

ADDRESS

of

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to the

NEW YORK STATE BANKERS ASSOCIATION

"THE S.E.C. AND THE COMMERCIAL BANKER"

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Mr. Chairman, Members of the Association and Guests:

I was glad to be invited to talk to you today. Unlike other speakers before the Association I am not an economist; and I have no disposition to leave my depth for dangerous waters. I accepted your invitation because the Securities and Exchange Commission, although it does not have much to do with banks directly, is nevertheless concerned, as you are, with the general functioning of the capital markets.

You will recall the terseness with which the President, in his recent message said that the state of the union was "good". I hesitate to use any single adjective to characterise our capital markets. But from where I sit, the figures seem to show that these markets are still pumping new money into industry at a high rate and that the private American securities buyer is still a factor to be reckoned with in the growth and development of American business. Out of the total volume of registration with this Commission over the years 1934 to 1947, 26 per cent was for new money purposes. In contrast, you may be interested in knowing that, out of about six and one-half billion dollars of securities registered with us during our last fiscal year for public offering 81 per cent was for the purpose of providing business with new money. Of course, these figures relate only to financing registered with us, and do not include financing through private placements, small issues, term loans, railroad issues and other exempt methods. But this comparison makes it obvious, first, that our national plant is adding phenomenally to its development, and second, that the channels of securities distribution to direct investors are still being substantially used in the course of this development. Don't discount the private investor, he still kicks in the billions to keep the economy working and growing.

That is where the Commission comes in. Every penny of this six and one-half billion dollars went through the process of registration with the S. E. C. and was sold pursuant to prospectuses distributed under the

requirements of the Securities Act. That Act requires that certain public offerings of securities be registered with the Commission by the filing of a statement which contains the information an investor needs to know, and the law requires also that every buyer of securities in such a distribution receive a prospectus which summarizes that information. These requirements, now on our statute books for fifteen years, were once branded as a sure bottle-neck and stumbling block in American financing. I wonder if you recall some of the arguments that have been made against the registration and prospectus requirements administered by the S. E. C. It was said that the Commission would overstep its limited authority to require the disclosure of full and truthful information and would censor the process of securities selling and buying. Fifteen years of administration of this Act have proved the contrary. Investments running the gamut from triple A to Z have been sold under this law. High grade investments and pure speculations have been registered and sold under the Act. For the only condition upon selling is that the entire truth be told in the registration statement and prospectus. While many questionable deals die at birth because the promoters fear disclosure, the Commission itself does not pass on the investment merit of any security.

You may ask why I make this recitation to a group which consists of people whose job it is to find investment outlets for deposits. The answer is, I think, obvious. While in a sense, all investors compete with each other for investments, I believe that all segments of the investment community in fact constitute an integrated body; all in fact participate in providing capital and credit for the growth and maintenance of a healthy economy. I know that we are far from having achieved any true integration of functions among the various elements of the investment community. I know something of the problems of the commercial bankers and of their complaints at being

restricted in the extension of credit while other segments of the investment community have been free to increase investments. The investment banker complains of private placements, and all who have assets that must be invested watch with interest the trends in internal financing of industry through surplus and depreciation funds.

But the truth remains that in a very important sense all segments of the investment community do and must complement each other. Institutions and banks are, generally, lenders. And, as the trend toward term loans continues, banks tend to become another source of debt capital. But a healthy economy needs very substantial amounts of equity investment. I have long been an advocate of improving the equity position of American industry. As long as the investment habits of institutions and banks remain as conservative as they have to be for safe operation, we will have to continue to look to the American private investor as a market for equities.

This is a problem with which all of us have a direct and vital concern. There is no better security for debt than a substantial equity base. The most ingeniously devised security arrangement is no substitute for a capitalization which can cover its debt service and amortization by a comfortable margin even while weathering the uncertainties of the business cycle. A good equity base for industry is not the concern of management alone, but of all whose welfare depends on the sound operation of business.

I think it obvious that much of the hope for an expanding equity base for American business lies in maintaining the integrity of our securities markets, and in preserving the confidence of the American public in those markets. It is the Commission's job to help maintain that confidence through a forthright administration of the requirements of the securities laws. A sensible man may buy a pig in a poke once. But, generally, if he is being asked to take a risk he wants to take a calculated risk. With his

equity he wants the protection that these laws afford through the provision of information, the prevention of fraud, protection against abuse of inside position and abuse of the proxy machinery.

You cannot maintain a sound and permanent market for equities by appeals to cupidity and the desire to take a flyer. When a company seeks additional equity capital its first recourse is, generally, to its existing security holders. And the measure of success of a rights offering is likely to be, in large part, the extent to which its equity holders have bought an interest in the growing enterprise rather than a slice of the Dow-Jones index. A steady flow of equity money and stable equity markets can come only from investors who are given a chance to know what they are buying and are assured that their rights as security holders will not be manipulated behind closed doors. I do not want to be misunderstood - I have no personal policy, and the laws we administer express no policy against honest and informed speculation. Our function is to provide the means for informed decision as to buying and selling.

In passing let me make it plain, too, that I believe that administration of these requirements must be open-minded and flexible as well as forthright. Over-regulation which impedes financing without adding significant protection to investors is a disservice rather than a service to the investor. The laws we administer assume the American system of investment; they are designed to strengthen and not to revolutionize it. To keep these laws useful, to facilitate the flow of capital, we must remember that we live in a changing world. Old problems and policies become obsolete as new problems arise and new policies are needed. Only constant vigilance to keep ourselves aware of the problems of legitimate business and to keep ourselves flexible to meet them can preserve the continuing usefulness of the securities laws.

To that end the Commission keeps itself open to conference and suggestion. It maintains continual studies of the requirements and of the way they work in practice and is constantly engaging in reviewing, revising, streamlining, and simplifying them. As an example I should like to note the recent adoption of a rule which we call the "document rule". While in itself not of major importance it indicates the trend; and it should be of some interest to those who help issuers to handle the details of rights offerings. The new rule does away with a practice of many years standing - but nevertheless not sacrosanct - which resulted in the duplication of prospectuses in offerings by issuers of additional stock to existing stockholders. By a simple adjustment, hedged with limitations we think necessary for the protection of investors, we have eliminated unnecessary effort and expense in at least one field of securities distribution.

Our efforts have not stopped with review of rules and regulations. For a long time we have been engaged in a study of the operations of the statute itself. We have been in touch with all segments of the public interested in the operation of the Securities Act. As you may have noted we have recently been conferring with a committee of interested members of the securities profession and we hope to be able to reach recommendations which would not only protect investors but substantially facilitate securities distribution by doing away with certain restraints of which securities distributors have long complained.

Taken as a whole the work of the Commission should be of direct interest to the commercial banker. To mention one phase of our work bearing directly on the commercial banking function: many companies whose internal accounting, auditing, reviewing and reporting systems were in a sorry state before passage of these laws have been forced to over-haul their record keeping and reporting systems. The path of the commercial banker in assessing and appraising a

proposed loan has been materially smoothed in many cases as a result of the requirements we administer. No commercial banker would want to see a deterioration of these systems of accounting, auditing and reporting. As an investor whose transactions are likely to be large and significant he has an interest in their continual improvement.

Because our complex economy is made up of so many interdependent factors; because the lender, as well as the owner and manager, has a stake in the proper financing of business and in the maintenance of sound capital markets I think that our work at the Securities and Exchange Commission has a particular value to you. I hope I have, in the short time at my disposal helped you to see why this is so.