stock market action.

The price movements reflect the sum total interpretation by the populace of facts that are known and those yet unrevealed. They are in constant motion--acting, reacting, and interacting upon each other. Their study reveals three distinct trends; primary or long term, secondary, and the daily fluctuations.

The Dow Theory with its rules about full confirmation of the industrials and the rails, lines, extent of reactions, double tops and double bottoms is nowhere presented as infallible, but useful through its understanding. It neutralizes bias, prejudice, and warped judgement.

"The man who means to hold his own in an encounter re-

2. Ibid--p. 180
stock, and the state and federal tax upon the dividends, a wiser selection may be made in an issue with greater appreciation prospects based upon inherent growth factors—as daily evidenced in the chemicals.

Since in the Adjustable Stock Ratings, a supplement to the Magazine of Wall Street, strong and weak companies often get the same rating in various periods of their cycle, the investor may profit by applying the common rules of buying in periods of depression and exercising patience in following his decision. Innumerable instances can be found of wise selection of industry, and company within it, but bad timing either of the purchase or sale of the security. Charts justify their existence by clarifying such positions.

Perhaps the most constant variable before the investor is competition as seen in the bid and asked prices of the securities themselves, between industries within a group, and between materials within the industries from modern research laboratories.

To benefit from anticipated changes in any of these denominators, the investor must be on constant guard of his securities and limit the number of industries he must follow; for the neglect of the news commands the highest price in the investment market.

"The people who keep on sawing wood in all kinds of weather are the ones who have the biggest woodpile at the end of the season." ¹

¹. Wall Street Journal—1/18/1940—Candid Comment
New Industries

New inventions and potential new industries which might develop therefrom are of such importance to the nation that an elaborate survey of the subject was undertaken by the National Resources Committee. This was the first major attempt to show the kinds of new inventions which may affect living and working conditions in America in the next 10 to 25 years. Listed as "A few very important inventions that may soon be widely used with resultant social influences of significance are: the mechanical cotton picker, air-conditioning equipment, plastics, the photo-electric cell, artificial cotton and woolen-like fibres made from cellulose, synthetic rubber, prefabricated houses, television, facsimile transmission, the automobile trailer, gasoline produced from coal, steep-flight aircraft planes, and tray agriculture.

"According to the Commission of Patents, more inventions are being made in the field of construction (particularly prefabricated buildings) than in any other. Other fields in which invention is active are plastics, artificial silks, permanent waving and manicuring, clothing and machines for making clothing, automobile bodies and automobile servicing, wooden and paper receptacles, photography, petroleum and printing.

Chemistry is broadening its position in the construction field by creating with plastics additional products for the building supply trades. The application of plastics, along a wide industrial front, is perhaps the most important

1. Technological Trends and National Policy--June 1937
Superintendent of Documents, Washington, D. C. $1.00
commercial development in recent chemical history. As identified under two classifications by the United States Bureau of the Census, the value of plastics manufactured in 1937 exceeded $125,000,000. This figure represents scarcely ten years' growth for the industry.

In the manufacture of paint and varnish, plastics are included to impart higher gloss, quicker drying, better water resistance and longer durability. As solids, plastics offer unlimited uses from thin, transparent and colorless sheets for safety glass to thick, opaque and colorful shapes for door knobs.

One-seventh the weight of brass, one-sixth of steel, one-fifth of cast iron and one-half of aluminum, plastics compete in many markets with these metals and serve in others to their exclusion. For instance, laminated canvas has given motorists the 'silent shift' of timing gears which eliminate the clash of metal parts, and outlast metal gears. In addition, bearings, pulleys, springs and washers and other heavy duty parts for automobiles, airplanes, railroad cars and ships, as well as for oil refinery, steel, paper, textile and other mill equipment, are made of laminated materials. Approximately 70% of laminated plastics use paper.

Substantial economies result from the use of plastics. A survey by the U. S. Tariff Commission indicates that laminated fabric bearings in rolling mills reduce power consumption as much as 40% to 60%. Since water is a good lubricant for plastics, such savings are important in paper mills and ships where moisture is prevalent.
Since price is an important point in the choice of materials to fill any of our needs, plastics must undergo this test in the competition for business. A number of essential resin materials are the by-products of certain manufacturing processes. For instance, phenol (carbolic acid) is the chief derivative of coal tar, and glycerin is from soap. Therefore in gauging the market for these chemicals, it is necessary to study the conditions surrounding the main products.

A wide range of materials have been subjected to intensive investigation as resin sources: casein, soybeans, oat hulls, petroleum, and soft pine and lignin being most important.

The paint and drying oil industries were among the first to feel the impact of the plastics. The experience of the automobile producers is the best illustration of the point. Under the old system of finishing, cars required extensive treatment with many coats of paint and varnish that were slow

I. Taken from: U. S. Bureau of Agricultural Economics--The Fats and Oils Situation April 14, 1938--Statistics of Miscellaneous Crops 1939--#34

The five year average production 1929--1933 was 14 million bu. 1938 alone produced 63 million bushels

The United States is now the third largest producing nation. Factory consumption for "Drying" (include paints and varnishes linoleum and oilcloth, and printing ink) increased from in 1931--8,901,000 lbs. to 17,157,000 lbs. in 1937. A marked increase in the use of soybean oil in shortenings and oleomargarine has developed since 1934, while the drying industries maintain a steady percentage.
in drying and quick in dulling. Since painting took weeks, manufacturers were forced to invest heavily in assembled cars which remained at the factories awaiting surface finish. However, the introduction of lacquer, based on cellulose, caused a sharp reduction in painting time. Accordingly, century-old ideas of paint materials and methods were altered completely. The advent of synthetic resins marked a further change. With this group of materials, there were developed a new series of better oil paints for certain uses. Drying time is reduced to hours and durability is extended to years. Other industries, such as linoleum, printing ink, and patent leather have found advantages in resin coating products.¹

In brief, plastics have converted paint manufacture into an advanced chemical process. Since paint finds its largest outlet in building, it follows that construction provides a major market for plastics.

1. U. S. Tariff Commission
   Production of Alkyd Resins from Phthalic
   and Maleic Anhydride

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¹ Taken from—"Synthetic Resins Revolutionized Paint and Varnish Industry"—The Wall Street Journal 1/31/40—
John Munroe Weiss
Basing their designs on the diversity of uses of resins, architects and decorators have had free play for their ingenuity. Thus, plastic materials are molded, cast or laminated for utility and decorative purposes. For example, the new annex of the Congressional Library contains 450 miles of laminated shelves to hold 10,000,000 volumes.

Bathrooms and kitchens are lined with wall tiles and equipped with soap dishes, sink tops, hamper tops, towel bars and toilet seats of plastics. Since resins can give any desired effect, plastics are used for wall and door paneling and for store fronts, lobbies and halls of hotels, theaters, public and private buildings.

The electric field is another important outlet. Since plastics possess excellent insulating and heat resisting properties, it was natural for electric manufacturers to adopt these materials early. Producers of electrical equipment are applying plastics for parts for radios, for switches, and switch plates, sockets, plugs, wire connections, vacuum cleaners and other appliances. Previously, the production of telephone apparatus required large quantities of resins such as rubber, shellac, and asphalt--natural resins. Now, these materials are displaced by synthetic resins which have the advantages of better resistance to breakage, corrosion, and perspiration. The highly colorful telephone handsets are the product of plastic manufacture.

Due to the combination of light weight, strength, and beauty, plastics have been adapted for building hardware, furniture and furnishings. For example, plastic table and counter
tops are not affected by burning cigarettes, alcohol and acids. Restaurants and bars, therefore, find plastics unusually advantageous in saving depreciation and maintenance charges. They are also formed into modernistic radio cabinets and furniture.

One of the most important markets for plastics is in lighting fixtures. It has been found that plastic shades and reflectors transmit and diffuse light to an exceptional degree. Since they are light in weight and unbreakable, plastics are strong competitors for lighting glassware. The extent of this field is indicated in the value of such glass manufactured in 1937 at $22,000,000. Incidentally, as compared with fabrics plastic lampshades are not subject to easy tearing.

As adhesives and binders, resins have improved profoundly the outlook of several industries. Builders, for instance, have known for a long time that plywood has many advantages. In manufacturing plywood a sheet of tissue paper saturated with a synthetic resin is inserted between the plies as a convenient means of applying the resin glue. By combining the grains of alternate veneers at right angles, the wood becomes stronger and yet easily workable. However, previously available adhesives principally starch, hide, fish, casein and blood glues, deteriorated shortly after application due to moisture and mold. Therefore, plywood was restricted to limited interior uses. Other difficulties with wood are swelling and fire hazard.

Plastics have solved these problems. As a result, the
use of plywood, for both exterior and interior structural purposes, has increased so that millions of square feet are produced monthly. The binding power of resins is put to further use in the production of linoleum mastic tile and other floorings and coverings. For instance, one company, engaged in the manufacture of steel prefabricated homes, is using a mixture of cork and plastics for floors. Of particular interest is the use of agricultural wastes, such as lignin and other fibrous materials, for wallboard roofing, and siding bonded with resins.

As stated in Barron's of June 12, 1939, 'Lignin forms about 25% of the weight of wood. The 3,000,000,000 pounds annually sewered away by all paper mills are regarded as the only known source whence parapropylphenol might be obtained cheaply, and paper mills face legislation which will forbid the discharge of lignin-bearing waste water into streams'.

Although a comparatively young industry, definite trends are manifest in plastics. 'DuPont, the largest chemical company in the country, now derives 40% of its total sales from twelve new lines brought to fruition in the last ten years. Making these new products required the employment of 7,000 more workers and the price of the new things was reduced on an average of 40% during the decade. The largest dollar sales come from rayon, next is organic chemicals, third is fabric and finishes, and fourth is cellophane—all of which have made their major growth since 1929.'

1. Henick, Bernard--"Plastics Industry Hits Its Stride"--
Barron's--6/12/39
cians who worked out the production of cellophane could hardly have imagined that it would virtually wrap up America.

Union Carbide and Carbon Corporation is identified with two of the most promising resins perfected. One of these, vinyl resin, represents a vast improvement for safety glass in resisting breakage at low temperatures. Others in the field: Allied Chemical & Dye Corporation, Commercial Solvents, American Cyanamid Co., Pittsburgh Plate Glass Company, General Electric Company, Westinghouse Electric & Manufacturing Company, and in the miscellaneous group--Quaker Oats Company, Eastman Kodak Co., Goodyear and Firestone Tire and Rubber Companies."

"The great American oil industry, fourth ranking in the country with over $2,000,000,000 invested in its far flung refineries is in the midst of its second major change in basic refining methods.

It is a change that conceivably might be more far-reaching in its effect than any even in the industry since the real use of gasoline as a motor fuel was first realized. The first major change in refining came when the old method of distilling gasoline was supplanted by the cracking processes which used terrific heat and enormous pressures to smash up the petroleum into its component parts.

Now the industry is hurriedly preparing to change itself into what will be virtually a synthetic, organic chemical industry. The remarkable new processes that will accomplish

1. Self, Sydney B--"Dynamic Research Brings to Light Potentialities of the Chemical Age--Wall Street Journal--2/19/40
this, all use what are called "catalysts", a sort of chemical wand, to shuffle and reshuffle the petroleum molecules around much more effectively, and incidentally without the sledge hammer technique of the heat and high pressure cracking processes.

To the petroleum industry this means very much larger production of gasolines with higher octane (efficiency) ratings. It means better balance in production between profitable gasoline and relatively unprofitable fuel oils. It will also mean many millions spent on new refineries."

"The first of the new catalytic chemical processes to be translated into new plant construction and substantial production is the now famous Houdry Process.

Ten years ago a Frenchman named Eugene Houdry came to this country looking for capital to develop a new oil refining process, using a catalyst which he had been nursing along in France for some years. He finally interested the Vacuum Oil Company, later merged into Socony-Vacuum, which put up some money and a little later the Pew family of Philadelphia, which controlled Sun Oil with $2,000,000 or $3,000,000. Five or six years were spent on research which culminated when Sun's first unit went into production in 1937."  

Standard Oil of New Jersey has bought patents from

1. Self, Sydney B--"Research Creates New and Improved Products for Petroleum Refiners"--Wall Street Journal--2/26/40
2. Self, Sydney B--"Super Motors and Planes in Prospect as result of Oil Industry Research"--Wall Street Journal--2/29/40
German interests for synthetic Buna rubber based on petroleum products. In the past few years the cost of synthetic rubber has been cut approximately in half. It is especially well adapted to tire treads because of its long wearing qualities and because of its resistance to deterioration by contact with oil and gasoline. The synthetic rubber is already used considerably for special purposes, such as gasoline tubing and tank car lining. dupont's Neoprene, and Goodrich's Koroseal are both used for these purposes.

Since rubber tire manufacture accounts for 70% of America's consumption of crude rubber, use of the synthetic product in treads alone would cause a tremendous demand for Buna and other artificial rubbers.1

"Dow Chemical has developed a plastic, vinlylidene chloride, particularly promising because of its high tensile strength and for its quality of flowing cold under pressure like a metal forging. The automobile industry may find wide use for it in large-scale molding."2

"Automobiles with a plastic body may become a reality. Briggs Manufacturing Company will make for Chrysler to exhibit at the New York World's Fair, a steelplast body which has greater tensile strength than steel, although it will contain wood fiber. Such a body weighs about one-half as much as a conventional steel body and also costs less and

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1. Barron's -- February 19, 1940
2. Duncan, L. C.--"Progress of Dollars that Multiply"--Barron's--7/3/39--3
forms a self-supporting unit. In addition, the top of the body is transparent."  

"That Ford Motor Company is considering using more plastic parts in automobiles was revealed in a talk of an official before the American Society of Tool Engineers in Detroit recently, when he said that adoption of plastic engine hoods and doors is being held up because a suitable chemical dye to match the painted metal body hasn't been found."  

"Eastman Kodak's rayon and plastics subsidiary, Tennessee Eastman Corporation, Kingsport, Tennessee has been selling its Tenite plastic for auto dash boards and now it is claimed to be the first plastic used in making gunstocks."

"Sanforizing" is hailed as the most important development in the textile industry since the discovery of fast dyes. Cluett, Peabody owns the Sanforizing process for preshrinking cottons, and the amount of such goods which is being Sanfor- ized is growing by leaps and bounds, with large benefits to the company's royalty income. The process has a patent protection for at least ten years. The machinery costs $25,000 a piece. The income of major source is from the continuous royalty from the use of the Sanforizers. The minimum annual royalty per user is $5,000. The total yardage of fabrics processed in recent years has been as follows:

---

1. Barron's--July 31, 1939--p. 5
2. Barron's--July 24, 1939--On the Business Horizon
The business received a big impetus from a ruling issued by the Federal Trade Commission on June 30, 1938. It said that Sanforizing is the only process discovered up to the present, which can control shrinkage to a uniform and dependable residual shrinkage figure—less than 1%. The name "Sanforizing" has important advertising advantages which it would take a competitor considerable time to overcome.

The process is also applied to Rayon which is used in over 50% of all apparel, and has since its inception been confronted not only with the problem of shrinkage but stretching as well.¹

duPont's success in developing an entirely non-vegetable fibre—NYLON, of greater strength and elasticity than silk, has spurred other companies in their research for artificial fiber. VINYLON, generically different from nylon, but also having silk-like qualities is made by Union Carbide from lime, coal, and salt. It has almost the same elasticity and resistance to attack by acid and bacteria.²

According to the chief chemist at Pacific Mills, Lawrence, Mass., the trend in textiles is definitely away from wool, silk, and linen. The second revolutionary introduction represents changes in manufacturing processes. And finally there is to be an increased use of new synthetic resins as finishing material, with an increased emphasis on style.

The Bureau of Dairy Industry in the Department of Agriculture has been granted public service patents for a process of making casein fiber said to be somewhat different from the process for making 'lanital', the Italian synthetic wool. National Dairy Products is conducting its own experiments to develop casein fiber from milk which contains about 3% casein and in composition resembles the crystallized albumen of the white of an egg.

Another candidate for the artificial wool field is derived from the amazingly versatile soybean. Its meal protein has been used to form the basis of a new wool-like fiber, said to be moth-resistant and possessing 80% the tensile strength of wool. Encouraged by Ford Motor Co. which has long wanted to use upholstery fabric from soybean as well as plastic parts, Glidden Company has been developing this type of fiber in its laboratories.1

From the Census of Manufacturers 1937 covering Buttons and Synthetic-Resin and Other Plastic Products are interesting figures on the growth and value of buttons from synthetic resins:

<table>
<thead>
<tr>
<th></th>
<th>1937</th>
<th>1935</th>
<th>1931</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross</td>
<td>9,407,563</td>
<td>9,074,489</td>
<td>4,835,730</td>
</tr>
<tr>
<td>Value</td>
<td>$4,341,742</td>
<td>$3,241,738</td>
<td>$623,637</td>
</tr>
</tbody>
</table>

From Cellulose Compounds

<table>
<thead>
<tr>
<th></th>
<th>1937</th>
<th>1935</th>
<th>1931</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross</td>
<td>327,427</td>
<td>724,875</td>
<td>496,785</td>
</tr>
<tr>
<td>Value</td>
<td>$716,557</td>
<td>$1,579,709</td>
<td>$1,207,716</td>
</tr>
</tbody>
</table>

These figures include data for buttons of horn and hoof composition and of compounds other than cellulose.

1. Barron's--November 13, 1939--P. 5
One of the leading plastic button manufacturers is Catalin Corporation. "The high cost of dies is an important factor in plastics a die for a button, for instance costs as much as $200; and the larger dies are much more expensive. High volume is needed to reduce unit cost of plastics products." 1

This company has been rated from B1 to A3 by the Magazine of Wall Street since 1933, and its earnings have been:

<table>
<thead>
<tr>
<th>Year</th>
<th>Earnings</th>
</tr>
</thead>
<tbody>
<tr>
<td>1933</td>
<td>18¢</td>
</tr>
<tr>
<td>1934</td>
<td>48¢</td>
</tr>
<tr>
<td>1935</td>
<td>47¢</td>
</tr>
<tr>
<td>1936</td>
<td>52¢</td>
</tr>
<tr>
<td>1937</td>
<td>17¢</td>
</tr>
<tr>
<td>1938</td>
<td>07¢</td>
</tr>
<tr>
<td>1939</td>
<td>31¢</td>
</tr>
</tbody>
</table>

Whether or not this company remains independent, or is to be absorbed by some larger chemical company such as Fiberloid and Resinox have been by Monsanto since 1936, and Bakelite by Union Carbide will be interesting for the investor to follow.

It was during the early career of the magazine, Life, that much publicity appeared about the new fast drying ink. In some way, ink instead of being liquid, resembles coal in form and by the heat of the presses, the ink is dried immediately by evaporation. Interchemical Corporation is interested in this new development.

Other novelties in the printing field include the use of perfume with ink for advertisements on cosmetics. The perfume is mixed with a green-tint ink with one part perfume used for three parts ink.

By the cultivation of southern pine, and the use of the same in the production of newsprint, some paper companies are becoming less dependent on the paper business alone and...
are developing waste products in such a way as to make them competitors of chemical companies. The significance of this development is that while it is still small in dollar volume, it may add much needed stability to paper company earnings. Such by-products as plastics, chemicals for tanning and for the manufacture of inks, beverages, soaps, medicines, and textiles are being produced.

The new technological developments mentioned reduce manufacturing costs or improve the product. These new uses have been instrumental in creating a larger market for the consumption of paper, estimated at 250 pounds more than 1929 per capita. An example of a new application is that of paper bags. Multi-wall bags made from kraft paper are now used as containers for rosin and asphalt which are poured in while hot.

The use of the paper milk bottle has been increasing steadily, in spite of the fact that in many communities its use has been opposed by ordinances favoring the glass bottle. Paper has had expanding uses in other branches of the food field at the expense of the tin can and the glass jar. This is particularly true with the growing use of frozen foods, which are almost exclusively wrapped and boxed in paper.1

Eastman Kodak Co. looking for a way to pack films in vacuum cases finds a superior way of making vitamins for General Foods to use in flour and cattle feed. So—interrelation of all research and consequently of all industry becomes closer and closer and only a mental tight rope artist

can keep track. 1

The results of all these and many more are of deepest concern to the executive and the investor. They mean cheaper and better goods, and incidentally the opportunity for bigger profits. But it also means cross competition from a hundred sources, most of them unexpected. It means more rapid changes in industry than ever before. The chemical industry is going to compete with nearly every other industry, and nearly all industries are apparently on the road to competing with each other and with the chemical industry.

Out of this maelstrom will come big profits for the alert and ruin for the lethargic. Unexpected sources of income will come to apparently water-logged industries and profitable monopolies will be spoiled.

The little company will sometimes have as good a chance as the big one, because, contrary to general belief, there is no complete monopoly on brains, and patents these days often mean only the basis for law suits. 2

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1. Wall Street Journal--February 19, 1940
2. Self, Sydney B--"New Horizons for Industry"--Wall Street Journal--2/19/40
Before leaving the Plastics Field, these figures should be presented as a tribute to their growth:

PLASTIC TRADE STATISTICS
Statistics compiled by the United States Tariff Commission on the production and sales value of plastic products during 1934, are presented in table 1 to indicate the relative cost and industrial importance of various types of organic plastics.

<table>
<thead>
<tr>
<th>Product</th>
<th>Total Production</th>
<th>Sales</th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Derived from phenol</td>
<td>24,800,000</td>
<td>5,233,000</td>
<td>.23</td>
<td>1934</td>
<td></td>
</tr>
<tr>
<td>Cast Products derived from phenol</td>
<td>4,986,000</td>
<td>2,099,000</td>
<td>.44</td>
<td>1934</td>
<td></td>
</tr>
<tr>
<td>Derived from cresol and/or phenol</td>
<td>10,887,000</td>
<td>1,705,000</td>
<td>.21</td>
<td>1934</td>
<td></td>
</tr>
<tr>
<td>Derived from Phthalic anhydride</td>
<td>14,877,000</td>
<td>1,022,000</td>
<td>.14</td>
<td>1934</td>
<td></td>
</tr>
<tr>
<td>Derived from maleic acid, styrol or xylene</td>
<td>177,000</td>
<td>67,000</td>
<td>.36</td>
<td>1934</td>
<td></td>
</tr>
<tr>
<td>Derived from urea or thiourea</td>
<td>3,471,000</td>
<td>1,291,000</td>
<td>.41</td>
<td>1934</td>
<td></td>
</tr>
<tr>
<td>Miscellaneous resins of non-coal-tar origin (vinyl, petroleum, etc.)</td>
<td>442,000</td>
<td>225,000</td>
<td>.51</td>
<td>1934</td>
<td></td>
</tr>
<tr>
<td>Cellulose nitrate</td>
<td>12,934,569</td>
<td>7,799,283</td>
<td>.77</td>
<td>1933</td>
<td></td>
</tr>
<tr>
<td>Cellulose acetate</td>
<td>4,826,347</td>
<td>4,633,054</td>
<td>(a)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Casein (imports only; domestic figures not available)</td>
<td>13,264</td>
<td>4,981</td>
<td>.38</td>
<td>1933</td>
<td></td>
</tr>
</tbody>
</table>

(a) Approximately 10% higher than cellulose nitrate

From the same source, the following figures are available on urea resins in production pounds only:

<table>
<thead>
<tr>
<th>Year</th>
<th>Quantity</th>
</tr>
</thead>
<tbody>
<tr>
<td>1933</td>
<td>3,234,000</td>
</tr>
<tr>
<td>1934</td>
<td>3,471,000</td>
</tr>
<tr>
<td>1935</td>
<td>4,203,000</td>
</tr>
<tr>
<td>1936</td>
<td>5,500,000*</td>
</tr>
<tr>
<td>1937</td>
<td>7,000,000*</td>
</tr>
<tr>
<td>1938</td>
<td>8,000,000*</td>
</tr>
</tbody>
</table>

*Estimated

2. Weiss, Joseph--"Urea Assumes More Important Place in Fertilizer, Resin Fields"--Wall Street Journal--2/7/40
From the Census of Manufactures: 1937--Page 10

PRODUCTS, BY KIND AND VALUE: 1937 and 1935

(No comparable statistics are available for 1933)

1. "Synthetic-Resin, Cellulose-Plastic, Vulcanized-Fiber, and Molded and Pressed Pulp Fabricated Articles, not Elsewhere Classified", industry, all products, total val. $77,715,723 $40,298,937

2. Fabricated articles of synthetic resin, nitrocellulose, cellulose acetate, transparent cellulose sheeting, vulcanized fiber, and wood pulp........... 73,037,371 46,966,309

3. Other products not classified in this industry 4,678,352 3,332,628

4. Fabricated articles of synthetic resins, etc., made as secondary products in other industries.... 12,779,555 7,996,143

5. Fabricated articles of synthetic resins, etc., total value (sum of 2 and 4).................. 85,816,926 54,962,457

Synthetic-resins (phenolic urea vinyl, acrylate, etc.):

Laminated products--

Sheets, plates, blocks, rods, tubes, and blanks.. $12,588,713 $4,767,616

Gears, bearings, mach. pts. 2,765,009

Electric goods 1,233,863

Other and not specified 4,251,736

Molded or Cast

Electrical goods 8,791,667 29,216,141

Closures 4,228,460

Housings (for cameras, scales, radios, etc.) 1,235,769

Cigarette cases, compacts 764,075

Other and not specified 15,100,769

Battery boxes (principally asphalt composition)

Cellulose compounds (nitrocellulose, cellulose acetate, etc), housings for radios, etc.) cigarette cases, vanity cases, etc. 13,765,286 8,534,474

Vulcanized fiber--

Rods, tubes, and other unfinished forms 2,948,657 4,718,844

Hollow ware (boxes, cans, pails, etc.) 2,044,259 1,044,749

Laminated sheets and plates 4,767,728 2,389,313

Other and not specified 1,913,776

Molded pulp products (dishes, egg-case liners, etc.) 4,765,341 4,291,320

Fiber conduits and fittings 1,710,905
From the Census of Manufactures 1937 are the figures showing the increase in dollar value of Diesel engines from 1933 to 1937. They are taken from Table 4 on Page 3 in part:

Production, by Class, Type, Number, Rated Horsepower Capacity, and Value, for the United States: 1937 and 1933

Internal—combustion engines, total value $131,650,929 $29,623,763

(Subdivisions show)

- Diesel (surface-ignition)
  - Compression-ignition (Diesel) Marine
  - For Electric Drive and Auxiliary use
  - Other Diesel
- Stationary
  - Other (tractor, bus, heavy truck, aircraft, rwy diesel-elec)
  - Surface-ignition (hot-spot, hot-bulb, etc.)

By far the largest single producer of Diesel Horse Power is Caterpillar Tractor, though primarily a farm machinery company. For trucks—Hercules Motors, Waukesha Motors; others in the spotlight are Ingersoll Rand, Fairbanks Morse, Imperial Diesel Engine Co., International Harvester, and General Motors. Through its subsidiary, Electro-motive Corporation, General Motors leads the field in railroad diesel engines, and through its other subsidiary, Yellow Truck and Coach makes auto engines. Second in the railroad field is American Locomotive; Baldwin also makes switching Diesels, and Cooper-Bessemer makes railroad engines.

I. Cook, R. P. —"Diesel Spotlight Turns to Trucks"—Barron's—6/27/38—11
**Facsimile transmission** is an invention which holds great promise in the field of communication. In facsimile, printed matter and pictures are sent from one point to another point by radio or wire. Facsimile differs from television in that the former's aim is to have the transmitted material made into a permanent record. Recent developments make possible "home newspapers" in rural homes, or enable a military bomber with its portable radio-facsimile equipment to send drawings to enemy lines back to headquarters.

As a laboratory trick, facsimile has been in existence for fifty years. In recent years, facsimile circuits have been set up by American Telephone and Telegraph and Western Union, so that the public can send by wire such material as blueprints, advertising layouts or pictures. News services have established wire-photo systems for sending pictures to newspapers.

Radio is particularly suited to carrying high-speed facsimile pulses. There are fewer obstacles to putting radio-facsimile on a commercial basis than television. Equipment is much cheaper, the range is about the same as that of radio and there is plenty of room in the radio spectrum, particularly in the high frequencies, for facsimile stations.

Probably the most outstanding inventor in radio-facsimile is William G. Finch, former engineer of the Federal Communications Commission. He has made important discoveries for low-cost facsimile communication, and now is the head of Finch Telecommunications, Inc. New York City.
Finch Telecommunications has licensed about thirty facsimile stations to use its equipment in the United States and Cuba. Those in the U. S. operate on an experimental basis.

Market for home receivers, however, will probably be restricted until commercial licenses are granted by the FCC. For that reason the company is concentrating on other types of facsimile equipment. One is the light mobile transmitting and receiving unit for police autos, ships and military airplanes. It is capable of sending and receiving at the rate of 150 words a minute (as well as pictures). It costs $35 per unit in quantity amounts.

Using this unit, police headquarters could contact roving police cars, sending them not only instruction but also pictures of suspects. A battleship can transmit diagrams to ships beyond the horizon, informing them of future maneuvers.

Cost of news-gathering is a problem confronting the radio stations who would like to inaugurate commercial service. It has been suggested that they might lease the receiving sets and split the fees with the news agencies. 1

Although the Securities Exchange Commission has not yet passed on the merits of any securities registered with it from Finch Telecommunications, Inc., a complete story of their organization and the mechanics of facsimile transmission in their prospectus is available to any investor in the field.

2. Finch Telecommunications, Inc.--Distributors Group, Inc. 63 Wall Street, NYC.
In the past five years $13 million dollars has been spent on television, and until it is worked out to be profitable, it will still be unemployed commercially.

Everything about it is expensive. The range is limited to about forty miles and the pictures, although fifty times improved from those introduced in 1931, are limited in size. Supplementary stations must be used to telecast images a longer distance. Television needs a wide channel in the ultra high frequency band—6,000 kilocycles wide. This means that "each television signal takes up about six times as much space in the air as the entire broadcast band, or as much as 600 ordinary broadcasting stations." International Business Machine's radio typewriter uses less than 1 kilocycle. The 24–90 megacycle band, upon which television would operate is now used by the Army, Navy, and Departments of Agriculture.

Radio waves on the ultra high frequency do not travel so far around the earth as longer waves and have the unpleasant habit of bouncing off buildings and interfering with each other.

The problems of getting talent and costumes with continuity of program and a network broadcast limit its early use; therefore there is yet a market for the higher priced console radio sets. The patents are held by Radio Corporation of America, Philco, and Farnsworth Television & Radio Corporation. The public may expect to get its first sets from

2. "Television II—Fade In, Camera One!"—Fortune—April 1939
RCA, but the per share earnings for some time would be negligible. 1

"No one knows yet what a television program is, let alone pay for it. No one even knows what a television actor is or ought to be. No one knows what kind of programs the people will like, or whether in fact they will like any programs well enough to buy sets. It is perfectly evident to everyone in the industry that advertisers will not buy television time until the public buy sets; and since at present writing, there are only a handful of sets in the entire U. S., it is clear that the public has a long way to go. How far it will go, on the other hand, depends upon how well it can be amused. So, in the end, and probably for a considerable time to come, the broadcasting companies are left holding the bag, in the sense that they must invest millions of dollars in television programs, in order to make the public want sets, in order to make the advertisers put up the money." 2

"It will cost three to four times as much as regular broadcast programs as pictures are much more expense to produce than words. The final answer lies with the American public. But the country's drive toward scientific advancement and a high standard of living is so strong and so wide that it is impossible to conceive, either emotionally or historically, that television can be neglected or left undeveloped. The technical means and economic machinery by which tele-

1. Television--Financial World--2/24/37--15
2. Television II--Fade In, Camera One!--Fortune--4/39--72
sion will grow are still unclear, but it would be a rash prophet who dared to say that the televised life of the Jones family can never be achieved." 1

1. Television II--Fade In, Camera One!--Fortune--4/39--164, 5
Conclusions

The writer at this point somewhat resembles the alarm clock—about run down, but
sure that a turn in the right direction will produce the de-
sired results tomorrow. Hobbies often develop into stable
earners, and it was from that aspect that this overall study
covering the Problems of the Investor 1929--1938 was made.
Future commitments will reflect better judgment, if not rela-
tive returns, when altered by the correlations established.

American industry catapulted from hilarious heights to
sober depths, was handed miscellaneous potions by unprece-
dented authority with staggering repercussions. Periods of
affluence are saturated with extravagance and disintegrate,
crumble and fall from their own accrued superficiality. This
fact has no boundaries.

Education is a slow process. Production alone creates
wealth. Speculative plantings of the 20's flourished for
the merciless reaper. Consuming greed supplanted moral obli-
gation. Mob psychology postponed reason; while the gambler's
rule—"Never give a sucker a chance"—operated overtime.
Profit prospects minimized tight money conditions; property
not already mortgaged was bought on the installment plan; pro-
tective publicity was unknown.

The credit bubble burst; paper profits vanished; failures
and foreclosures multiplied. The dizzy decline found no base
until June 1932. Fear gripped the country. Capitalism and
competition had failed, according to the multitudes. Any
change was welcome. The promises in the Election Campaign
were magnetic; victory for the Democratic Party was confirmed
in the November landslide for Franklin D. Roosevelt.
and no change is made in the capitalization of the company, the earnings increase the assets, and the representation of each common share in them is likewise increased and justify a rise in price.

If intense activity materializes upon the breaking of some headline news event, the long position stockholder is unaffected, and if his issues are wisely selected, the fundamentals governing his decision doubtless remain and soon exhibit themselves again on a stronger technical base.

The margin trader in this situation, however, is on dangerous ground unless he has a sizeable reserve to cover his debt. As emphasized in the body of this thesis, margin trading should be confined to those who can afford to lose.

Heavy trading means spotlight performance. The understanding and intelligent use of charts and the Dow Theory are the investor's best guardians of risk. Through them he sees the news before he hears it; and can take advantage of stop-loss orders to protect his profits or limit his losses.

It is often said that those in industry are so close to its problems that they often fail to be a profitable owner of its stock in prosperous periods and from a phase of loyalty keep it when the industry is in trouble. Therefore, the outsider may have a clearer perspective of relative values.

All training in accounting and economics together with the full acknowledgment of the power of research and adver-
tising in developing and maintaining any industry are fundamental to investment analysis. A logical approach must have a retrospective background. This thesis has given that to the writer. Developed along with this is a filing system based upon the different industry groupings with both cards and folders by which to catalogue current happenings.

Fortunately we have no charts successfully forecasting our future. Therein lies its challenge and fascination. For pleasure, for education, for excitement, and appreciation the writer finds this her engrossing hobby--THE FUTURE OF AMERICAN INDUSTRY.

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