FIFTY YEARS IN WALL STREET

by

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The first rule that an investment man must learn, is that in economics things change constantly. Because a stock is earning $1 a share this year, is no indication that it will earn $1 a share next year. The fact that $1 will buy a pound of chopped beef today, is no indication that it will buy the same next year. The work of the investment man is to try to judge longterm trends and this takes constant study and judgment.

When I came into the investment business in 1922, corporate management was willing to give very limited information. Corporate statements were tiny and uninformative. To get further information was difficult—particularly anything unfavorable.

In the bond field, a man by the name of Moody had developed a rating service for bonds. There was certain information which he required before he would rate. The bond buyers came to lean on these ratings and if a bond did not have a Moody rating, it was very difficult to sell it. For that reason, the information that would tell whether a bond was safe, poor or average, was generally available. During the 20's, I did almost entirely bond analysis because I could not get the information on stocks that I felt was necessary.

When the 1930 depression came, everything collapsed. Earnings became almost non-existent and many well-rated bonds got into trouble. My customers were hurt but not as badly as those in the stock market. In 1931, I had the best year in my history up to that point. I had established the record of a conservative and people wanted the advice of a conservative.

During the 20's and early 30's, I found that I could get a fairly good report on a Company by visiting the competition in the respective industry. This took a lot of time and one could not cover the large industries—there were too many companies. After I had visited two or three companies in an industry, I was bound to learn some of the problems. This was particularly true of the smaller companies where the officers needed my help more than did the big ones. As the depression of the 30's came in, I found that the Presidents of the larger corporations were more helpful. At that time, I was Vice President of the Trust Company of North America in charge of the Investment Department.

A group of brokers and bank officers made arrangements for us to have the third floor restaurant of Schwartz on New Street. Mr. Schwartz agreed to serve us a meal for $1 *consisting of day-old food*—but it was a meeting place. There were lots of under-priced securities in those days. When our discussion brought up one which seemed a particularly good value, various members would visit the companies in that industry and bring back to the group, the results of their visits. In that way, we learned a great deal about some securities. To be successful in the securities business, requires the finding of a profitable security and soon most of us were doing far more business than we had done in the 1920 boom stock market.

One day we decided to invite the President of the corporation under study, to visit us. To our surprise, he agreed to come, eat our day-old food, and answer any questions we might have. We made the talks "off the record." This was so successful that we invited other Presidents to come—and to our surprise, they came, too. We invited friends to come to these meetings. We had dues of $2 a year by this time and most of our friends joined. Gradually, this built up to the point where we were having two or three meetings a week. A meeting that had been off the record could no longer be kept off the record, so it was opened to reporters. This was the start of the New York Society of Security Analysts which has now grown to a national organization with societies in major cities and a membership of over 7,000. It has been helpful in providing information to security analysts and, through them, to security holders. A stock which was a good value, could be presented by the President to the Security Analysts Societies. If the analysts were convinced it was a good value, this information was quickly disseminated to the public investors.

Security Analysis is a business of change. Around 1969, the biggest House in the Street—Merrill Lynch—found that conditions in Douglass Aircraft were deteriorating. Slowly, so as not to break the market, they sold out their customers' stock. Anyone else could have gone to Douglass and could have gotten the same information Merrill Lynch had obtained. Shortly afterwards, the market on that stock broke and the Securities & Exchange Commission held that Merrill Lynch had taken advantage of inside information. After this, many Presidents were unwilling to talk to the Security Analyst Societies and those that still do, are being very careful not to give any material that is not public knowledge. I suspect that the very great work done by the Security Analysts Societies in disseminating information, is going to be lost.

As a broker, I have found that I can, if I know the Company, find out most things I want to know but I have to be very careful not to tell my customers but merely advise them to buy or sell. Getting information ahead of the crowd is a part of the security business and always will be.

During this same period, another development was coming along which made annual corporate meetings more informative. I will illustrate this by the case of the Curtis Publishing Company, although the same thing happened in many others. Ruth's father had been with Curtis for many years and, through him, I was kept informed of developments. However, I did attend annual meetings.

In the 30's, a man by the name of Gilbert died leaving to his two sons, who were lawyers, a large fortune. This comprised stock in small amounts of practically every Company listed on the New York Stock Exchange. The Gilbert Brothers attended a few annual meetings but found, as I had found, that it was difficult to obtain other than the most meager information. They decided that they would attend annual meetings and attempt to make them more democratic.

The Curtis meetings for years had consisted of a perfunctory business meeting in which a vote was quickly called for electing the Directors. While the vote was being taken, the Treasurer droned out a long Treasurer's report which no one understood. As soon as the votes were counted, the meeting was adjourned. I was usually invited to join the officers at a bar which they had in the building and we had a very jolly hour. I was told everything I asked about the Company so I was completely happy.

Then Mr. Gilbert arrived at the annual meeting, asked a lot of questions which were largely ignored or unanswered. Ultimately, he spent an hour lecturing the management on their failure to be responsive. The management listened tolerantly and, as soon as he was through, announced the vote and adjourned the meeting. After all, Mr. Gilbert owned only ten shares.

The next year, as soon as Mr. Fuller (the Curtis President) opened the meeting, Mr. Gilbert was on the floor stating in his rather quiet but obnoxious manner that he had a whole series of questions. In the midst of this, a loud voice from the far corner of the room said, "Shut up! You do not know how to talk to those fellows." This man turned out to be a restaurant owner who had brought a little Curtis stock and was upset at the way it was turning out—the price had gone down. He started to talk when another voice, from another corner of the room, called out, "That is plain silly." For two and a half hours this discussion among the three of them went on—none recognizing the Chair. Around six o'clock, the vote was finally taken and I again went up to the bar with them. (Perhaps I should state at this point that I was then, and still am, a teetotaler.) Walter Fuller, the Curtis President, was very much upset. I had been attending quite a few annual meetings where these three had attended. In one of them, the presiding officer had merely declared them out of order, had gone ahead with the vote, and then said, "I am willing to answer any questions you may have." At 6:30 p.m., he got lunch boxes for the Company management, which they ate at the meeting. (There were none for the stockholders.) My suggestion was that they do this in Curtis the next year—which they did. The meeting was over before 5 p.m.

I did favor Mr. Gilbert in his demand that questions be answered. I had called Mr. Gilbert to congratulate him. Mr. Gilbert did a great deal to make annual meetings more democratic. The demand that information be made available was coming from the Financial Analysts and from the stockholders under the leadership of the Gilberts. This did lead to heckling from others who were uninformed investors.

This leads up to the Simplicity Pattern Company whose stock we started buying in 1946. I had felt for some time that the Curtis Publishing Company was heading for problems and had been steadily selling the large holdings that I represented. Many of the problems of Simplicity were similar to the publishing business. Sales in the pattern business were increasing—radio and television were becoming a serious competitor of Curtis. Simplicity had no debt and enough cash to pay off everything they owed. They sold half of all the dress patterns sold in the world. The stock was selling at five times earnings. By personal interviews, I found that those earnings were reported on an ultra-conservative basis. They were writing off about $1 a share each year that seemed unnecessary. The effect of such write-offs was to reduce reported earnings but increase the amount of cash retained by the Company.

Then I visited all of Simplicity's competitors including Butterick, McCall's and Vogue. (There were only five.) It became apparent that four of the five were having greatly improved business. The fifth was too small and was shortly afterwards discontinued. Every competitor agreed that more women were using patterns. All agreed that Simplicity was their toughest competitor.

With that study, I decided to make Simplicity a major recommendation and we purchased carefully a lot of stock. For five years thereafter, the price of the stock declined while the general market increased.

About every two months, I would spend from 4 p.m. to 7 p.m. or later, at the Simplicity offices talking to Mr. Shapiro and the other officers. Each time, I returned more enthusiastic and bought more stock until my customers had accumulated 20% of the outstanding stock. As I write this, Simplicity has increased to a price about 150 times the price at which I was buying it during those five years.

From these experiences, I have deduced a few general rules:

1) No one can gauge short-term price swings of stocks

2) Stock swings over a two or three year period are no indication of value. There is a tendency for people to follow the leader—buy when stocks are going up and sell when they are going down. Normally, the best time to buy is when a stock is declining and to sell when the price is rising.

3) Successful stock investment requires a lot of study. It should not be done on an emotional basis. Perhaps the age of the

computer will eventually take the place of study. To date, this has not been true. The programmers are not yet skillful enough.

4) Probably more losses are created by selling after small profits are attained than in any other way. Stocks tend to increase with inflation which is a steady trend. Because of this, stocks should be sold only when the long-term statistics indicate considerable deterioration in prospects—or for diversification.

Economics is a business of change. As I write this, the country and the world are moving towards greater controls—control of prices, control of wages, control of production—all being done by government. A good investment man does not fight these controls. He tries to figure the long-term direction of the economy and how to make a profit from it. He must always remember that money is a medium of exchange and that money will be manipulated in such a way that it keeps the majority of the people happy. Right now, people are objecting to inflation but most people like inflation. People want to see their own income increase—and that is more important than the fact that prices go up.