

ADDRESS

of

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During the last few months, despite the feverish search for political issues, regulation of investment banking and stock exchanges was scarcely mentioned. These two achievements of the past four years could not be made political issues. So well had the principle of federal regulation of security transactions been accepted as a traditional part of American economic life, that even political skirmishes avoided this field. But to infer from this that the outcome of the election had no bearing upon the future of these principles of federal regulation would be erroneous.

The verdict of November 3rd reflected fundamental and deep national desires. It reflected an enthusiastic acceptance of new concepts of what the aims of an enduring governmental system must be. It reflected the intensity of the national desire to move closer to an ideal of industrial and financial security. In its ability to respond to and to effectuate this desire lies, in a large sense, the justification of finance.

At the beginning of this new political year of 1936, it is well to recall for a moment the opening of the political year of 1932. The contrast reveals a tremendous difference in emphasis. In 1932 and 1933 our concern was eternally the depression. Every national measure was attuned to the emergencies of the hour - the great tide of bankruptcies, foreclosures, bank closings and industrial stagnation. The whole administration of government and the whole thought of the nation was conditioned by and concerned with a depression.

In 1936, however, the scene has changed and the emphasis has shifted. The issues in the political campaign of last summer and last fall concerned not the defeat of a depression but rather the direction of a recovery. Amid the flights of oratory and recriminations of the campaign, there came slowly to the forefront a recognition that the problem of the coming four

years was the direction and control of the recuperative forces that were obviously already in motion. And, just as that attitude crystallized in the political campaign, so will it inevitably find expression both in new legislation and in the administration of those laws which relate to the direction of these forces of recovery. Today, instead of ministering to a depression, our problem is to administer a recovery.

This shift in emphasis - from ministering to a depression to administering a recovery - is nowhere more strikingly illustrated than in our own field. Only two years ago our concern lay with the absence of capital issues, sagging markets, and a frightened and embittered public. Two years ago we were bending our every effort to restore life and health to a sick, fearful industry. Almost the whole of our energies was given to the stimulation and encouragement of the tiny flow of capital issues in our security markets. Today one thinks in terms of a wholly reversed situation - rapidly rising markets, expanding volume and an apparently insatiable demand for capital issues. Indeed, the situation is such that already apprehension over the trend has been aroused. Questions as to what can be done to prevent a stock market boom used to be grimly academic. Now throughout the country there is an unmistakable concern as to whether our Commission or the Governors of the Federal Reserve System, or both of these agencies, have the power to check the recurrence of 1929, and secondly, the question is also asked, if these agencies have the power, will they have the courage to exercise it?

Indeed, we hear increasingly the general inquiry not only as to the powers and courage of the government, but as to the direction of its efforts in meeting the new problems of the recovery. "Where", they ask, "is government going in the next four years? Will it turn left or right or will it pursue a middle course? Will the next four years be years of more or less

Where you and others ask that question of government, government seems to me in truth to be asking the same question of you. In other words, how are you going to interpret the mandate of twenty-seven million voters? To listen to and to try to understand the public voice is certainly as much a duty of industry and of finance as it is of the government. Those votes bespeak national desires; they bespeak the hopes and fears of American men and women directed not so much to the forms of government control as to the objectives of the society in which they wish to live. The interpretation of these desires for finance is thus primarily with the industry itself and only secondarily that of government. In short, far more important than knowing whether our Commission and the Governors of the Federal Reserve System can and will exercise certain latent powers is the question whether the operations of private finance, so largely in your hands, will create the occasion for their use. The challenge offered by the verdict of November 3rd is thus a challenge that, to my mind, is directed mainly towards those in control of industry and finance. And may I suggest here that the inclination on your part to heed such a mandate might not be prompted wholly by an altruistic sense of social responsibility.

Each of the three Acts which the Securities and Exchange Commission administers is in fact a repetition of the public resolution that 1929 shall not recur. Law has been carefully built upon law to the end that finance shall be not a game of magic to mystify, bewilder and mislead the investing public, but a forthright business deriving honest business profits from open dealings with customers who come to its counters in good faith, glad to pay a fair commission for a fair service performed. To reach this end was indeed a tedious task, for you may recall how few were the customers with any faith remaining two and three years ago - the customers who had taken all the investment trust, real estate, and holding company securities which were concocted for their consumption in 1928 and 1929.

But that we have made advances - great advances - is clear. Through the sanction of disclosure we have checked to some degree the useless waste that had hitherto attended the flow of savings into industrial enterprise. Through publicity we have checked many of the outstanding defects in the origination and distribution of securities. In these accomplishments we were aided by a measure of acceptance by private finance, and by the legal and accounting professions of the obligations embodied in the legislation.

But now, the intensity of our present sellers' market is in danger of bringing about a subtle dulling of responsibility. It seems to be characteristic of originators and experts alike. Indeed one can draw a strange contrast before the almost tearful protestations of originators and experts against the provisions of the liability sections of the 1933 Act, even after its amendment, and the current tendency of these same individuals to cut corners in the matter of forthright disclosure. The impact of almost daily tilts with accountants, some of them called leaders in their profession, often leaves little doubt that their loyalties to management are stronger than their sense of responsibility to the investor. Such an experience does not lead readily to acquiescence in the plea recently made by one of the leaders of the accounting profession that the form of statement can be less rigidly controlled and left more largely to professional responsibility alone. Simplicity and more adequate presentation is of course an end much to be desired, but a simplicity that misleads is not to be tolerated. The choice here of more or less regulation is an open one for the profession. It is a "Hobson's choice" for Government.

Two other characteristics of present day security distribution deserve comment. First is the insistence upon speed which still dominates both underwriting and distribution. The Securities Act of 1933 concluded that in this demand for speed, lay one of the prime bases for the break-down of

the process during the twenties. The risk of underwriting, it felt, should really rest on something more than the ability to judge the mere over-night marketability of an issue. In delaying the organization of the selling group, something has been accomplished. Some of the pressure that the originating underwriters used to exert upon the selling group members in the "sticks" has been tempered. The importance of preserving and encouraging the independence of the small security dealers and their freedom from subservience to the originating houses of Wall Street and LaSalle Street must be recognized. But what new independence they have achieved under the existing system is threatened too much by the shortness of the underwriting commitment, by the drive for the immediate organization of the selling group, and by the pressure exerted by underwriters to unload in a few hours the risks they are paid to assume.

Then, there are the problems that flow from the prospectus. The hope that adequate investment information would be widely circulated is perhaps the keynote of the Securities Act. Yet today, in a market that has a plethora of buyers, the selling document too rarely has the attention paid to it that it deserves. Its length results not so much from the requirements of the law, but from the fact that the writing of what should be popular portrayal of business facts is dominated by lawyers nurtured in the drafting of trust indentures. The responsibility for perfecting the mechanism of the prospectus rests not alone upon the Commission. The prospectus must be used, and its purposes honored. Otherwise, the objectives of existing legislation will be far from being reached.

I mention these facts not in the spirit of carping criticism of investment banking methods. I mention them rather as factors for whose success we of the Commission cannot alone assume responsibility. Failure in the field of security legislation is too tragic to contemplate. National desire is so intensely bent upon success, so deeply determined that the conditions of the late twenties shall not repeat themselves, that you, to whom that desire is directed, we, who are in part agents to superintend its consummation, dare not fail. If we fail, others will take charge; their sanctions, their mechanisms, will be different. But have no doubt, the objective of our national life in this field will be attained. The cost of that achievement is negligible beside the cost we know will attend failure.

It is easy to pursue the same theme, the same comparisons in the field of trading upon our organized exchanges. Our problems there are even more clearly those that spring not from the depths of depression, but from the appearances of recovery. That recovery cannot follow the traditional cyclical patterns. Any interpretation of our national aims as looking for the return of the shallow prosperity of boom days is false. I know that some financial circles still see the country as one that wants a repetition of the late twenties. But those financial circles have already earned the reputation as poor prophets of the tempo of America's desires. The atmosphere of the board room is a poor litmus test of the hopes of our national life.

It is your responsibility, as much as ours, to think in terms of the relationship of today's and tomorrow's market conditions to those that brought on the catastrophe of 1929. I know of the efforts to lay the blame for market imperfections onto matters over which the Exchange, considered as a community of its members, has no control. Irrespective of what truth may inhere in these complaints with respect to particular

forces, to place the whole burden of an unstable market on matters such as margin requirements, the Commission's anti-manipulation activities, a purported flow of trading abroad, or our forms of taxation, is, to use a psychological term, mainly escape ideology. Of one thing we can feel sure, that when price has no relationship to earning power, present or prospective, a mechanism that will permit maintenance of values of that character, has lost its justification. Every aspect of trading must therefore be adjusted to operate against the potentiality of such a condition. How far, we may well ask, does our traditional thinking carry that emphasis? What price liquidity, on a plane that reflects and can reflect no real wealth?

Those are the dominating questions that underlie administration for recovery. In our consideration of the problem of segregation on the floor of the exchanges, in fact essential to any solution of the place of dealer activity on these exchanges, was the relationship of that activity to the building up of undue speculative positions and the effect of that activity on price trends. We cannot accept the conceptions of the place of speculation in our security markets that built a justification for the prices of the late twenties. And if we have a responsibility to think beyond conceptions that time has proved hollow, that responsibility also devolves upon you. Instead of the common concern that one constantly hears about the difficulty of liquidating at a moment's notice huge blocks of securities in the markets, should not the real concern be with the causes that place strains and stresses of this character upon the financial mechanism? If these strains spring from useless speculative desires the answer is plain. Instead of trying the hopeless task of constructing a mechanism that will absorb the huge pressures of that type, effort must be directed towards closing the investment machinery to the play of irresponsible forces of such a character.

Investment rarely seeks the board room. It rarely follows the hunches of talkative customers' men or the advice of ignorant investment counsel, whose recent rise presents a problem of national consequence. Investment, though it does not despise close market spreads, regards them as of minor consequence in relation to significant trends. How far our trading mechanism is adjusted to emphasize these qualities, rather than to the minutes and seconds essential for the purposes of speculation, may well represent the difference between the hoped for sobriety of the new recovery and the mania of the old.

One of the fundamental hopes of the Exchange Act was that through some consciousness of the nature of corporate enterprise we, as a nation, should develop into investors -- rather than speculators. Pure speculation we can tolerate at the race track or elsewhere, where it cannot stalk under the enticing garb of investment. But on the exchanges we sought a reflection of values that have a relationship to something more permanent than mere liquidity. Yet today one wonders where the growing emphasis lies. One wonders just how the battle between the dull registration statements of listed securities and the fascination of the Trans-Lux will eventuate. And the responsibility for that outcome will not be ours alone, nor will its glory, if such there be, be the monopoly of political party or economic creed.

The rightness or leftness of Government in this field is no more capable of prediction today than next month's market. On trueness to the ideals that two years ago gave Government responsibility in this connection, you can count. But the direction of the effort is less in our hands than in yours. What tempo you bring to tomorrow's market will mark the direction of action. What responsibility you assume means more today than the immediate tenor of our activity.

In the field of holding company regulation the same needs and the same emphasis upon administration for recovery are present. The picture of the industry in 1936 is a familiar one. Maintenance and construction budgets were curtailed in the years of depression. Meanwhile invention and education in the uses of electric power made for an increasing demand. Surplus capacity is in many cases on the point of exhaustion. Every indication points toward the need for expansion and the concomitant employment of both men and capital. The direction of business administration for recovery should plainly be that of courage to assume responsibility for fulfilling the growing needs of communities. Yet it is clear that our national determination is not that these needs shall not be met from private sources, but that the manner of meeting them shall not repeat the tragedies of the last decade. We have had our fill of write-ups of security issues balanced by engineering mythology rather than the potentiality of worth, of empires of power costly to acquire, more costly to maintain, and uneconomical to operate. These things demand adjustment and the administration of that adjustment is a condition in the nature of the recovery that is demanded. The administration of the content of such a program cannot, of course, follow prejudiced and Procrustean lines. There must inhere in it flexibility sufficient to meet the engineering and economic demands of our time.

These national desires of the new recovery are writ large and clear in the framework of the Public Utility Holding Company Act of 1935. Opportunities for economical integration and expansion - the types of opportunities that investment banking has a responsibility to discharge - are present on every hand. Yet the action that the judgment of the

operating man and of the investment banker dictates finds itself thwarted elsewhere through some incoherent lack of trust in the destiny of American enterprise. The responsibility that should lodge in the hands of men who wish to do and to act, has moved strangely into the hands of men who had no vision but that of the past, and of men whose political hatred for the direction of American life made them believe that through some abracadabra of legal learning they could turn it backward. Where yesterday we saw the tragedies of irresponsible action, today we are face to face with the tragedies of selfish and irresponsible inaction. In this contest of power between a handful of men and a nation, no longer lethargic but vocal and tense, there can be no question as to the final outcome. And if this handful seeks again a verdict, to the charges of the past will be added this refusal to think in terms of adapting an industry to the needs and social aims of a people. Failure here on the part of Government would be its failure to interpret aright our national desires. But as the stage is now set, if there be no misconstruction of these aims, the unnecessary cost and what may be unwonted delay in a recovery now overdue, is chargeable elsewhere than to Government.

Administration in this field has thus been partly driven into stagnancy, forced to take up the gauntlet of a legalistic challenge, but still hopeful that a recognition of the demands of the new recovery will become plain to a handful of men, and hopeful that from such a recognition will spring the program of expansion, readjustment and employment that already a year ago should have been in the doing.

The challenge of the coming years is thus a brave one. Out of the crucible of the depression has evolved a firm determination as to the

character of the new recovery. Its problems are too large to permit play on the part of government or on your part for petty hatreds, mere political ambitions or recriminations. Upon matters such as these we dare not waste time. The direction of the resolve of November 3 is too clear. The intensity of its depth is too fully measurable. But the exact methods of translating that resolve into administrative action cannot be known until its effect upon powers other than those politically responsible to an electorate is fully understood. That translation is first and foremost your problem and your opportunity.

The administration of the new recovery is not and cannot be a matter of unilateral action. Its success can only rest on a recognition of the need for continuing industrial and financial reorientation - practical in attainment, true, but always idealistic in direction. You cannot forget that the last recovery was your recovery and that it almost destroyed you. Fairly or unfairly, you became the scapegoats of a bewildered and discouraged people. This new recovery, certainly in its initial stages, will also be your recovery. Its responsibilities are now yours. How long you will discharge them is first your concern. How well you will discharge them is first your challenge. The direction of administration depends upon your answers to these questions and the answers must be clear, unequivocal and free from hesitation. If the mandate of last November means to us that we must not fail, more clearly does it mean to you that you dare not fail.