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THE influence of the rapid growth of investment trusts in popularizing stock market activities has aroused some degree of apprehension. Paul M. Warburg, international banking expert, in reproaching the Federal Reserve System for failing to take drastic measures against the "Stock Exchange debauch," ascribes to these trusts a part in what he regards as a threat of general trade depression.

Mr. Warburg refers to the Standard Statistics Company's index of stock prices, that records for fifty industrials, twenty public utility stocks and twenty railway stocks a growth in market value, during two years, from approximately $17,500,000,000 to $33,000,000,000. Here is a gain of about $15,500,000,000 which, Mr. Warburg says, in a majority of cases is "quite unrelated to respective increases in plant, property or earning power." Yet this stupendous growth in "value," he adds, covers only ninety stocks, excluding bank stocks, real estate values, and "some of the subtlest elements of inflation — incorporated stock pools, called 'investment trusts.'"

Other authorities regard the investment trusts less harshly. For instance, Albert Ottinger, Attorney General of New York State, after an exhaustive investigation of the activities and forms of investment trusts, concludes:

"They have a very real and substantial place in our financial structure. In the main they afford an opportunity for the investor to make a reasonably safe investment based upon broad diversity of securities. . . . Nor do I wish to present the conclusion that there have been evils in the management of investment trusts which require State regulation."

If Mr. Ottinger proceeds to recommend certain measures for the regulation of these bodies, it is only to prevent the abuse of a plan of investment organization which he regards as perfectly sound.

A SURVEY of the investment trust field, made in 1927 by Leland Rex Robinson, revealed 172 American and Canadian investment trusts and companies, all but thirteen of which were in the United States. Mr. Robinson estimated that there were 119 investment trusts of the general management type. This is significant, because general management trusts follow closely the lines of their British progenitors in allowing their managers considerable discretionary power in making and shifting investments. In this respect they differ sharply from the fixed or limited type, which confine their dealings to certain groups, such as public utilities, bank and stocks, bonds, or common stocks of a few industries. The general management type is not limited to any one class of securities. Mr. John F. Fowler estimates that there were 199 investment trusts in existence at the end of June 1928, with capital investments totaling $1,200,000,000. The number today is estimated to be about 300 with investments well above $1,500,000,000.

Is their influence in popularizing stock investment a good influence? Has it boomed the inflation of the market? Has it encouraged "speculation"? Trusts of the general management type are constantly buying and selling securities. They are regarded jealously and criticized with caustic tongue by the old investment houses which sell "sound" securities — mostly "gilt edge bonds." It would be natural that such houses should think these trusts risky.

The business of the investment trusts is perfectly legitimate and helps to fill a long-felt want. Nevertheless, although the principles of diversification and investment management, upon which investment trusts of the discretionary or management type operate, are sound, it must clearly be understood that not all investment trusts are sound, either in their organization or management. The investor must not assume that, because the principles are sound, any investment trust is as good as the best.

In truth, investment trusts are just the opposite of dangerous. They represent not only expert knowledge, such as that to which the older investment houses can lay claim, but two other safeguards — diversification and incessantly vigilant management. The old idea of "salting away" securities "for good" in strong boxes is being supplanted by that of a perpetual and rapid turnover.

One result is the substitution of independent expert judgment for the second-hand, inexpert judgment of the lay speculator. In the old days the public was like a flock of sheep. How easily it was led by a single bellwether is shown by the stock market of 1904, when Thomas W. Lawson published scarehead advertisements in the newspapers advising that the public sell certain securities.

Lawson's readers did not independently reckon the risks they were encountering. If they had made their mistakes independently, some in one direction and some in the other, some with one set of stocks and some with others, the results might not have been so bad upon the general market, because they might have counteracted each other. Instead, they all ran like sheep the same way. It was a mob of easily-led investors, all seeking for "straight tips," which might bring them instant wealth. All made their mistake in common. Then all tried *en masse* to escape. It was like a sudden panic rush of all the passengers on a ferryboat to one side, making the boat list and even capsize.

Where speculation is ignorant and imitative, it is dangerous alike to those who engage in it and to the public. Where, on the other hand, speculation is based on the independent knowledge of many well-informed groups of investors, furnished with sound statistical facts, its utility can be very great.

The investment trust principle acts to reduce risks by utilizing the special knowledge of expert investment counsel, and by diversifying investments among many kinds of common and preferred stocks and bonds, foreign and domestic.

It also operates to shift risks from those who lack investment knowledge to those who possess it. As a consequence normally speculative properties gravitate into the hands of these skilled agencies which are better able to forecast their true future value. Many investment trusts of the general type have built up their own investing organizations, depending neither on the facilities of banks nor of investment banking houses sponsoring them. Others have fiscal agencies that exist solely for the purpose of investment trust administration. Such an agency supervises a widely distributed list of holdings by means of a skilled staff. All figures bearing on the investments held are kept up to date. This followed the precedent of investment trusts both in the United States and in Europe.

Can such trained organizations be engaged in inflating stock prices? Or, do they stabilize rather than inflate? And, is the stock market so greatly inflated, after all?

One important fact is that the tradition that common stocks are risky has been modified. A single stock is risky when a dozen are not. Diversification acts as insurance to reduce risk. This means that investment trusts, buying over a wide range of stocks, can afford to pay higher prices than individuals, buying stocks simply, could afford to pay.

We have had seven years of prosperity. Since August, 1921, the Standard Statistics index of common stocks listed on the New York Stock Exchange has risen 260 per cent. Never before has there been so long and so rapid a rise in stock prices. Never, either, has there been so rapid a development in national resources, in improved technology. A relatively stable level of general prices has been maintained. This has prevented overbuying of supplies. Transportation has improved. With no expectation of strongly rising prices of commodities, excessive inventories have been kept down. Inventories on hand have not been forced or frightened into liquidation. There has been scientific study of the sources of their supplies by manufacturers and merchants, with constant statistical check upon volumes produced. Pronounced improvements in machinery and in production methods have lowered costs, reducing prices and increasing profits. So society as a whole has benefited in real income. Both business men and wage-earners have taken advantage of the relatively stable price level to budget their expenditures, making commitments undisturbed by violent fluctuations in the purchasing power of money. That is, they have been much more sure of making both ends meet.

Finally, abundant bank credits have not resulted in inflation of the general level of commodity prices. But with the post-war expansion of world trade and the resumption by most nations of the gold standard or the gold exchange standard, the need of economizing gold as a basis of credit is being emphasized.

THE gold exchange standard itself, in the opinion of so good an authority as Dr. E. W. Kemmerer, will continue to develop as in the past, with a measure of economy of gold in foreign balances. The system of doing business with checks is being expanded in countries other than English-speaking countries. Checks used in place of bank notes economize gold still further. Business is turning over faster. It is piling up reserves. It needs less credit based on gold, and repays its loans more quickly. In his book, *The American Omen*, Garet Garrett tells of an automobile factory with equipment, personnel, product, and market for 2,000 motor cars daily, all created within seven months after breaking ground — a feat which a few years ago would have required eight to ten times as long. The money to finance the extension is speedily paid back from income, and the gold underlying the necessary loans is released for other purposes.

The technique of production has been and is being revolutionized. It was the warring nations that first organized scientific research on a grand scale and set the new pace. Their manpower was absorbed at the front. New and improved automatic machinery took the place at home of the fighting men sent to the front. The result was enormous increase in American plant production.

Technical men, men of science, were transferred from the universities to the research and planning departments of the large industrial concerns. Herbert Hoover became the engineering type of man in scientific control of industry. Human engineering stepped in to aid mechanical and electrical engineering in bringing about a genuine coöperation of labor and capital in the public interest. Wages became liberal. The mightily augmented purchasing power of the public created new consumer markets. Prohibition came. The average worker, no longer an absentee on "blue Mondays," and more steadily providing for his family, became a good "risk" for instalment sales.

THUS the years of post-war recovery, especially after the deflation of 1921, have witnessed the largest increments of real income of any like period in our industrial history. Production has augmented, real wages have increased, great mergers have reflected the opportunities of mass production in the rich American market. Absolute free trade between forty-eight sovereign states has helped. According to the National Bureau of Economic Research, American income was nearly sixty-three billion dollars in 1921. It rose to ninety billions in 1926 and is probably considerably more for 1929. The average income of those gainfully employed would buy more than one-third more goods in 1928 than in 1921.

Such considerations force themselves on any proper appraisal of the long "bull" market. The higher commodity price level, as compared with 1913, should account for about 40 per cent increase in stock values. Much of the remaining increase represents solid values added by more efficient labor, higher per capita production, cheaper and better processes, and the reduction of risk involved through diversified holding by investment trusts.

There remains a margin of genuine stock inflation representing the tendency of shoals of investors, big and little, to follow "market tips," blindly and without any warrant. How large this true inflation is, cannot be definitely estimated. My guess is that it is about ten per cent.

But the influence of investment trusts and investment counsel is largely toward cutting the speculative fluctuations at top and bottom, thus acting as a force to stabilize the market. Investment trusts buy when there is real anticipation of a rise, due to underlying causes and sell when there is real anticipation of a fall. In such a situation as the stock market has just passed through, the stabilizing influence of the investment trusts is beneficial. They discourage the booming of unsound stocks and support the market for sound stocks, thus diminishing the losses arising from both inflation and deflation of stock prices.

Anything which does not manipulate the market but anticipates it, stabilizes it and is advantageous. For the interests of all concerned, the more nearly a stock is selling at its true value the better. The more knowledge there is in the market, the more promptly a stock will reach its true value.

The investment trusts are cognizant, for example, of the fact that Duco paint, when evolved and marketed, tremendously speeded up production. Gains in time resulted in economy of capital. Virtually every line of manufacture witnesses, daily, technical developments of importance. These result in a greater total of products, with less expenditure of human effort. Altogether it means reduced costs, greater net profits to producers, lower prices to consumers. Many corps of specialists employed by the investment trusts are watching out for these signs. They know about improved and cheapened processes beforehand, and discount them in their purchase of stocks and bonds. By their influence, the steeper declines or ascents are drawn out into milder ones.

In this beneficial sense the investment trusts of the general management order may be said to "speculate." They buy securities, they look for profits in appreciation of stock prices. They buy at prices less than the true worth of the securities purchased, taking advantage of their superior knowledge of industrial and trading conditions. They are alert, outstripping the mass of investors, and they profit by a constant change in investments.

All modern production is called speculative-capitalistic production. It is managed by "captains of industry." These are men specially fitted at once to forecast and to mold the future, within the realms in which they operate. The industries of transportation and manufactures, particularly, are under the lead of an educated and trained speculative class. Their function is to assume for themselves the main risks, with the ordinary investor, who is not so equipped, coöperating as a mere lender or "silent partner." Yet some of these industrial captains may prove incompetent, or may betray the confidence reposed in them. They may throw the burden of risks on those whom they pretend to shield. The analysts, statisticians, and counsel of investment trusts guard against such betrayals of confidence, or imcompetence, by their constant scrutiny of the conduct of corporations.

It has been held that it is no business of an investment trust to "sell short," that is, to contract to deliver securities of which it has no actual ownership. Many American investment trusts have adopted the rules of the British companies to exclude "short selling," and have adopted resolutions forbidding such practices.

No doubt an investment trust practises soundly when it avoids extensive contingent liabilities. But the violent opposition to short selling is largely the result of ignorance. Normally it is not only legitimate, but beneficial.

INDEED, civilization lives and grows by selling futures. If you sell land you are selling future crops. In other instances you are selling future services. We are always selling the future. Selling short in the stock exchange or produce exchange is a special form of this principle. Those who believe that prices will fall will sell from their present holdings, or may sell short, agreeing to supply such holdings at a later time at a fixed price.

You cannot build a house without someone "selling short." A building contractor who had taken a large contract was asked whether he was not taking big risks, as he could not know in advance the costs of building. He replied, "No, I am taking no risks at all except on 'labor'; I have made contracts to be supplied with all materials when needed, at fixed prices."

THOSE who undertook these contracts thus assumed the risk of future fluctuation in price in the special materials in which they dealt, relieving the contractor of the necessity of informing himself of the special market conditions for stone, brick, timber, and so on, and enabling him to make a closer bid for the contract, inasmuch as there was less need to allow for unknown contingencies. Most of those materials contracted for did not exist when the contract was made. The stone was unquarried, the brick unbaked, the lumber unfelled. The public, of course, gets the benefit of such a shifting of risk into expert hands, in the form of reduced building costs. Similar results follow from most other "short" sales.

Far from acting as a force that multiplies risks in the market, the American investment trusts today are steadily reverting to the British type, which is credited with having strengthened the pre-war position of London as the money centre of the world. They invest their funds in many securities, foreign and domestic, so that the law of averages may balance losses with gains. They limit their investment in any one security. They supervise the investment funds continuously. They select securities with care to get a favorable average interest and dividend yield; in this process, diversification helps raise the yield higher than would be possible with the relatively small capital of an individual investor. As the result of their extra skill, they look for investment profits and the continuous accumulation of earned reserves and surplus built up out of net income. Such companies favor legal regulation.

There is public advantage in granting to State authorities power to refuse a charter to dishonest or improper incorporators of an investment trust. This is recommended in the report of the Ottinger investigation. Further, there should be the requirement that a minimum be paid in capital in cash. There should be publicity, frequent reports and examinations. Thus the investor can assure himself of the ability and integrity of the management.

The investment trust has come to stay in America. It is already comparable in strength here with its congener in Great Britain, which has had fifty years to grow instead of six, as here. It is bound to wield a profound influence in the security market, and thus upon trade and industry. Rightly regulated, so as not to impair the financial discretion of its directors, I am persuaded that the net influence of the American investment trust will be good.

INSTALMENT SALES UNAFFECTED IN LULL
New York Times (1923-Current file); Mar 18, 1928;
ProQuest Historical Newspapers: The New York Times (1851-2007)
pg. 45

INSTALMENT SALES UNAFFECTED IN LULL

Credit Executive Sees Volume This Year Up to Last, With Gain Likely.

OVERDUES ARE LOWER

May Be Traced to Higher Standards, but Spread of the Business Is Great Safety Factor.

The lull in business during the last few months has caused no repudiation of instalment contracts by consumers nor has it played a part as yet in diminishing the volume of instalment business, according to H. B. Lewis, Vice President of the Commercial Credit Company. He said yesterday that instalment sales generally were holding their own and even expanding in some lines in which special efforts were being put forth.

"As I view the outlook for instalment selling this year, the total volume will probably approximate that of 1927, which was a fairly good year," Mr. Lewis continued. "Some of the leading companies discounting instalment paper, I believe, will show increases of up to 10 or 15 per cent.

"The unemployment situation, if it is as serious as it is reported, has had very little, if any, direct reflection on instalment sales. If it were to have a serious retarding effect either on volume or repudiations this would become apparent at once in instalment sales of motor cars. All the reports I have been getting, however, indicate that this year the percentage of instalment to cash sales of motor cars is increasing.

Contrast to Last Year.

"This is somewhat in contrast to the development last year when the ratio of instalment to cash sales of cars showed a decline. I can give no special reason to account for this, excepting that consumer tendencies in this respect seem to move in psychological cycles--many people at one time having the inclination to pay cash and at another to make use of the instalment method. Incidentally, motor car manufacturers look for this year to show notable gains in sales.

"Taking all our outstanding paper, we find that overdues are appreciably less than last year. While this may be due in part to the high standards we are maintaining for this paper which has had the effect of preventing the dealers from offering paper which they have reason to believe may not be accepted, it is my guess that a similar situation with respect to overdues is also true of the other leading credit companies.

"It appears to me unthinkable that any ordinary recession can affect the instalment business. The safeguards being taken to protect the accounts are effective and, not only these, but the tremendous geographical spread of the business are great strengthening factors.

"Instalment selling now covers this country and Canada, and depression, considering the present financial organization available to limit the effects of panics, is not likely to cover the entire country at once. There may of course be 'black spots' here and there that must needs be taken into account, but these, according to past experience, will not show up seriously when taken in relation to conditions as a whole.

Got Through 1920 Storm.

"Instalment selling weathered the depressed conditions of 1920-21 most satisfactorily and those conditions were worse than any we are likely to meet in the near future. It may be objected that the volume of instalment sales is now much greater than it was then, but it is questionable whether their volume shows a greater relative gain than the general increase in business.

"Any added risk is offset by the higher credit standards which prevail today and the better organization of collection services. Added to these are the ability of most consumers to take care of their contracts, the marked gains made in saving bank deposits and life insurance coverage indicating the possession of funds to meet their contingencies.

"Recently the finance companies satisfactorily faced the conditions in the mining sections of Pennsylvania, where intense unemployment prevailed. I know of no concern that succumbed to these conditions. They nursed their accounts along and gradually collected the great majority of them.

"In the total volume of instalment sales, those of motor cars rank first and finance practice in this field has now become so standardized and terms have been so well worked out and followed by most companies that there is little to fear in this direction.

"Should a mild depression occur and unemployment grow greater, this mightshow up in smaller sales, but not in the 'backing up' on the finance companies of much of their paper. The people who are likely to be most affected by unemployment are those usually interested in the purchase of used cars, of which the smaller percentage is sold on time and these with higher down payments and generally shorter terms of sale."

Rugged Individualism Speech, Herbert Hoover, 1928

This speech was delivered in New York City by Republican presidential candidate Herbert Hoover on October 22, 1928, toward the close of the election campaign. In this classic example of American conservative philosophy, Hoover condemned the Democratic platform as a misguided attempt to solve the problems of prohibition, farm relief, and electrical power through state socialism; he extolled free, private enterprise and initiative, a system of "rugged individualism," as the foundations of America's "unparalleled greatness." Government entry into commercial business, he argued, would destroy political equality, increase corruption, stifle initiative, undermine the development of leadership, extinguish opportunity, and "dry up the spirit of liberty and progress."

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Excerpts

It is false liberalism that interprets itself into the Government operation of business. The bureaucratization of our country would poison the very roots of liberalism that is free speech, free assembly, free press, political equality and equality of opportunity. It is the road, not to more liberty, but to less liberty. Liberalism should be found not striving to spread bureaucracy, but striving to set bounds to it. True liberalism seeks freedom first in the confident belief that without freedom the pursuit of all other blessings and benefits is vain. That belief is the foundation of all American progress, political as well as economic.

Liberalism is a force truly of the spirit, a force proceeding from the deep realization that economic freedom cannot be sacrificed if political freedom is to be preserved. Even if governmental conduct of business could give us more efficiency instead of giving us decreased efficiency, the fundamental objection to it would remain unaltered and unabated. It would destroy political equality. It would cramp and cripple mental and spiritual energies of our people. It would dry up the spirit of liberty and progress. It would extinguish equality of opportunity, and for these reasons fundamentally and primarily it must be resisted. For a hundred and fifty years liberalism has found its true spirit in the American system, not in the European systems.

I do not wish to be misunderstood in this statement. I am defining a general policy! It does not mean that our government is to part with one iota of its national resources without complete protection to the public interest. I have already stated that where the government is engaged in public works for purposes of flood control, of navigation, of irrigation, of scientific research or national defense that, or in pioneering a new art, it will at times necessarily produce power or commodities as a by-product. But they must be by-products, not the major purpose.

Nor do I wish to be misinterpreted as believing that the United States is free-for-all and the devil-take-the-hindmost. The very essence of equality of opportunity is that there shall be no domination by any group or trust or combination in this republic, whether it be business or political. It demands economic justice as well as political and social justice. It is no system to laissez faire.

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In the last fifty years we have discovered that mass production will produce articles for us at half the cost that obtained previously. We have seen the resultant growth of large units of production and distribution. This is big business. Business must be bigger for our tools are bigger, our country is bigger. We build a single dynamo of a hundred thousand horsepower. Even fifteen years ago that would have been a big business all by itself. Yet today advance in production requires that we set ten of these units together.

Our great problem is to make certain that while we maintain the fullest use of the large units of business yet that they shall be held subordinate to the public interest. The American people from bitter experience have a rightful fear that these great units might be used to dominate our industrial life and by illegal and unethical practices destroy equality of opportunity. Years ago the Republican Administration established the principle that such evils could be corrected by regulation. It developed methods by which abuses could be prevented and yet the full value of economic advance retained for the public. It insisted that when great public utilities were clothed with the security of part monopoly, whether it be railways, power plants, telephones or what not, then there must be the fullest and most complete control of rates, services, and finances by governmental agencies. These businesses must be conducted with glass pockets. In the development of our great production industry, the Republican Party insisted upon the enactment of a law that not only would maintain competition but would destroy conspiracies to dominate and limit the equality of opportunity amongst our people.

One of the great problems of government is to determine to what extent the Government itself shall interfere with commerce and industry and how much it shall leave to individual exertion. It is just as important that business keep out of government as that government keep out of business. No system is perfect. We have had abuses in the conduct of business that every good citizen resents. But I insist that the results show our system better than any other and retains the essentials of freedom.

As a result of our distinctly American system our country has become the land of opportunity to those born without inheritance not merely because of the wealth of its resources and industry but because of this freedom of initiative and enterprise. Russia has natural resources equal to ours. Her people are equally industrious but she has not had the blessings of 150 years of our form of government and of our social system. The wisdom of our forefathers in their conception that progress must be the sum of the progress of free individuals has been reenforced by all of the great leaders of the country since that day. Jackson, Lincoln, Cleveland, McKinley, Roosevelt, Wilson, and Coolidge have stood unalterably for these principles. By adherence to the principles of decentralization, self-government, ordered liberty, and opportunity and freedom to the individual our American experiment has yielded a degree of well-being unparalleled in all the world. It has come nearer to the abolition of poverty, to the abolition of fear of want that humanity has ever reached before. Progress of the past seven years is the proof of it. It furnishes an answer to those who would ask us to abandon the system by which this has been accomplished.

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