

ADDRESS

of

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Chairman, Securities and Exchange Commission

to

NATIONAL ASSOCIATION OF CREDIT MEN

"ACCENT ON EQUITY"

Atlantic City, N. J.

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The invitation to address you today came on the letterhead of the Association and, when I received it, I was struck with the motto it bears: "Guarding the Nation's Profits." That motto confirmed my impression that there is a community of objectives between the Securities and Exchange Commission and your Association. I was, therefore, glad to have this opportunity to meet you and to talk to you about some of those objectives.

The credit man reaches more deeply into the economic processes of distributing goods, and affects smaller companies more significantly, than does any group in the financial community with which we at the Commission regularly deal. But the credit man remains primarily an investor and a maker of investment policy. Whether he deals with big or little business or with individuals in the mass, he shares the concerns of our entire financial and commercial community with the state of the economy and its financial health. The very range of the discussions at this splendid meeting demonstrates that the modern credit man is aware of the broad problems we face today.

As investors and as framers of investment policy, you cannot help but be concerned with what the S. E. C. is and does, and what it means to you. I assume that you all know that the job of the Commission, under the laws it administers, is to protect the investor. There are many popular misimpressions about the way the S. E. C. works and, in outlining what we do I would like to stress at various points what we do not do and cannot do. Except for regulation of the financial affairs of companies that are parts of electric and gas utility holding company systems, and except for some regulatory functions involving investment companies, the keynote of the activities of the S. E. C. is disclosure and the maintenance of securities markets free of fraud and manipulation.

Companies seeking to raise capital through the public offering of securities are required by the Securities Act of 1933 to register those securities

with us. The registration statement contains the essential information investors and their advisers need to have for informed investment. Not only must companies file information with us, but our laws are designed to assure that at some time in the process of selling securities, the securities distributor will actually give to the investor a prospectus containing this essential information.

With minor exceptions securities traded on national securities exchanges are registered with the Commission under the Securities Exchange Act. That Act requires the issuer of such securities to file initial and periodic information portraying the company's financial condition, and in addition, regulates the solicitation of proxies, and requires disclosure with respect to transactions in the companies' securities by officers, directors and certain large stockholders.

While our jurisdiction over public utility holding company systems and investment trusts extends to regulating certain of their financial affairs, these companies too must provide us with initial and periodic information as well as data related to specific cases where a record of the facts is necessary before the Commission can act.

Neither the Securities Act nor the Securities Exchange Act authorizes us to tell companies what securities they can or cannot sell. Nor do our laws authorize us to advise investors as to what they should or should not buy. As long as the whole truth is told, investment decisions are left to the free judgment of buyers and sellers. Under these laws informed self-interest remains the key to financial activity.

As a result of our functions, we are one of the most important present storehouses of financial information and we are, of necessity, actively concerned with the disclosure aspects of accounting and the reporting of corporate affairs. In a very direct way our activities affect and benefit the credit man. To the extent that he needs information about companies who

file with us, he has at his finger tips a wealth of data. We do not have the money or the people to collect, organize and summarize as much of this information as we would like, but our statistical series have been of enormous use to credit men, industrial and commercial managers, and others who put a premium on informed economic activity. We have received requests in the thousands for some of the series we publish, alone and in combination with other agencies. For example, credit men have welcomed our industrial financial report series published jointly with the Federal Trade Commission, our series on the composition of individual savings, and those relating to expenditures for plant and equipment. If I do no more tonight than bring home to you the fact that the Commission may be able to provide information useful to you in credit analysis, and induce you to make broader and more effective use of this information, this talk will have served a worth-while purpose.

It was not so very long ago that there was considerable confusion and lack of uniformity among accountants in the application of proper accounting standards. Recognizing that fact, Congress has given the Commission great responsibilities in dealing with significant accounting problems of companies filing information with us or otherwise under our jurisdiction. One of our primary tasks, and a continuing one, has been to clarify and refine accounting standards and to bring about uniformity in the preparation and reporting of financial data. The Commission, together with associations of accountants and others, is constantly engaged in a study of accounting standards, resolving individual cases in the light of these standards, and reviewing the standards themselves to keep them currently useful in the light of changing conditions.

Credit men and others who have dealt with these companies have been beneficiaries of these efforts. I would expect the credit man to understand

how difficult our task is because many of you have in your own profession done the same thing for business. In dealing with smaller companies whose problems nevertheless lap over from double entry bookkeeping into the realm of accounting, credit men have performed a singular service by insisting on accounting, reporting and control methods. No company which is likely to be an issuer of securities in the public markets can afford to ignore the accounting standards we have been developing in conjunction with the accounting profession. Rather than wait for the eve of such an offering to put its methods into shape, it would do well to begin early. The credit man is emerging more and more rapidly into the status of business adviser. He will serve himself, his borrowers and the public well by remembering that the transitions from a closely held enterprise to one in which the public has an interest can be considerably improved by careful adherence to high standards in all segments of the balance sheet and profit and loss statements.

The credit man is frequently a key factor in the planning of financial programs for the small and middle sized business. His primary business is lending. But he cannot, for his own sake and the sake of the economy, be indifferent to the equity position of his industrial and commercial borrowers. Several days ago I participated in a forum on equity financing. That forum, others like it, and recent statements by representatives of all segments of our economy have indicated our growing awareness of the importance of providing a sound equity base for individual companies in our economy and, thereby, for our economy as a whole. The problem of debt is, as you are all aware, an extremely complex one. It would take a text book for an adequate discussion of the underlying factors in taxation, cyclical change, interest rates and so on that affect changes in our over-all ratios of debt and equity.

A fact commonly overlooked in discussions of the equity problem is the distinction between big and little business and the wide range of distinctions

between businesses of various kinds. In many ways it is inevitable that small business should accent debt; but it is by no means always fortunate that this is so. Little business works under special difficulties in attempting to procure an adequate and conservative capitalization. Because of the importance of inventory and receivables to many smaller enterprises, because of habit, because of lack of public interest, because there are so few mechanisms available to them for effective distribution of equity securities, the smaller businesses tend to turn toward the debt route, long term and short term, for many aspects of their financing.

Without the credit man many small businesses would be utterly without means of current financing, and even large businesses depending on wide distribution of inventory would be hard put to meet the short-term needs for funds. Credit men are to be commended for the amazing way in which they have developed techniques to meet these needs. Modern methods of financing of inventory and accounts receivable are as much a testimony to the genius of our economy as are fluid-drive and the jet-plane.

But your emerging status as consultants and advisers brings you of necessity into a field broader than that of commercial credit alone. Of what use is it to have evolved security devices which assure the lender immediate and effective means of attaching the security, if the collapse of the loan signifies collapse in the value of the security. Your life blood is an active consumer demand at a fair level of prices. Like any part of a complex mechanism, this part of our economy can be sustained only if it is geared into many other smoothly running parts. Producers and distributors are not only in competition with others in the same line but depend on them, as they depend on the rest of the economy. If Company A, producing men's suits, should have to dump inventory in distress, it may hurt its competitors more than if it could continue in business selling at a competitive price.

You must, therefore, be sensitive to all the factors that might endanger the continued prosperity of Company A, whether you have financed that company or its competitor. Therein lies the good sense of your motto "Guarding the Nation's Profits" - and, in a sense, therein lies my theme of "accent on equity."

The smaller business presents many problems untouched in the recent wave of thinking about the need to provide a sound equity base, and sound equity markets for American industry. Financial analysts, securities distributors, and investment institutions now thrashing out the equity problem, are not likely to have the same know-how and skill that you have in your special field. But your field is an important one. We would not be America if we did not have a constant formation of new businesses, growing from little to big; nor do we justify ourselves by the high rate of mortality of the smaller business which characterizes recession periods. The segments of our economy are interdependent. Failure anywhere is dangerous. There is therefore a high premium on keeping the smaller enterprise healthy.

Financial health in this sense means sound equity. That problem is on the lap of the credit man in his role as business adviser, consultant, and guardian of the nation's profits. He must as I see it, be alert to whatever opportunities exist for his borrowers to increase equity. Below a certain range, the route of public equity financing is impractical. But within a median range of business size, opportunities for such financing should not be missed.

I do not foresee the millenium. To promote public equity financing for the smaller enterprise is about the toughest job I can imagine. It needs more than good intentions. The problem must be studied and your Association should be a splendid forum for such a study.

I may have raised more problems than I have answered. But if I have been able to stimulate any further thinking about these problems I have done my job. I do not think I could have had a better audience or a more appropriate forum for a discussion of these vital challenges we face today.

Thank you.