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**News
Release**

Past Successes, Future Challenges

**Remarks of
Richard C. Breeden, Chairman
U.S. Securities and Exchange Commission**

**Securities Industry Association
Boca Raton, Florida**

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PAST SUCCESSES, FUTURE CHALLENGES

REMARKS OF

RICHARD C. BREEDEN, CHAIRMAN
U.S. SECURITIES AND EXCHANGE COMMISSION

SECURITIES INDUSTRY ASSOCIATION
BOCA RATON, FLORIDA

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Ladies and Gentlemen:

This is my third opportunity to address you as Chairman of the U.S. Securities and Exchange Commission, and I want to thank you for your invitation today. Though someone should check to see whether the speakers committee needs a new list of prospects, I am honored to have a chance to be with you again.

Two years ago we were all reacting to the sudden plunge of the market in October of 1989, when the Dow lost 191 points. For markets and investors that had only really begun to shake off the effects of the even larger trauma of Black Monday in October 1987, the "crashette" of 1989 was a troubling reminder that market volatility remained potent and unrestrained.

Last year, we were coming to the end of the worst year in a generation in the operating results of the industry. Though the capital base was strong, brokerage volume was at very low levels, underwriting activity was sharply reduced and profits had turned to losses for a great many firms.

This year is a very different story, and it is worth taking just a moment to reflect on the changes that we have seen. As you know, recent public commentary on the state of the economy has ranged from dismal to gloomy. Meanwhile, the securities markets in 1991 have produced a volume of financing unprecedented in our history. Across the board, from debt to preferred to common stock, from established issuers to initial public offerings, we have seen a vast increase in the amount of financing. By the end of the year we expect that total financing, public and private, will have exceeded \$650 billion, which is an increase of more than \$200 billion over 1990.

One of the most positive developments during the year has been the strength and depth of demand for equity securities. The total of all issuances of equity securities is headed for roughly \$80 billion, nearly double the total of \$44 billion in 1990. Public offerings have grown even more than the total issuances, with equity underwritings rising from under \$25 billion last year to more than \$60 billion this year. Happily, the IPO market has also surged back this year, with last year's \$4.6 billion leaping to around \$14 billion for 1991.

This vast torrent of financing demonstrates the strength and vitality of the U.S. securities market, which remains the largest and most dynamic market in all the world. It serves the needs of

more than 50 million investors and 12,000 public corporations seeking the capital to finance operations, research and development, and growth for the future. This volume of capital for the economy has also been raised without any federal deposit insurance, without any public subsidies and without asking the federal taxpayers to become contingently liable for anyone's mistakes.

That the volume of financing has not translated into more vigorous economic growth at this stage is perhaps a reflection of many factors. Certainly among them is the fact that these funds are not all going to finance new activities, but rather in many cases are being used to repair corporate balance sheets that had become all too weak during the "debt binge" of the last half of the 1980s. However, though there is much more to do in that area, the fact that we have set in motion the healing process is itself a good sign for the future strength and resilience of businesses all across America.

Of course, the aggregate return to investors of 19% on the S&P 500, and the more than 20% return on equity of the securities industry, compared with a loss in 1990, are certainly worth mentioning in any review of the year. However, in my personal view, the most positive of all the elements in the capital markets picture for 1991 was the fact that, for the first time since 1983,

this year we will have had a "net issuance" of equity securities in an amount of roughly \$35 billion.

The destruction of the equity base of America's public corporations that occurred from 1984 to 1990 was considerable. During that time there was a net retirement of more than \$550 billion in equity. In only seven years, one half trillion dollars of equity was converted into debt. In the process, we lost a half trillion worth of shock absorbing capacity for the economy. To understand the scope of this conversion it may help to note that the net loss in equity was equal to more than 40% of all the equity value accumulated in the history of our country through 1980.

Was the return to a net issuance of equity capital an isolated event, or will it be the beginning of a sustained trend? Of course I would violate our own rules if I made a projection on that question. However, I hope that this year marks the turning of the tide, and the commencement of a long term shift in the capital raising mix of American corporations. Indeed, it needs to be a sustained trend, because it will take almost 15 more years at the current pace to replace the equity that was retired during the 1980s.

In saying that I do not mean to imply that there is anything wrong with issuing debt securities. Indeed, some debt securities such as "high yield" securities share many characteristics of

equities. However, the 1990s as a whole are likely to be a decade of increasing need for investment at home to enhance productivity, and for investment internationally on an unprecedented scale. A strong base of equity capital allows companies to think and plan and build for the long term, and to absorb downturns when they periodically occur.

One reason for the relative unattractiveness of issuing or holding equity securities is that the United States at present has among the most punitive systems of taxation of equity securities of any developed country. Though the issue of the capital gains tax is a contentious one, it is an inescapable fact that this country will need abundant amounts of equity capital to finance our future economic needs. At present, our tax structure penalizes the most heavily the very part of the capitalization spectrum that is the most important for promoting future economic growth. If the world today can find ways to stand down nuclear missiles, surely we in America can be as creative as our competitors in Japan, Germany, France, Britain and elsewhere. Surely we in America can find a way to stand down the tax penalties on investment -- real, long term equity investment for our country's economic future.

While the tax issue is important, there is more to promoting a surge of new investment for our economic future than taxes. Here I believe that the securities industry can play an important role in the "Re-Equitizing" of America. You have the intellectual

talent to design the most complex capital market instruments in the world. You have been instrumental in developing a whole new spectrum of asset backed securities that, among other things, allow the homeowner in search of a mortgage to benefit from the secondary markets for capital from all over the world. You have invested huge sums in the technology and know-how to support trading in far higher volumes and complexity than ever known before.

These talents ought to permit you to seek out ways to broaden the availability of capital to small and medium size businesses for which the traditional underwriting process is too costly or simply heretofore unavailable. These firms are now dependent for financing on a banking system with serious problems, yet these same firms produce a large quantity of our jobs, technology and products.

Obviously the penny stock scams that we have worked hard to eradicate demonstrate that there are significant potential risks to investors from the securities of small companies. Even where fraud is not an element, illiquidity itself represents a serious risk to investors as we have seen in the limited partnership and other areas.

Though there are obstacles, your industry has the talent to help find ways of serving the capital needs of this sector of the economy more effectively, and at lower cost, than occurs today.

As part of the process, the Commission should be willing to revisit our own rules under the Securities Act and the Investment Company Act to streamline the process by which smaller companies can tap the market without abandoning protections against fraud. Without elaborating all the details, expansion of the ability to make simplified offerings under Regulation A, expansion of the use of simplified forms such as S-18, simplification of filings under the Exchange Act and broader use of the business development companies provisions of the Investment Company Act could all help to lower costs and improve access to capital for smaller companies.

Education is another tool for making the 1990s the Decade of Equity. Long term returns for investors in equity have been consistently superior, yet many Americans may have come to believe that investing in stocks is somehow akin to gambling and is not an option available to them. Here the SIA has made a commendable contribution through your educational efforts, but both as an industry and as individual firms more can be done. We have the world's finest securities markets, and they are studied in countries in every corner of the globe today. How many American high schools study those markets, and seek to impart to their students with an appreciation of the fundamentals of our market system? We shouldn't keep Adam Smith locked up until our kids are enrolled in college.

Hopefully, the 1990s can be the decade for Re-Equitizing the American economy. At the same time, I believe that it will also be a decade of continued internationalization of markets. In only the last two years, the gross purchases and sales of foreign securities by U.S. investors have risen by one-third. Hundreds of mutual funds are now available solely for investment in foreign securities. Clearly investing in foreign markets involves special risks, and we must work to make sure that this process of internationalization of investing and trading is carried out within a framework of strong international cooperation to prevent fraud and to minimize risks to market stability through the clearance system or otherwise.

In response to this trend, the SEC has signed ten foreign agreements to promote enforcement cooperation as well as market development and stability during the past two years. These agreements include Memoranda of Understanding with the United Kingdom, France, the Netherlands, Norway, Mexico and, next week, Argentina. We have also entered into our first agreements with the Commission of the European Communities and the Inter-American Development Bank.

If present trends continue, your customers will be increasing their investments in foreign securities both through foreign listings in U.S. markets and in investments under other legal and regulatory systems. We hope to remain leaders in the world

community for the development of strong codes of law and ethics for the protection of investors worldwide. Here I would like to thank the members of the U.S. industry who have served on our Emerging Markets Advisory Committee, and helped us to offer the benefits of America's experience with securities markets to countries around the world. At the same time, through continued development of systems for 24 hour trading and other moves, the U.S. markets and industry must work hard to retain the competitive edge internationally that we have enjoyed thus far.

A final, but no less important trend for the 1990s is likely to be the continued "electronification" of markets globally and domestically. Here, the interface between physical exchanges and electronic systems involves issues of safety and issues of competition. Issues of fragmentation, transparency, best execution and liquidity were the subject of thorough study by the SEC as well as the market community and Congress almost twenty years ago. In the intervening time vast changes in the market have occurred, including the enormous growth of institutions, and rapid technological change. Today entrepreneurs and institutions have developed systems that clearly have the potential for assuming a major role in the operation of the market.

These market developments are a reflection of the ingenuity and innovation that have been hallmarks of our system in the past, and will be in the future. They may bring important cost savings,

convenience and other desirable features to the investing public. However, there are also important questions of transparency, liquidity, consumer protection, domestic and international competition, security and stability. Indeed, it is worth noting that the volume of trading in listed shares off exchange today is greater than the average daily trading on the New York Stock Exchange at the time of the 1975 amendments to the securities laws.

In order to respond to the technological evolution of the market in a more careful and thorough manner, I have directed the Division of Market Regulation to commence a thorough and comprehensive study of the current market structure, and what trends and challenges we expect the U.S. trading markets to experience in the coming decade. This "Market 2000" study will seek to build a thorough base of knowledge and an intellectual framework for deciding the complex and vital regulatory questions that will shape the U.S. markets as we approach the next century.

I do not expect that this study will be complete for at least a year, but I hope that the SIA, the SROs and the entire market community will be active contributors to our work. Our goal should be to make sure that, in an era of intense international competition and rapid technological change, we will be equipped to take the steps necessary to fulfill our Congressional mandates and to safeguard and enhance the efficiency, safety and integrity of

our national market system for the benefit of professionals, investors and our overall financial system.

In these and other challenges as yet unforeseen that I am sure the markets will arrange for us, I hope to draw on the resources of the full spectrum of the U.S. securities community. The securities markets are playing a growing and essential role in financing the U.S. economy. The system that we have built is justifiably a source of pride at home, and an inspiration to nations around the world. It has had to survive assaults on its integrity from within, and it has stood the test of time in evolving to meet the needs of an ever-more diverse economy and marketplace around us. For the future, we can hopefully respond to new challenges successfully so that our markets continue to sustain and encourage strong economic growth while providing fairness and equity to investors.