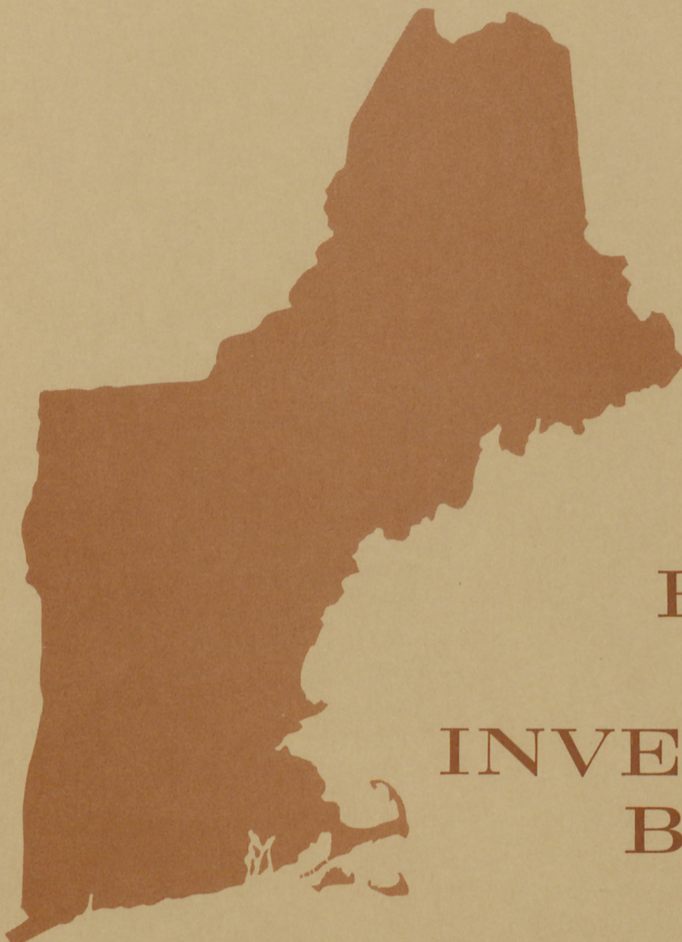

A HISTORY OF INVESTMENT BANKING IN NEW ENGLAND

FEDERAL RESERVE BANK OF BOSTON

To the Reader:

Since the early days of this nation, New England investment banking houses have contributed significantly to the economic development of both the region and the country. As securities underwriters and dealers, either individually or as members of syndicates, they have played vital roles in the creation and expansion of innumerable manufacturing, transportation, communication, public utility and other business enterprises. And through their work in the field of state and municipal bonds, they have aided notably in the development of public facilities and services.

The study presented in the following pages was first published as a part of the 1960 annual report of the Federal Reserve Bank of Boston. It is now reprinted as a separate booklet in response to continuing requests from teachers and students of financial history throughout the nation.

George H. Ellis, *President*
Federal Reserve Bank of Boston

August, 1965

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a History of Investment Banking in New England

FEDERAL RESERVE BANK of BOSTON

Be it known, That Israel Thorndike

of Boston in the county of Suffolk is entitled to one Share, viz. No. 110

of the property of the **New Hampshire Iron Factory Company:** *transferable only by deed absolute and without condition, under* his *hand and seal, acknowledged before some Justice of the Peace, and recorded by the Clerk: and the purchaser, shewing to the Treasurer of said Company such deed so recorded, and delivering up this Certificate, shall be entitled to a new certificate, certifying the property of such share to be in such purchaser.*

In testimony whereof, *I the Treasurer have signed this certificate, and affixed the seal of said Company thereto, this* Eighth *day of* May *in the year of our Lord one thousand eight hundred and* eleven

Gideon Snow Treasurer.

FOREWORD

Modern investment banking is a product of evolution, reflecting economic and financial developments of the past. The industry's present organization, functions, and range of services are designed to meet the demands for investment capital in a highly industrialized society with an increasingly broad investor class. In a little more than 100 years the United States economy has been transformed from one predominantly agricultural to one with industries using large amounts of capital on an intensive basis. This transformation was facilitated and speeded by the contributions of investment banking, with New England firms playing a major role in the process. The industry today provides a channel through which savings are transformed into permanent capital.

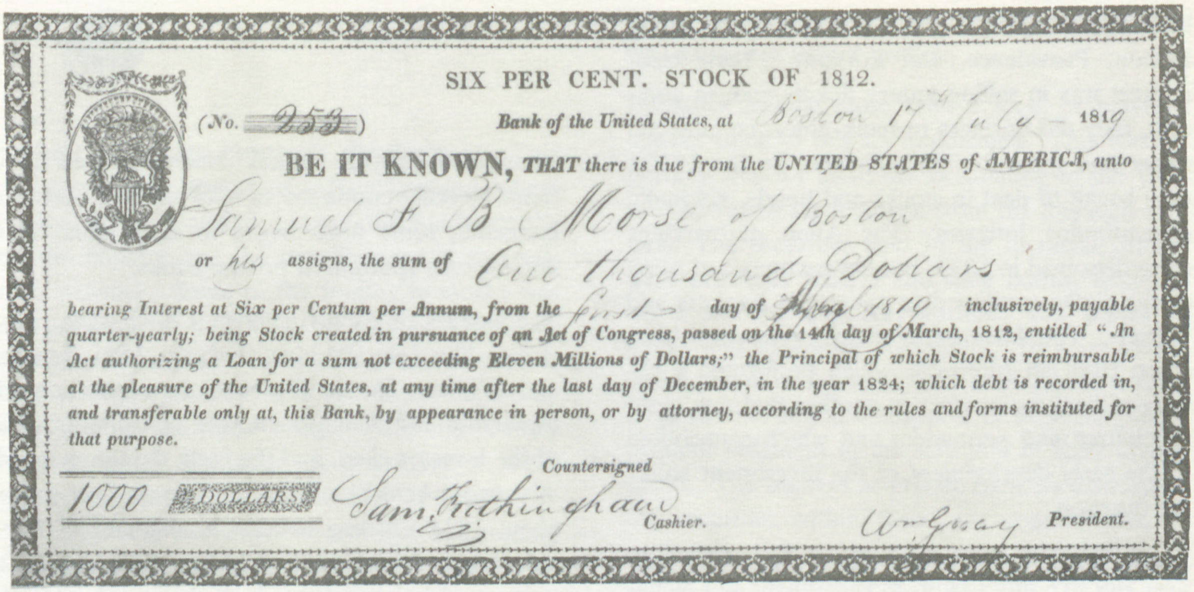
To a considerable degree the high output per capita of the nation's industrial system results from an extensive use of capital. Increasingly rapid technological change, characteristic of the postwar period, places a premium on the development and replacement of capital equipment such as generators, turret lathes, hydraulic presses, entire manufacturing establishments. With a rapidly growing labor force, investment must continually be made merely to maintain the existing level of output per capita. Productivity must be advanced at least enough for a nation to hold its position in world markets. In addition, there is a broad field of public investment, such as highways, bridges, schools, and hospitals, which provides services essential to productive efficiency and to an advancing standard of living. The long-term borrowings for these purposes also constitute a demand in the investment market. When both corporate and public financing calendars are heavy, the investment banker's problem becomes increasingly complex.

Since World War II the demands for capital by both corporations and governmental units have been at record levels. In the private sector of the economy new security issues provide about one-quarter of the funds required for expansion or other capital purposes; retained earnings account for the balance. Although the amount of new money raised through security issues may be marginal in relation to total capital investment in the private sector, it represents a major portion of capital outlay of particular firms. During the years 1946-1960 nearly one company in three with public ownership of stock floated one or more new issues of securities.

In 1960 the number of corporate issues exceeded 1,200, ranging from less than \$100 thousand to more than \$250 million. More than 400 investment banking houses were involved in originating and underwriting these issues, and at least 1,000 firms participated in their distribution. During the postwar period the volume of new corporate capital issues has ranged annually from \$6 billion to \$12 billion. The issues of state and local governments aggregated almost \$8 billion in 1959, the highest figure on record. The total was only \$1 billion at the close of the war.

The investment banker plays a distinctive role as an intermediary between the issuer of securities — private corporation, municipality, or state government — and the investor — individual, insurance company, pension fund, or other institutional investor. In this process the investment banker provides a series of interrelated services for the issuer — the formation of plans for raising capital and the assumption of risk through purchase and distribution of the securities. The banker provides immediate capital for the issuer and reaches the market which will afford the best possible prices and the desired distribution of securities. The compensation — which varies — is the difference between purchase and sale prices of the securities, and represents in part profit for the undertaking of risk and in part compensation for the work performed in "originating the issue" and concluding the sale. Investment banking firms will be found in some communities with a population as small as 25,000, but are for the most part concentrated in the larger cities, particularly New York, Chicago, Boston, San Francisco, Philadelphia and St. Louis.

New England financiers and financial institutions contributed significantly to the early development of investment banking. Before the emergence of the specialized firm in the industry and of primary capital markets, New England merchants were leaders in establishing new sources of credit and actively participating in the creation of productive enterprises. They placed mercantile capital in New England textile mills and in railroad financing and other ventures on a national scale. They also established links among the several domestic capital markets as well as between domestic markets and those in London and on the Continent. During the period from 1840-1855 Boston became the nation's principal market for railroad capital. The region had large holdings of domestic capital and experience in financing its own railroad construction. It also had established a secondary market institution, the Boston Stock Exchange, and had a group of individuals and institutions experienced in purchasing locally issued bank, insurance and public obligations. Some of the firms now in existence trace their history to predecessors founded between the 1820's and the 1850's. These early firms laid the foundation for specialized functions in the capital markets.



SIX PER CENT. STOCK OF 1812.

(No. 253) *Bank of the United States, at* Boston 17 July – 1819

BE IT KNOWN, *THAT there is due from the UNITED STATES of AMERICA, unto* Samuel F B Morse of Boston *or* his *assigns, the sum of* One thousand Dollars *bearing Interest at Six per Centum per Annum, from the* first *day of* April 1819 *inclusively, payable quarter-yearly; being Stock created in pursuance of an Act of Congress, passed on the 14th day of March, 1812, entitled "An Act authorizing a Loan for a sum not exceeding Eleven Millions of Dollars;" the Principal of which Stock is reimbursable at the pleasure of the United States, at any time after the last day of December, in the year 1824; which debt is recorded in, and transferable only at, this Bank, by appearance in person, or by attorney, according to the rules and forms instituted for that purpose.*

Countersigned

1000 DOLLARS Sam Frothingham *Cashier.* Wm Gray *President.*

Chapter I

Financing Before the Civil War

Investment banking in the United States did not begin to emerge as a distinctive specialized function in the nation's capital markets until after 1860, and its later development paralleled the rise of the great industrial combinations of the late 19th and early 20th centuries.

The first half of the 1800's witnessed some major developments in American banking and business, developments which shaped our present institutional structure. In this period businessmen, bankers, and investors emerged as distinct groups and the separation of ownership and management of business began. Although considerable reliance was still placed on British and Continental sources of capital, and arrangements between the American and foreign capital markets were increasingly developed, an institutional structure for effectively utilizing American capital advanced rapidly. Commercial banks, private banks, insurance companies, brokers, and dealers in securities assumed the basic form and structure with which the financial system operates today. Another characteristic of the period was the financial and commercial rivalry of Boston, New York, Philadelphia, and Baltimore. Dominance in the capital markets shifted among these cities, being held by Boston from 1840–1855 before gravitating to New York.

Early Sources of Capital

In the first quarter of the 1800's there were few issues of securities and few investors. Securities were largely limited to a few government bonds and the common stock of insurance companies and corporations formed to build turnpikes, bridges, and canals. Some private banking firms continued to handle lotteries, which had become an accepted and important means of helping finance private as well as semi-public and charitable projects. The purchaser of the ticket gambled on a prize; the undertaking secured capital, and the seller received as a commission a percentage of the money raised. Among the lottery tickets sold in 1812 were those for Harvard College and Union College.

The story of S. & M. Allen & Company, established in New York in 1815, illustrates certain aspects of the early development of private banking. The firm established bank partnerships (the Allens and one or two resident partners in each branch house) in a number of cities including Boston, Providence, and Portland. Their chief interest was in selling lottery tickets and, in addition, they did business in bank notes, commercial paper and some foreign exchange. In the 1820's they began to deal in stocks and bonds, gradually discontinuing lotteries. The Allen partnerships were dissolved in 1837, but the partners and some of the clerks continued to operate as bankers and brokers. The Allen partnerships represent a transition from an enterprise which performed a variety of banking services to another that was more specialized and permanent and which contributed to the early development of the investment banking function.

In the early part of the century the most important business activity was foreign trade and shipping. Probably the greatest single source of capital was the merchant class, which comprised small country storekeepers as well as such wealthy metropolitan merchants and importers as Thomas H. Perkins in Boston, Stephen Girard in Philadelphia, John J. Astor in New York, and George Peabody in Baltimore. The merchant was trader, commission merchant, warehouseman, carrier, banker, and sometimes manufacturer. The capital and experience which these merchants accumulated, coupled with the introduction of machine manufacture and the increasingly widespread use of the corporate form of organization, brought about business and financial changes in the second quarter of the 1800's. Among the merchant's numerous functions, the supplying of banking services to the community led subsequently to the formation of private investment houses. These were the forerunners of modern investment banking houses, some of which are still important today. Merchants were often the leaders in chartered commercial banks, some of which made long-term advances directly to borrowers. Through long-term loans and frequently extended short-term notes, banks were, in reality, providing investment capital.

After 1830 American business activity began to spread inland from the eastern seaboard. The general merchant gradually gave way to the specialized businessman who often provided only managerial ability and looked to a new class of investors to provide capital. Nonspecialized merchant banking continued to exist and, as business increased, some firms began to drop other lines and become specialized private banks.

The careers of New England's China trade merchants like John Perkins Cushing, John Bryant, and William Sturgis illustrate the separation of ownership and management, the concomitant rise of the investor class, and the early development of investment banking. Upon retirement from trade about 1828 Cushing became a customer of Bryant, Sturgis & Company. The firm held Cushing's uninvested balances on which they paid interest, and managed investments for a fee. Cushing's investments, as well as the firm's own, were distributed during the 1830-1850 period primarily among firms with which Sturgis was personally acquainted. The extent of the investment in each firm was governed by a desire for wide diversification in the portfolio and maximum earnings. Many of the investments were in New England companies, but securities from the West and Mid-Atlantic regions were also included. In such fashion the capital of Cushing and other merchants was transferred from foreign trade to the country's internal development.

The formation of stock exchanges served the dual purpose of providing new capital and broadening the market for existing securities. In addition it prompted the transformation of the early commodity and share brokers into dealers in securities. The New York Stock Exchange was organized about 1792 and the Philadelphia Stock Exchange about 1800. By that time a considerable business in stocks had developed, reflecting the growth of corporations engaged in banking, insurance, manufacturing, and transportation. The late 1820's and the 1830's brought a great increase in the securities business. An exchange was formally established in Boston in 1834 which listed primarily stocks of New England manufacturing companies. Though by later standards these early stock markets were small and trading facilities primitive, they helped build up an investing public which was willing to provide risk capital for private economic development. This was particularly important in New England, where equity capital provided most of the funds for the textile industry and the development of the railroad network. Some of the trading in stocks was independent of both the brokers and the exchanges; it was handled by merchants as part of their trading operations and to a lesser degree by some of the chartered banks. After the 1830's "free banking" legislation by a number of states greatly encouraged the creation of new commercial banks and stimulated investment and trading in bank stocks; and in turn these banks performed an increasingly important part in assuring supplies of capital both directly and indirectly.

Origination of New Securities

New issues of securities were placed on the market by various methods. Some were sold directly to individuals. Others were offered to the public at some central meeting place where subscription books were opened. Large investors often requested brokers to subscribe for them, thus saving themselves the trouble of appearing in person. Brokers who anticipated an unusual demand for a particular issue would subscribe on their own account hoping to resell the stocks or bonds at an advance. Promoters offered concessions to influential brokers, hoping to secure the advertising value of their names. In this way, there gradually developed an affiliation between the broker and the issuer of new securities which contributed to the development of investment banking.

Small issues were sometimes handled by an incorporated or private local bank which disposed of its holdings through correspondents if the immediate market would not absorb all of the securities. In communities like Springfield, Worcester, New Bedford, and Hartford some securities, such as those of banks, transportation companies and textile mills were sold directly to local capitalists or banks who bought them not primarily as investments but to aid local enterprise. In the cases of comparatively small or family-owned industrial units, capital was provided privately and the firm was expanded out of profits.

Investors seeking more than a local or personal market came to rely on middlemen. This was especially true for securities originating in the West or other areas far removed from the financial centers. The securities sold in the financial centers were primarily federal and state bonds, issues of canal and railroad corporations, and shares of banks and insurance companies. In spite of the development of the stock exchanges, there was no large class of investors capable of exercising independent judgment in the selection of their investments. The brokers or private bankers distributed the securities within their own communities, to capitalists with whom they were in touch or to agents like themselves in other cities. In this way something like a regional and even national system of security marketing developed without any one centralized market. For example, William Sturgis of Bryant & Sturgis of Boston bought bonds and stocks through Prime, Ward and King of New York, thus entering into a larger decentralized domestic market.

European Capital and American Development

In Europe the investment banking function had become specialized much earlier. Fortunes amassed in the 18th century by Europe's mercantile interests enabled those concerns to devote their primary efforts to investment banking as early as the 1780's and 1790's. The House of Baring in London is an excellent example. Using wealth accumulated mainly in mercantile pursuits, this family organized its investment banking enterprise in 1763. Potentialities for American economic growth attracted its attention from 1790 onward, and the financing of American trade and the marketing of American securities was its major interest from 1828 to 1861.

In the late 1820's and the 1830's promotion of new enterprises gained considerable support from foreign capital. British and Dutch investors, encouraged by the high yields on American securities, developed a strong interest in investments in the United States. They purchased stock of the Second Bank of the United States, state bonds, Erie Canal bonds and early railroad securities. Close relations were built up between American and foreign merchant bankers who purchased American securities for retention, or for distribution among foreign investors. A number of these foreign houses established branches in the United States and developed a clientele among wealthy merchants in eastern seaboard cities. In Boston the Barings used Thomas Ward and later Thayer & Brother as their agents, thus establishing the close relationship which still exists with Kidder, Peabody & Co. — the successor firm to Thayer & Brother. The Hopes of Amsterdam and the Hottinguers of Paris, among others, also had one or more agents or correspondents.

American Securities Owned Abroad in 1853
(millions of dollars)

	Total Outstanding	*Foreign Owned*	*Percent Foreign-Owned*
United States	$ 58.2	$ 27.0	46
States	190.7	111.0	58
Counties and cities	93.3	21.4	23
Railroad bonds	170.1	43.9	26
Railroad stocks	309.9	8.0	3
Banks and insurance	279.6	7.1	3
Canal and navigation	58.0	2.5	4
Miscellaneous	18.8	1.1	6
	$1,178.6	$222.0	18

Source:
33rd Congress, 2nd Session, Executive Doc. 42. See also Myers, *New York Money Market*, Vol. I, p. 36.

Demands for capital were heavy during the period of internal development and railroad extension between 1850-1860 and the amount of securities held abroad increased more rapidly than in any other decade before the Civil War. State securities held first place in volume although some of them were repudiated issues purchased before 1840 and held unwillingly. The railroad securities, which ranked second in amount, had been purchased after 1838 and most of them after 1840.

State and Municipal Securities

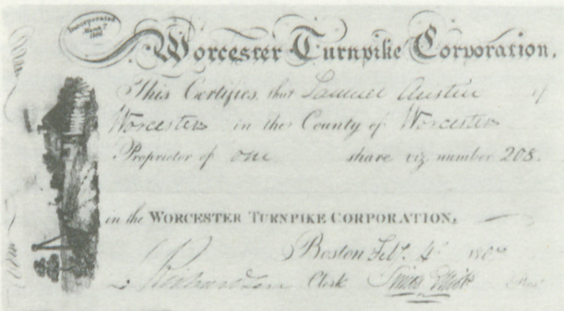
Debts of the various states were assumed by the federal government in 1790, and from that time until 1830 long-term state and municipal securities issues were relatively rare. By 1830, however, the demand for improved means of transportation and the expansion of the banking system were creating an ever-growing demand for capital. By 1841 state debts totalled $231.7 million and municipal debts had reached $27.5 million. Nearly two-thirds of the borrowings were used to finance the building of railroads, canals, turnpikes, and bridges, and most of the remainder used to capitalize banks.

Similar building programs in New England were financed with much less long-term borrowing. Connecticut, New Hampshire, Rhode Island, and Vermont had no state debts as late as 1841. Maine issued $1.7 million of debt between 1837 and 1841 for general purposes including schools, hospitals, and expenses incurred during the northeastern boundary difficulties with Great Britain. Massachusetts issued $6.5 million of securities in the same period to aid railroads, principally the Western Railroad. In 1841 Boston's debt was $1.5 million; that of Providence, $222 thousand.

From 1840 to 1860 various governmental units, mostly municipalities, financed public improvements and aided railways either by purchasing their securities or by issuing securities on their behalf. This policy of state and local support of internal improvements was not a break with past tradition, but merely a modification of policies initiated in colonial times. It had been common practice for states and cities to grant monopoly privileges to aid private ventures which held the promise of increasing the economic strength of the community. In 1667, for example, the Massachusetts General Court, by resolve, offered a 21-year monopoly to anyone who would build a drydock.

During the two decades preceding the Civil War, Massachusetts was one of the few states which continued to support railways; by 1860 Massachusetts had devoted some $7.3 million to railroad development. In areas where state governments refused support, localities aided the railways they hoped would bring permanent prosperity to their communities. Prior to 1860 towns in Massachusetts spent $228 thousand in support of railroads. In Maine, Portland contributed $2 million to the Atlantic & Northeastern. In Rhode Island and Connecticut, local aid was lavishly given. Hartford, Bridgeport, New London, Norwich, and Providence contributed heavily to the railroads.

Massachusetts and Boston retained their ties with the London house of Baring Brothers, which marketed large portions of their issues. In instances where cities exchanged their securities for those of a railroad, the railroad company undertook the problem of marketing the city issue. In most cases the government securities were given by the railroad company to contractors in payment for work performed, in which case the contractor had to market the securities or use them as collateral for commercial bank loans.


Worcester Turnpike Corporation.
This Certifies, that Samuel Austin of Worcester in the County of Worcester Proprietor of one share viz. number 208.
in the WORCESTER TURNPIKE CORPORATION.
Boston Feb. 4
Clerk

Local banks were a major market for state and local government securities since they were often required by law to hold some of these securities as a reserve against their note issues. The practice of selling municipal bonds to local banks and individuals without public notice gave way, as the issues became larger, to the advertising of new issues and their sale on a competitive basis. Blocks of these bonds were purchased for resale by individuals and institutions, and these intermediaries, therefore, performed in a small way the function of the modern investment banker. By the outbreak of the Civil War outstanding state and local issues in the nation totaled about $200 million each.

Development of Textiles in New England

In the second quarter of the 1800's New England's financial institutions moved more rapidly toward specialized functions. Specialization was, in turn, accompanied by the development of closer working relationships between institutions. This factor, along with the tendency to concentrate available capital in the more promising enterprises, was a notable stimulant to cotton textile manufacturing and the inland extensions of eastern railroads.

Concentration of resources in cotton manufacturing made it the first American industry to feel the full impact of the Industrial Revolution. By 1860 cotton manufacturing represented a capital investment of over $93 million, of which over $65 million, or 6 percent of the $1.1 billion total capital investment in all industries in the nation, was in the New England states.

Particularly important in New England was the "Massachusetts" type of textile mills such as the Amoskeag, Boston, and Lawrence, which were large integrated operations as compared to the small, single-operation ("Rhode Island" type) mills that prevailed in other areas. Unique in the capitalization of these integrated mills was the heavy reliance on equity financing. Heretofore, only small local industries had been able to attract equity capital.

Stock sales provided almost all of the original capital for the integrated mills. During the three decades from 1829 to 1859 mercantile groups provided about one-half of the original equity. Non-textile merchants and firms subscribed to one-third of the new issues. Individual holdings ranged from $2,500 to $200 thousand. Less numerous, but with larger individual investments, were the textile merchants, who bought about 17 percent of the dollar volume of new issues during the late 1830's and early 1840's. In addition to making an investment they assured themselves of a supply of merchandise. To some extent, shrinking returns from foreign trade led merchants to turn to textiles because they were the only important alternative investments available. More significant, however, was the favorable profit record of 9 to 10 percent on capital stock.

Financiers also performed an important function by supplying large textile firms with new equity capital from their own funds. Individual investments averaged about $10 thousand, and the investors included bank officers, insurance company officials, brokers, and private bankers. Indications are that their investment policies were strongly influenced by current profits shown by the industry. Particularly striking were the almost complete absence of foreign capital and the very small amount from other parts of the United States. Essentially, textile firms were locally financed.

Many financial institutions received their first experience as intermediaries in equity financing with the textile industry. Insurance companies acquired stock as a permanent part of their investment portfolios. Commercial and savings banks acquired the stocks as collateral on loans and sometimes took title as a result of forfeited loans. Brokerage firms frequently purchased textile stocks for resale. As a group, however, institutional investors did not often buy new issues from the issuer, but were typically a part of the secondary market. In this way, they freed the funds of individuals who in turn provided the primary market for investment in new issues.

The mills also secured capital through long-term loans. Savings banks and trust companies were the chief suppliers, making loans for as long as 10 years and supplying about 70 percent of the total funds for loans. The remainder was largely supplied by individuals, most of whom were retired merchants.

The record suggests that experience with these mills proved equity capital to be a sound means of financing large industrial developments. Individuals and financial institutions gained experience in investing in, and acting as intermediaries for common stock issues. For the first time in America it was demonstrated that a large industry could be financed without substantial foreign assistance. Generally satisfactory results, both in safety and return on capital, advanced the use of equity financing in later years.

Railroad Financing in the Nation and New England

During the 1830's, the first decade of railroad building and the greatest period of canal construction, three techniques were used to finance railroad projects. Most important was the use of government funds, either directly in state-built projects or indirectly by grants of state credit to assist private transportation companies. The latter was accomplished by the sale of state bonds for cash and the use of the proceeds to buy the securities of private companies, by the exchange of state for private obligations and by state guarantee of private bond issues. Sterling bonds issued specifically for the English investment market was a second way for private companies to raise funds. The stock share was used infrequently except in New England.

Railroad finance of the 1830's was dominated by the pattern set by Philadelphia. The middle Atlantic and midwestern states all depended heavily on bonds issued either by the states or by the companies themselves to pay for construction of their transportation systems. They also tended to rely on Philadelphia, either through individuals like Moncure Robinson or through the Second Bank of the United States, for assistance in marketing bonds in England. As long as England considered American securities a good investment, such financing was possible.

The panic of 1837 and the resulting depression delayed the development of transportation in Pennsylvania and the states to her south and west. After the collapse of American credit the English market would no longer take American bonds, public or private. Between December 1840 and December 1846, only 86 miles of railroad were reported as having been constructed in Pennsylvania, and even fewer in New Jersey and the seaboard states south to Georgia. With the depression, and the closing of the Second Bank, Philadelphia lost her dominant position in American transportation finance. New York's function as an important market for railroad stocks also ended temporarily in 1837.

The rail promoters of New England suffered less than those of Pennsylvania and other states to the south primarily because during the 1830's they had been far more self-reliant financially than their neighbors. Stock issues rather than loans had paid for the first railroads in the area, and by far the largest portion of the stock was sold in communities along the rail lines.

Boston Dominance in the Nation's Capital Market

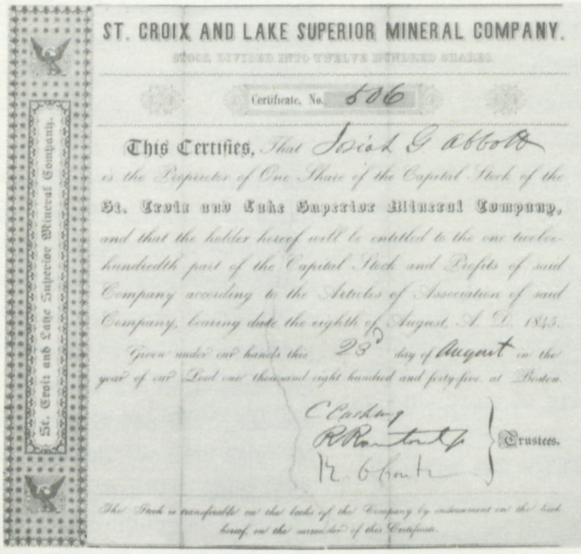
New England, in general, suffered less than any other section of the nation from the depression of 1837 and was also the first region to recover. Prosperity encouraged the building of more shipyards, more textile mills and especially, more railroads. Between 1845 and 1850 the region's basic rail network was completed. Almost two-thirds of the 3,660 miles built in the region in the 30 years before the Civil War was constructed between 1845 and 1851. Boston financed the railroad and industrial expansion of New England in the 1840's and in doing so, quickly became the center of American railroad finance. Roads to the south and west, which had depended on Philadelphia, New York and England for financial support, now turned to Boston. The two most important Pennsylvania roads, the Reading and the Philadelphia, Wilmington & Baltimore were reorganized and revived in the mid-1840's with the aid of Boston capitalists and Boston capital. Such prominent New Englanders as David A. Neal, John E. Thayer, Nathan Appleton, and William Sturgis became closely identified with the Reading, and by 1849 its control resided in Boston.

During the early 1840's the railroads in central New York associated with Erastus Corning also looked to Boston for aid, establishing relationships with John E. Thayer and J. M. Forbes who helped market securities in Boston. In 1845 Thayer and Forbes joined with Corning to purchase the Michigan Central from the state, and in the following years financed its construction across the state to New Buffalo on Lake Michigan. By 1852, the line had been extended to Chicago, making the first all rail connection between Chicago and New York. At the same time the New Englanders Samuel Henshaw and William Ward reorganized the Mad River & Lake Erie Railroad in Ohio.

Before 1850 the buying and selling of corporate securities were generally handled on a personal level. It was on such a basis that Stockton, Robinson and others raised funds for the roads in the middle Atlantic states in the 1830's. During the next 10 years railroad promoters of New England and the West who came to Boston for funds dealt personally with individual capitalists who were likely to influence others. Such moneyed men were willing to invest their funds in these railroads because they had firsthand acquaintance with the conditions, prospects and, most important, the management of the roads. This became less and less true after 1850 as the number of roads increased; with nearly 100 instead of a dozen trying to raise money, the individual promoters faced increasing difficulty in obtaining capital from personal acquaintances. Nor could investors in the East and in Europe easily contact the officials of the road for the purpose of purchasing its securities. Still fewer were their chances of knowing its management personally. Both the users and suppliers of capital soon found it advantageous to rely on specialized banking firms. In New York the firm of Winslow, Lanier & Company and in Boston the firms of Henshaw & Ward and John E. Thayer & Brother specialized in buying and selling rail securities. Reliance on intermediaries made it possible to tap a larger number of investors, and the investors themselves were provided with a wider choice of securities.

The institutionalization of the investment market for railroad and other securities also led to its centralization in New York. The city exploited its combination of geographical advantages in oceanic, coastal and inland shipping, becoming of first importance as a commercial center. The earlier personal investment was bound to be predominantly local, with each large city providing the capital required by its radial roads. Only

Boston, Philadelphia, and New York financed more distant roads, and New York before 1850 had been much less active in railroad finance than either Boston or Philadelphia. In 1850 Boston listed on its exchange many more securities for railroads outside its region than did New York. By 1857, however, far more railroad securities were listed in New York and these included nearly all the important roads in the nation. Boston and New England capital and capitalists, however, continued to be an important influence in the development of railroads to the West.


ST. CROIX AND LAKE SUPERIOR MINERAL COMPANY.

STOCK DIVIDED INTO TWELVE HUNDRED SHARES.

Certificate, No. 506

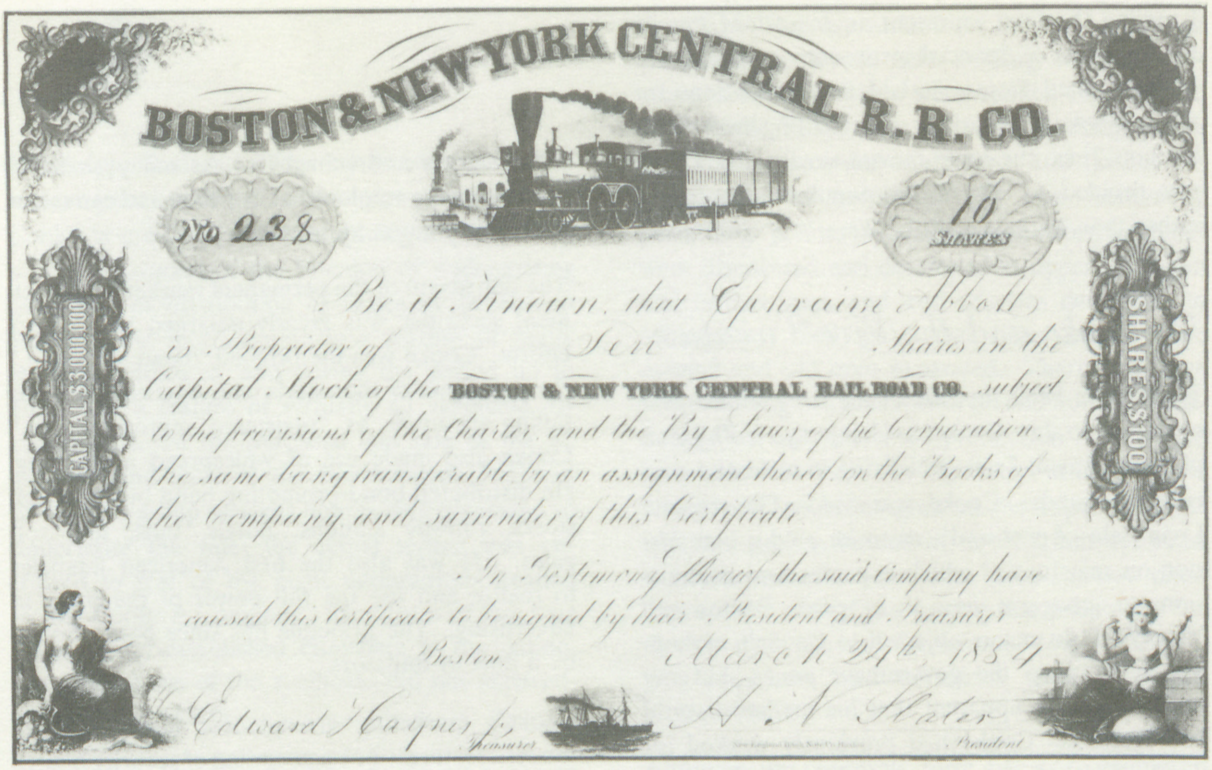
This Certifies, That Josiah G Abbott is the Proprietor of One Share of the Capital Stock of the St. Croix and Lake Superior Mineral Company, and that the holder hereof will be entitled to the one twelve-hundredth part of the Capital Stock and Profits of said Company according to the Articles of Association of said Company, bearing date the eighth of August, A. D. 1845.

Given under our hands this 23d day of August in the year of our Lord one thousand eight hundred and forty-five, at Boston.

Trustees.

The Stock is transferable on the books of the Company by endorsement on the back hereof, on the surrender of this Certificate.

St. Croix and Lake Superior Mineral Company.



Chapter II

The Civil War and Subsequent Expansion

The Civil War marked the end of the first period of development of American capital markets and their institutional framework. During the years immediately preceding the war, banking and other forms of financial organization moved toward greater specialization, and large scale activity became increasingly centered in New York. By the time of the war, investment houses had developed in Boston, New York, Philadelphia and a few other cities, which purchased large blocks of municipal and railroad securities for their own accounts and for later distribution among their clients. Partners of some of the houses had promoted or participated in the promotion of the railroads whose securities were purchased. Moreover, a number of strong commercial banks had developed which co-operated with each other and private bankers in purchasing issues — part of which they retained and part sold. This institutional framework became important in the financing of the Civil War.

The pressing financial needs of the war led to huge borrowings by the federal government. Funds had to be raised largely in the domestic market because the unpopularity of the Union cause abroad had practically closed London and Continental markets. The earlier war issues were floated through competitive bids, a method which had been used in 1847 and 1848 in financing the war with Mexico. Tenders were received from individuals and banks — all of them from the East, and most of them from New York, Boston, and Philadelphia. In Boston, the Merchants Bank assumed a key role in selling the bonds of the early loans in New England.

The loan act of 1862 provided for a huge long-term federal borrowing — $500 million at 6 percent. The 20-year bonds were callable in five years and thus became familiarly known as the five-twenties. The sale of the five-twenties was an unprecedented operation, and the mechanics of handling the loan represent an important step in the evolution of financial institutions and practices in the United States. It laid the foundations for the business of securities underwriting and distribution. Since the issue moved slowly, the Treasury decided to appeal to popular subscription rather than bargain with banks.

Jay Cooke and the Five-Twenties

In October 1862 the sale of the five-twenties was entrusted to Jay Cooke & Company, a Philadelphia investment firm specializing in state and government bonds. Cooke was made Government Loan Sales Agent and was to be paid a commission on sales out of which expenses and commissions to subagents were to be paid. Boston and New York financiers objected to Cooke's monopoly in handling the government issues, but not until it became apparent that his methods would be successful. Cooke had previously worked for E. W. Clark & Company, a Philadelphia house with branches in important cities including Boston. With this firm he had acquired experience through marketing the Mexican War Loans and Missouri and Illinois state issues, as well as those of a number of municipalities. The firm had also been active in railroad finance and the sale of western lands. All these operations contained elements of modern syndicate procedure, as had transactions by firms in New England and elsewhere. Associations of firms had purchased securities without assuming joint responsibility in sales or in management of the sales.

In handling the five-twenties Cooke drew upon his experience and imagination. He created an organization for distributing the bonds which put into association for the first time virtually all the retail and wholesale security distributors in the nation, as well as banks and insurance companies. In the East, a number of the firms were given some responsibility for setting up and managing the selling organization in their areas. In Boston, Spencer, Vila & Company provided very active support as did Brewster, Sweet & Company, general agents for New England. The bonds, which were issued in both large and small denominations, were distributed widely and there were in all some 2,500 agents and subagents. As many as 5,000 salesmen were employed at one time and canvassed the country house by house.

The dimension of the permanent market for investment securities was greatly enlarged by Cooke's efforts. Cooke was the original "bond salesman," the prototype of thousands who now earn a living selling securities as "registered representatives." Cooke also made use of widespread advertising. He distributed bond-promoting hand bills through stores, railway stations, hotels, inns, and toll gates. He was also the first American financier to realize and use the full power of the press in advertising. The principle has since been applied by a host of imitators.

Cooke's marketing arrangement involved three modern features: (1) association of security houses under central direction, offering different services for the purpose of having outlets in every possible area, large or small and (2) the energetic solicitation of the individual investor and (3) maintenance of the price of the bonds during the distribution by entering the market to buy and sell, using his own as well as Treasury funds.

Not only did the Civil War place extraordinary demands on the financial capacity of the Union Government, but state and local governments also were required to raise money for war purposes. Many bond issues were made in order to equip local regiments and to pay benefits to troops and veterans. The $47 million raised by the New England states was about 42 percent of the amount raised by all northern states. Unique in the history of Civil War finance was the effectiveness of Boston and Massachusetts in securing funds in the London money market — some $9 million. In addition, Massachusetts was the only state to maintain specie payments on both interest and principal throughout the war.

Late in the 1860's Jay Cooke & Company and E. W. Clark & Company brought investment banking still closer to modern underwriting by their joint purchase of bonds of the Lake Superior and

Mississippi Railroad. The bonds were also sold under joint account with joint management. Cooke is credited with introducing the next step — the separation of the function of underwriting from that of distribution of issues in the United States. This specialization is a feature of many modern syndicates, and during the period up to 1934 was a feature of virtually all syndicate arrangements. In the purchase and sale of the $2 million bond issue of the Pennsylvania Railroad in 1870, a group of eight houses was organized to underwrite the sale; the actual selling was entrusted to five of the eight underwriters headed by Jay Cooke & Company. Syndicates of this type were shortly established elsewhere in the nation, but general use of the syndicate did not materialize until the 1880's.

After the depression of 1873 syndicates began to shift to specialization of function in underwriting and wholesaling securities. In sales, the emphasis changed from soliciting the individual investor to soliciting the institution. Commercial banks began to devote an increasing part of their resources to the purchase of bonds, largely because of the attractiveness of new security flotations through syndicate participation and because of the value of association with corporate borrowers in times of good business. In addition to investment bankers, insurance companies, commercial banks and trust companies, as well as individuals, participated in the syndicates.

General Economic and Financial Developments

During the Civil War and early postwar years the financial and economic development of the United States broadened and deepened. Geographic expansion continued to be a dominating element in American economic development and such expansion naturally increased the area of production. Railroad building was accelerated as roads linked the East and West Coasts; and between the war and 1893 more than 150 thousand miles of track were laid. Rail networks were developed through consolidation, leases, and holding company devices. New coal mines were opened in the East. New textile mills, shoe factories, packing plants and iron works were established; and further development was encouraged by new technology permitting greater specialization. Copper mines were discovered and developed in upper Michigan and farther west, and iron ore was developed in Minnesota. New gold and silver mines were opened and old ones expanded. There was large scale building of roads, factories and houses. Technology not only increased production but brought into existence one new industry after another. Many new industries grew at the expense of the old, and profits, instead of flowing into the same channels year after year, were shifted to new ones. Toward the end of the century the telephone, the electric dynamo, and the internal combustion engine appeared, and industries soon developed around them.

Although the corporate form had been employed to an increasing extent since 1800, it was not until the development of rapid and cheap transportation systems that it became the dominant form for mercantile and manufacturing enterprises. During the early years of its history the factory system did not require large aggregates of capital — markets were for the most part narrow and local, transportation inadequate and wealth and population decentralized. The period after 1873 was marked by a great increase in the number of industrial corporations, reflecting the insistent pressure of wider markets as transportation improved, population increased and technological change made large scale production possible. The growth of small corporate industrial enterprises laid the basis for the spectacular development which began toward the end of the century — the consolidation and trust era.

The national banking system was established, bringing about a closer federation of the banking system. The National Bank Act of 1863 also continued "free banking," thus insuring continued expansion of facilities. It marked the close of the period of state banking which had failed to provide much in the way of uniformity or distribution of banking strength. The courts authorized national banks to purchase corporate and municipal bonds in addition to government obligations. This authorization carried the implication of power for further dealing in bonds.

Development of Investment Banking Houses

During the 1880's the sale of corporate securities for industrial concerns was taken over by investment bankers already familiar with U.S. government securities and those of railroads. Small enterprises like the operating telephone companies continued to raise funds locally but the larger units turned to financial centers to supplement retained earnings with funds for expansion through security issues. The investment bankers who met this need fell into two broad groups. In the first group were strictly domestic firms, most of which were located in the older cities on the eastern seaboard. Some, however, began to develop in the growing West, centering in Chicago and St. Louis.

A second group of houses which came into prominence after 1873 — one or two each in Philadelphia and Boston and several more in New York — had important international connections. These houses began establishing branches abroad; and many of these relationships have continued to the present time. The branch in some instances was an outgrowth of an earlier correspondent relationship. These houses were in a favorable position to direct the flotation of new securities and became the main channels for capital from abroad.

During the last quarter of the century many houses began to specialize in serving a particular industry and to develop continuing relationships with certain companies within those industries. In this process these houses became central sources of information about the industries and the firms with which they were associated. They facilitated the market for securities of particular companies and, in many instances, carried limited trading positions. Specialization of the function of investment firms emerged. Some firms limited their operations to originating and wholesaling new issues. They carried out the work of investigation, formulated the contract for handling the issue and disposed of the securities to other houses for sale to the public. Retail firms also developed which acquired securities for both their own accounts and for resale. In both functions, the firms tended to specialize in one type of security — railroads, municipals or governments.

Further Development of Railroad Finance

As noted earlier, New England capital and Boston investment houses had supported the construction and development of a number of railroads not only within the region but in various parts of the nation. Until about 1850 railroads were built as short lines and were essentially local in nature. The roads had been promoted by merchants in the eastern seaboard cities who had accumulated substantial capital, by local manufacturers at inland points who viewed the road as extending markets, and by "chief citizens along the line" who wanted the prestige of connection with enterprises promoted by the metropolitan businessmen. After 1855 and up to the Panic of 1873, local roads were frequently brought together to form through-lines between large cities. By 1873 almost 70 such consolidations, each of more than 200 miles in length, had been accomplished. In the majority of cases, particularly after the Civil War, new track was laid to complete unfinished lines going into the consolidation and to build new sections. Among the consolidations in which New England capital figured prominently were the Burlington & Quincy — merging the Chicago & Aurora and the Central Military Tract Railroad — and the Union Pacific serving the West. New England houses were instrumental in the consolidation, in 1873, of the New York and New Haven and the Hartford and New Haven into the "New Haven."

After the Panic of 1873, with the growth of competition, further consolidation of the railroads was undertaken with the specific purpose of developing railroad systems which would be unified and independent. The objective was not only to main-

Office of F. S. Moseley.

Note Broker. 51 State Street.

Boston. Jan. 25th 1887

C. A. Chase Esq. Treas.

Dear Sir

I can offer subject to sale

$50000 1 yr 4 1/2

Lee, Higginson & Co.
H. L. Higginson.
Chas Fairchild.

420 shares Eastern R. R. preferred stock as collateral. this has just been issued in place of the old 6% bonds, which were a savings bank investment you will remember. The stock sold today at 141 1/2 Mr. Oliver Ames will take $50000 for a year at 4 1/4 and will give Oregon Short Line bonds, Northwest stock or some first class Collateral with ample margin. Please telegraph me about these

Very truly

F. S. Moseley
Bowen

tain but to increase traffic. Boston businessmen and the Boston investment house of Kidder, Peabody gained control of the Atchison, Topeka and Santa Fe in 1872, then running 218 miles from Atchison to Hutchinson, Kansas, extended it to Pueblo, Colorado, and later connected it with the Southern Pacific, thus creating a considerable portion of a second transcontinental road. By 1888, the Santa Fe was an important union of several rail systems serving an extensive territory in the Mid and Far West. By 1892, the road was over 9,000 miles in length, one of five systems exceeding 5,000 miles. Systems had become even more fully developed by 1893 — some 35 roads possessed mileage of more than 1,000 miles. After 1893 and until World War I further consolidation and substantial reorganization of some of the railroads was accomplished, eliminating duplicate facilities.

Between 1880 and 1914 Boston houses participated as members of syndicates not only for the roads cited above, in which ownership and control was chiefly lodged in their city until the late 1880's, but for the bonds of the Boston Terminal, Boston and Lowell, Fitchburg, Bangor and Aroostook, Long Island, Baltimore and Ohio, Louisville and Nashville, Chicago Junction, Illinois Central, St. Louis and San Francisco, Great Northern, Northern Pacific, Utah and Northern, and Oregon Short Line railroads. Alone, the Boston houses placed several issues of these securities.

Boston's Early Stock Specialties

Prior to 1880 the market for industrial securities was generally narrow in the principal financial centers. Moreover, such securities were relatively few in number, ownership tended to be closely held and shares were only infrequently offered for sale to the public. An exception to this pattern was to be found in the cotton textile industry of New England. Here, as noted earlier, the corporate form had become prevalent and ownership was quite widely dispersed. Trading and listing of these shares on the Boston Stock Exchange had increased from 17 companies in 1835 to 46 companies in 1855.

Almost all the country's early mining enterprises took the form of proprietorships, with some exceptions in copper and coal mining. During the 1860's the copper resources of the upper Michigan Peninsula were developed by New England capital. Most famous of the mines were the Calumet and the Hecla. A number of Boston houses became specialists in copper securities in the 1870's and 1880's, among them Paine, Webber & Company, Bright, Sears & Company, and Lee, Higginson & Co. A number of new firms were also formed to deal in coppers and Boston became the world's chief market for copper mining securities. Over 62 companies were listed on the Boston Stock Exchange between the late 1860's and 1880's, many of which had been promoted and developed with New England capital. Among these were the Wolverine, Mohawk, Winona, Phoenix and Michigan Copper companies. Some of the companies were of substantial size for the period.

Probably the earliest consolidation in the copper mining field was that of the Calumet and Hecla mines in 1871 with the aid of Lee, Higginson. Subsequently these mines became extremely profitable. By 1907 one share had returned 90 times the purchase price in dividends and sold for 110 times cost. The consolidated company was controlled in Boston, and for over 40 years Alexander Agassiz, discoverer of the deposits, and Quincy Shaw, another Bostonian, held the majority of the stock. The corporation maintained its principal office in Boston until 1955. The original capital of \$1.2 million was supplied by H. L. Higginson, H. Russell, Quincy Shaw and John Simpkins. Lee, Higginson became its investment banker and a central point of information about the company. The stock was eventually widely held through New England, with large holdings in Boston.

New England continued its interest in copper securities, and in the early 1900's was instrumental in financing the Copper Range Consolidated Company and the Inspiration Consolidated Copper Company. The Copper Range Company merged Baltic Mining Company, Trimountain Mining Company, Champlain Copper, Michigan

Smelting, and the Copper Range Railroad Company. It produced 30 per cent of Michigan's annual output by 1904. Later the company integrated smelting and manufacturing operations as well.

Early Application of the Holding Company

The trend toward the large American corporation began in the 1880's and accelerated rapidly after 1897. A great variety of enterprises were brought forward as offering favorable opportunities for investment. None had greater popular appeal than those which combined firms within expanding industries. The demand for capital was prodigious. In New England this activity was reflected in a number of fields — utilities, foodstuffs, machinery, textiles, and banking. Many of the corporations now in the forefront of American business were formed in this period and their initial development and financing provided by investment bankers as well as individuals in New England.

The holding company is characteristically an American institution, and the first pure holding company in the utility field — American Bell Telephone Company, predecessor of the American Telephone and Telegraph Company — created by a special Massachusetts charter in 1880, was financed largely with New England capital. As late as 1894 about 85 percent of the stockholders were residents of Massachusetts. The corporation was empowered to hold stocks in other corporations doing business under telephone patents. Local or subsidiary corporations were established to develop telephone systems over limited geographical areas, and the capital was secured by local subscription. The holding company exercised control through contracts and control of shares delivered for the use of equipment. Later, collateral trust bonds were sometimes publicly offered. In the telephone business, early control of Bell patents, together with the advantages of a unified system of country-wide communication, made the holding company a valuable device for developing the industry rapidly on a large scale with relatively small capital outlays. The basic policy of controlling associated companies as it exists in the AT&T system today was formulated in the 1880's by a Bostonian, William Forbes, the president. Virtually from the outset, the telephone company used New England houses as investment bankers in public offerings — Kidder, Peabody; R. L. Day & Co.; Brewster, Cobb & Estabrook; and Lee, Higginson. The company early made use of privileged subscription, a practice still followed today. Kidder, Peabody has carried out more telephone financing than any other house in the nation.

Early application of the holding company was also made in the development of the General Electric Company, which was based on the merging in 1892 of the Thompson-Houston Electric Company of Lynn, Massachusetts, and the Edison Electric Company in New York. Lee, Higginson, which aided in this formation, had been banker to Thompson-Houston. The consolidation was accomplished by a direct exchange of shares. Thompson-Houston had been one of the earliest industrial companies to use preferred stock, with the issue distributed privately by Lee, Higginson. During the early experimental years, the growing electric equipment companies found it difficult to market their generating station and power distribution equipment. Financial interests were generally doubtful of the success of the light and power industry and provided little financing. Consequently, the equipment manufacturers decided to support their potential customers. This was accomplished by the use of holding companies, of which the United Electric Securities Company was one of the earliest and most successful. It had been created in 1890 by Thompson-Houston, which used the securities company as an "assumption company" to acquire stocks and bonds of the utilities which the company had received in exchange for its equipment, thus providing financial assistance to the operating utility. The holding company then issued collateral trust bonds which were marketed publicly. In 1904 the General Electric Company created a new and larger assumption company known as the Electrical Securities Corporation. Later the Electric Bond and Share System was developed by General Electric interests with the intent of some control of operating utilities.

Arthur Perry, the officer in charge of the bond department of Thompson-Houston and later General Electric, and two associates in the utility field, founded the firm of Perry, Coffin and Burr in 1898. This house, forerunner of the present Coffin and Burr, Inc., was one of the first to underwrite and market utility issues on a broad scale in the United States, becoming known as a specialist in these issues. They were also bankers for the United Electrical Securities Company. Between 1900 and 1913 the firm underwrote and distributed issues for utilities across the nation. Among them were the Southern California Edison Company, Portland (Oregon) General Electric Company, Detroit Edison and Consumers Power Company in Michigan, Fort Worth Power and Light, Alabama Power and Central Maine Power. The firm also placed some large Canadian issues. Early in the 1900's, the house worked closely with N. W. Harris & Company in Chicago. Having originally interested the Chicago house in utility financing, Perry, Coffin and Burr shared many large issues with them. Arthur Perry and Company, founded in 1915, continued in the utility field as did Coffin and Burr.

Jackson and Curtis were also well known in the utility field and were bankers for the Electrical Securities Corporation. Later the two G.E. securities companies were united under continuing G. E. management and Jackson and Curtis headed the managing underwriters which included two New York firms, Bankers Trust Company, and Kissell, Kinnicut. The firm of Baker, Ayling and Young of Boston was instrumental in working out the early financing necessary in developing the power network in the upper Connecticut River valley beginning about 1910.

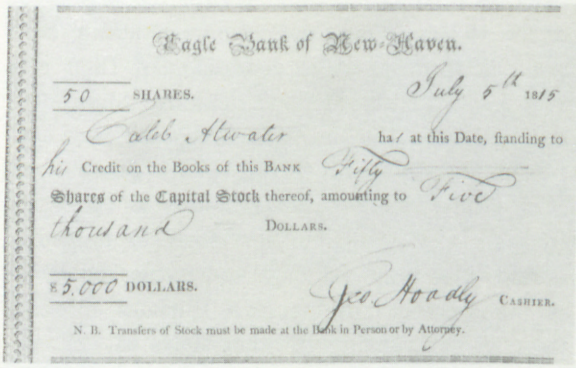
The original Boston firm of Stone & Webster, a holding company widely known in the utility field, began operations in 1889. It was the first service organization to develop in the electric power industry. In addition to construction work, it formed a supervisory organization and a financial advisory service for operating utility companies during the 1890's. In this latter capacity it employed investment banking houses in Boston to syndicate and provide for distribution of its clients' bonds. About 1900 a small department was formed in the Stone & Webster organization to market utility common stocks. The department grew and in 1927 became Stone, Webster & Blodgett, Inc., through the absorption of Blodgett & Company, and the head office moved to New York. This house specialized in syndicates and in dealing in utility securities. Today it is known as the Stone & Webster Securities Corporation.

Consolidations and Recapitalizations

The holding company, because of its ease as a consolidating device, was used in the formation of the General Motors Company — one of the largest and most important consolidations in the industrial field in the early 1900's. It brought under centralized direction the manufacture of 12 different makes of automobiles. Shortly after its formation in 1908 James J. Storrow of Lee, Higginson, as chairman of the Finance Committee of General Motors Company, was the dominating factor in recasting the financial structure and developing a plan for improving the operation of the constituent companies. Associated with Lee, Higginson in this move were two New York houses, J. & W. Seligman and Company and Kuhn, Loeb.

The H. B. Claflin Company of New York, which had been the largest dealers in wholesale dry goods since 1843, was reorganized and expanded in 1890 with the support of Blake Brothers, a Boston house, in the offering of $3 million of common stock. An early venture into Canada involved the consolidation in 1893 of four soft coal producers on Cape Breton — Little Glace Bay, Gowrie, Caledonia, and International companies — into the Dominion Coal Company, with transportation and marketing arrangements for New England and other regions. Kidder, Peabody offered the $1.5 million of securities for the financing.

One of the first large consolidations of banks


Eagle Bank of New-Haven.

50 SHARES. July 5th 1815

Caleb Atwater has at this Date, standing to his Credit on the Books of this Bank Fifty Shares of the Capital Stock thereof, amounting to Five thousand Dollars.

$5,000 DOLLARS. Geo Hoadly Cashier.

N. B. Transfers of Stock must be made at the Bank in Person or by Attorney.

occurred with the merging of eight national banks in Boston into the National Shawmut Bank in 1898. Kidder, Peabody formed a syndicate to take over certain assets excluded from the consolidation. The syndicate was familiarly known as the "Bank Stock Deadwood Syndicate."

Other nationally known corporations were consolidated or merged with the aid of New England capital and under the sponsorship of Boston houses. Among these were Chicago Union Stockyards (1889), Chicago Junction Railway and Union Stockyards (reorganization, 1890), American Sugar Refining (1890), Westinghouse (reorganized, (1891), P. Lorillard (1891), United Fruit (1899), American Writing Paper (1899), New England Cotton Yarn (1899), U. S. Smelting, Refining and Mining (1906), and Massachusetts Gas (1909).

Some of the unincorporated companies as well as the relatively small industrial corporations arranged recapitalizations or offered securities for public distribution. Others offered new issues for expansion. Procter & Gamble, a family-owned partnership, was converted to a corporation in 1890 and offered common and preferred stock and some bonds to the public under the sponsorship of Kidder, Peabody in Boston and Morehead, Irwin in Cincinnati. A closely held corporation founded in Massachusetts in 1780, Walter Baker & Company, Ltd., a name which became a household word for chocolate and cocoa preparations, offered its capital stock for public distribution in 1898 with the support of Lee, Higginson. This made possible further enlargement of operations. The following year, Lee, Higginson marketed an issue of bonds and stocks of the lead and oil paint company, Harrison Brothers & Company, of Philadelphia, founded in 1793. In 1899, Jackson & Curtis and Hornblower & Weeks with Clark, Dodge in New York underwrote $10 million in preferred stock for the American Agricultural Chemical Corporation. Lee, Higginson, R. L. Day, and Estabrook, separately or in association, underwrote in 1898 and 1899 $10 million in bonds for the American Bell Telephone Company to provide funds for expansion.

Beyond these national industrial names, New England firms were active in such offerings for local enterprises as the Seattle City Railway (1890), Brockton Street Railway (1890), Ellicott Square Office Building in Buffalo (1895), Akron Waterworks, Lorain & Cleveland Railway (1899), Rockland-Rockport Lime Company (1900).

Government Finance

The two most important influences on the market for United States government securities in the years following the Civil War were the note circulation privilege carried by government bonds, as granted by the National Currency Act of 1864, and the sharp reduction in Treasury debt. Jay Cooke's specialized dealer operations and the firms associated with him (principally Fisk & Hatch, and Vermilye & Company) became relatively less important in government security operations during the era of railroad and industrial financing after the Civil War. The bulk of trading in government issues was taken over by brokerage houses operating through the New York Stock Exchange.

During the 1870's the Treasury was mainly involved in debt refunding, and during the 1880's large budget surpluses made debt retirement operations possible. Federal flotations were important for only a few years in the 1890's. The continuous outflow of gold required replenishment of the Treasury's holdings if the country was to remain on the gold standard, and the Spanish American War necessitated resort to the market for new borrowing. The use of government bonds to secure national bank note circulation was an important factor in the success of these issues which were offered for competitive bidding.

After the Civil War the role of the investment banking house as underwriters of state and municipal securities became formalized as issues increased in number and volume. State legislatures often passed laws requiring municipalities to sell their securities at auction rather than privately. This led to the practice, common today, of specialized firms, either singly or in syndicates, purchasing new municipal issues and subsequently selling them at slightly higher prices to the ultimate investors. Massachusetts was one of the few states to continue the policy of issuing bonds in support of railroad projects. Some of these bonds were issued in sterling denominations for sale on the London market.

The depression which began in 1873 brought fiscal hardships to many local governments. Twenty percent of the outstanding municipal bonds fell into default, some irretrievably, a figure twice as high as the estimates for the depression of the 1930's. New England municipalities, however, came through the depression of 1873 with very few instances of bond defaults. Many New England cities and towns issued securities in support of railroads through the 1870's. Some of the earliest investment banking houses to be organized in Boston became specialists in municipal bonds. Not only did they underwrite the issues of municipalities in the New England area but those of governments in other states as well. Issues of several large midwestern cities were underwritten in Boston before the 1880's, with commercial banks representing one of the principal markets for these securities.


INCORPORATED UNDER THE LAWS OF THE STATE OF MAINE.

No. 1031 THE VAN CHOATE 10 Shares.

600.000 Shares. CAPITAL Par Value $10.

Electric Company

$6.000.000.

60.000 of the above Shares. NON ASSESSABLE. are 6% Preferred Stock.

This Certifies that Ayma L Hall of Rockland Me is the owner of Ten Shares of the Preferred Stock of · · THE VAN CHOATE ELECTRIC COMPANY. · · transferable upon the books of the Company by himself or his lawful Attorney only upon the endorsement and surrender of this Certificate to the Company.

Preferred Stock

The preferred stock is entitled to first 6% dividend out of the net traffic receipts of each year and after the common stock has received 6% dividend in any year, any balance of receipts for that year will be divided pro rata among all the stock both common and preferred.

In Witness Whereof the said Company has caused this Certificate to be sealed and signed by its President and Treasurer.

Portland Me JUL 11 1896 189

Treasurer. S. H. Van Choate, President.

Chapter III

The Turn of the 19th Century

No accurate census of investment banking firms exists for any period in the 1800's. Firms such as S. & M. Allen & Company, engaged in lotteries, brokerage and foreign exchange, and E. W. Clark & Company, active in investment banking operations, are early examples of the largest and most extensive houses. Partnerships of the two firms were located in principal cities. They followed a broad general policy set by the home office and occasionally acted in unison. These organizations set the general pattern for later development of the large investment banking house. There were, as well, independent firms which confined their activity largely to one geographical area. A number of these, however, developed ties through correspondent relationships with similar firms in other American cities and abroad.

The *Bankers Magazine* in 1854 listed 10 private banks in Boston, 18 in New York, 20 in Philadelphia and 15 in St. Louis. There were, in addition, a number of other firms dealing in investments, foreign exchange and conducting brokerage. Some of these firms, as well as the private banks, performed limited investment banking functions. At this time in Boston, houses like John E. Thayer & Brother, Blake Brothers & Company and Henshaw & Ward were typical. Firms were also established in Providence, Hartford, Springfield, Portland and other cities on the eastern seaboard.

Some like Brown Brothers & Co., of New York had offices in most of the principal cities.

The turnover of firms was relatively high and many went bankrupt during periods of business recession. Others overextended themselves and failed as a result of too heavy promotion of enterprises or excessive speculation. Successor houses were frequently formed; having learned from experience, they were generally more stable than their predecessors. There currently exist in New York, Boston and Philadelphia several houses which were either founded during the pre-Civil War period, or trace their origins to that period through absorption of other firms. A number of other houses active in Boston today began business between the early 1860's and 1900.

The 1902 fall edition of the *American Bank Reporter* carried a listing of 277 bankers and brokers in New England, in addition to state and national banks and loan and trust companies. Of these, 218 were domiciled in Boston. Among them were a number of private banks performing ordinary commercial operations and several firms dealing principally in commercial paper. Most of them, however, may be classed as security houses, including those underwriting houses which bought securities on their own account and offered them for sale, and those which performed largely brokerage functions. Almost half of the above number of houses in existence in 1902 were established before 1885, and within this group some 25 or more date back to the 1870's. A small nucleus, as noted before, began operations in the 1850's. A general classification of the firms by function is shown below:

Number and Type of Firm Engaged in the Securities Business in New England, 1902

Functions	*Number of Boston Firms*	*Number of N. E. Firms Outside Boston*
Private bankers (only)	60	38
Dealers in securities (only)	50	4
Private bankers and dealers	13	—
Brokers and dealers	95	17
	218	59

Probably as many as 50 of these firms originated or underwrote securities. Lee, Higginson & Co. (1848), Brewster, Cobb & Estabrook (1851), Tucker, Anthony & Company (1862), Kidder, Peabody & Co. (1865), Jackson & Curtis (1879), F. S. Moseley & Company (1879), R. L. Day & Co. (1892), Perry, Coffin & Burr (1898), were among the dominant firms, and provided what was considered at that time a broad range of services for the issuer. Several commercial banks were also active as underwriters at this time, including the Old Colony Trust Co. in Boston, Union Trust Co. in Springfield, and Worcester Trust Co. in Worcester. Several of the underwriting firms were in a position to handle an entire issue of large size; others could originate and distribute issues of modest size or participate in the distribution of larger issues. Some of the latter houses restricted their operations to municipal securities.

Organization and Functions of the Houses

Several of the houses began operating partially as dealers in commercial paper. Commercial paper dealers assisted in financing various businesses on a short-term basis through purchase and sale of negotiable notes, and provided a natural tie to later underwriting of corporate securities. This development was gradual, and for many years the two kinds of business were carried on side by side. Often the houses later specialized in underwriting; but even today several continue to conduct both kinds of business. A few of these houses carried on a very active letter-of-credit business covering imports of essential raw materials used in the region — wool, hides, rubber, Egyptian cotton, wood and pulp. They had branches, representatives, or close correspondents in the important trading areas abroad. The returns from this business were usually sufficient to carry the overhead costs of all of the activities of the firm, making underwriting activities when successful very profitable.

The organization of the typical investment banking house was that of a partnership or individual proprietorship. Traditionally, it was considered that unlimited liability expressed integrity better than the limited liability of the corporate form, and until 1953 membership on the New York Stock Exchange was denied a firm organized as a corporation. Many firms assume this position even today, although the corporate form has gradually become more prevalent in the industry. In the period from 1900-1930 the development of affiliated investment banking corporations by commercial banks helped make investors familiar with the corporate form, and a drift ensued toward corporate organization of investment banking houses.

In the period around 1900, as the investment banking structure developed, the underwriting of securities of major corporations, including railroads, was led by eastern houses in New York, Boston, and Philadelphia. Distribution of securities in the growing Middle West was largely accomplished through the Chicago offices of eastern houses or through the larger commercial banks acting in the capacity of dealers. The Chicago area, after 1900, experienced a substantial growth in investment banking firms, and one or two of the large commercial banks also became active in security dealings. The number of local firms, as well as Chicago branches of those domiciled in eastern centers, increased. By 1910 local firms were originating and distributing securities of midwestern corporations and municipalities in some volume and taking positions in syndicates centered in the East for distribution in the Chicago region.

Between 1900 and World War I the population of firms in both New England and the nation continued to grow. A compilation of houses located in New England in 1913 provides a general idea of the investment banking framework, including both corporate and municipal security underwriters and houses dealing in both kinds of issues. In the nation, there were only five houses which could be considered to have a national distribution system for securities. Two of these, Kidder, Peabody and Lee, Higginson were domiciled in Boston. William A. Salomon & Company was in New York and N. W. Harris and N. W. Halsey & Co., were in Chicago. J. P. Morgan & Co., Kuhn, Loeb & Company and William A. Read & Company were primarily underwriters in the New York market.

1913 Census
of Firms in the Securities Business

	Boston	*Elsewhere in New England*
Underwriters	59	13
Firms with branch offices	27	3
Branches in New England	27	7
Branches elsewhere	58	0
Branch offices of New York underwriting firms	16	17
Branch offices of underwriting firms domiciled in Chicago (and other principal cities)	2	2
Additional New England firms with principal business as brokers, dealers, etc.	334	86

Firms with a limited number of employees and a single office predominated in all centers; and much of their business was conducted within regions, both in terms of the securities handled, and the customers served. In addition to the firms which were active as underwriters and distributors there were over 300 firms engaged in some aspect of the securities business in New England. During this period, however, branching of firms throughout the nation increased, and the merger of firms for the purpose of increasing capital or securing complementary benefits by the combination of wholesale and retail types of business were not infrequent. New York and Boston firms led other centers in maintaining branch offices in other states as well as within their own regions. New York, Boston and Chicago firms had branches in each of the other cities — a pattern still followed today. Of the 24 branches of New York firms in Boston at this time 16 were considered primarily underwriters and distributors. Unlike their counterparts today, a number of which are principally sales outlets, these branch offices possessed considerable autonomy in underwriting and originating issues.

Some Boston houses, in order to widen their spheres of influence and broaden their market ties, opened branches in New York as early as the 1870's. Kidder, Peabody has maintained offices in New York since 1872, and Lee, Higginson had, in effect, a branch in the firm of Chase & Higginson in 1873. This procedure brought Boston firms closer to foreign borrowers. A number of these borrowers seemed to feel that a New York office was a requisite for firms handling their issues, some of which made their first appearance in the early 1900's. Although the capital markets began to develop further central tendencies, regionalism, nevertheless, continued to characterize an important segment of the market.

The differentiation of function became sharper in this period. Several firms in Boston and New York began to develop a high degree of organization and some departmentalization in order to increase the variety of services offered, some of which went beyond simple assistance in the raising of capital. Emphasis was also placed on improving distributive facilities. As these organizations increased in size and extended the locations of their branches, obtaining a relatively large volume of securities for distribution became important. Competition became intense for management positions and extensive participation in underwriting. Other houses fought for top positions in selling syndicates.

Although most of the houses did not attempt to develop retail business in the modern sense, and limited their advertising to "the tombstone" (an ad which was merely a dignified identification of the firm by name and address), a few emphasized their capacity for retail distribution and developed and trained salesmen who actively sought business instead of merely depending on "counter men" to service only such customers as approached the firm. Among these was N. W. Halsey & Co. of Chicago, predecessor of Halsey, Stuart & Co. In New England, several houses also began to develop retail sales. Lee, Higginson is credited with establishing one of the early statistical services, now a standard feature with the larger houses in the industry serving retail customers. The service grew out of the firm's pamphlet on railroad securities, first issued in 1879, which dealt largely with western roads and provided information based on personal investigation of the properties by the partners and interviews with the management — a procedure which has come to be highly developed by the analyst of the contemporary house.

Volume and Type of Issues Offered for New Capital

Measures of growth applicable to underwriting and new security distribution are difficult to apply. One such measure, however, is the volume of new securities offered by houses as syndicate managers; another is participations in syndicates. The table below provides data on new securities sponsored by the region's houses between 1900 and 1915 as syndicate managers. Several large issues were offered in 1900: in the railroad field, the largest were a $2.1 million bond issue of the Boston Elevated Railroad, taken by Kidder, Peabody, and a $2 million bond issue of the Chicago, Burlington

Corporate Issues for New Capital Offered Entirely by New England Investment Bankers or Syndicates Headed by Them

(millions of dollars)

	Totals		*Railroads & Traction Companies*		*Utilities*		*Industrials*	
Year	*Number*	*Amount*	*Number*	*Amount*	*Number*	*Amount*	*Number*	*Amount*
1900	31	$ 26.1	16	$ 8.1	7	$11.6	8	$ 6.3
1905	34	59.0	19	22.1	11	32.0	4	5.0
1910	54	96.6	18	33.6	21	34.8	15	28.2
1915	52	106.0	12	31.6	24	33.5	16	40.9

Source: *Commercial and Financial Chronicle.* Note: Refunding issues and short term debt are not included.

& Quincy Railroad, underwritten by Lee, Higginson. Kidder, Peabody also offered a $10 million bond issue of the American Telephone & Telegraph Company. The size of most issues was relatively small — less than $1 million — and railroad companies dominated the market.

Railways continued to dominate market offerings in 1905 with 56 per cent of the total number and 10 of the 16 issues of over $1 million falling within this category. Another large issue was $20 million of bonds for AT&T. Issues of industrials, although retaining their speculative character, increased in number.

In 1910, for the first time, both utility and industrial securities threatened the dominance of rail issues. All three types shared fairly equally in a market which was experiencing considerable expansion. Twenty-five of the new issues were for $1 million or more, and for the first time a major portion was for utilities, with railroads and industrials making up the remainder. Industrials showed the greatest change with regard to the number and volume of new issues. This year saw a growing tendency of firms to offer stocks (especially preferred) rather than bonds.

The trends evident in 1910 continued in 1915. More than half of the new issues in 1915 were over $1 million each, and industrials continued to take a growing share of the market with an increased volume of common and preferred stock offerings which later became one of the principal financing instruments. Throughout the whole period, Boston firms headed syndicates offering about $85 million of securities of the AT&T's associated companies.

During the period from 1900 to 1915 Boston investment bankers also participated in syndicates headed by firms located in New York or some other city outside the region. The issues aggregated $4.8 million in 1900 and by 1915 amounted to $69.5 million. These underwritings represented the same industrial groups and types of securities noted above. As issues increased in size and number over the years, the management of a syndicate was to an increasing extent shared with houses outside the region, generally in New York. Among the issues in which management positions were shared by houses outside New England were the $4 million bond issue of the Chicago Junction Railway and Union Stockyards Company in 1900 offered by Strong, Sturgis & Company of New York and Lee, Higginson, and the $2.5 million bond issue in 1901 of the St. Louis National Stock Yards offered by Lee, Higginson in conjunction with the First National Bank of Chicago. The securities market became still further centralized in New York.

In comparison with the period prior to the 1900's the scope and variety of offerings was striking, particularly in public utilities, industrials, and government securities. Common and preferred stock appeared in increased volume, with a number of features designed to appeal to a wider range of investors. Bonds also took various forms — as mortgages, debentures, or income and collateral trusts. The types of securities accommodated practically any desired division of risk, profits and control of a business enterprise.

Features of Security Distribution

It was difficult during this period for houses in any city to accumulate the substantial sums necessary to purchase and carry until time of sale the larger issues of securities that were appearing on the market. Very few firms had either the capital or distributive capacity to handle more than one type of security. Many distributions took longer than three months to complete, some as long as a year, and a few huge issues as long as two years. The New York group headed by J. P. Morgan underwrote the U. S. Steel Corporation consolidation, which involved securities in excess of $1 billion and continued from March 1901 to April 1903. Over half of the common stock involved in the offering, however, floated in the markets for a number of years before reaching final purchasers. The spreads obtained by the underwriters — i.e., the difference between the price paid the corporation and that at which it was sold

UNITED STATES OF AMERICA

Number 0000 | Number 0000

AMERICAN

1000 | 1000

TELEPHONE AND TELEGRAPH

COMPANY

COLLATERAL TRUST 4 PER CENT. BOND.

For Value Received the American Telephone and Telegraph Company will pay at the office of its Treasurer in New York, N.Y. to the bearer hereof or in case of registration to the registered holder hereof **One Thousand Dollars** in lawful money of the United States on the first day of July in the year Nineteen Hundred and Twenty nine with interest at the rate of four per centum per annum payable semi-annually on the first days of January and July in each year to the bearer of the proper annexed coupons on presentation and surrender thereof.

This bond is one of the bonds secured by an indenture of trust of even date herewith between said American Telephone and Telegraph Company and the Old Colony Trust Company under which certain shares in the capital stock of certain telephone corporations and other securities of said corporations, the property of said American Telephone and Telegraph Company have been vested in said Trust Company, to which indenture of trust reference may be had for the rights of the holders of bonds secured thereby.

This bond when payable to bearer, may be registered on the books of the American Telephone and Telegraph Company in the name of the holder and such registry shall be noted hereon. Thereafter title shall pass only by transfer registered on the books of the Company and certified hereon by the Treasurer unless and until a transfer to bearer shall have been so registered and certified. Such registration shall apply only to the principal of this bond and not to its coupons.

This bond shall not be obligatory until the said Trust Company has signed the certificate endorsed hereon to the effect that it is one of the bonds described in the indenture aforesaid.

SPECIMEN

In Witness whereof the American Telephone and Telegraph Company has caused its corporate seal to be hereto affixed and this obligation to be signed by its President and Treasurer, and the coupons hereto annexed to be attested by the name of said Treasurer at New York, N.Y. this first day of July in the year Eighteen Hundred and Ninety nine.

SPECIMEN — Treasurer | ONE THOUSAND DOLLARS | SPECIMEN — President

1000

to the buyers — were liberal by present standards because of the greater risk in distribution. Unsold securities were frequently left in syndicate hands at the close of the distribution. While the price to the corporation was fixed, the price at which the securities were sold to the public sometimes varied according to market conditions. At times the buying power of the investor brought concessions. Increasingly, it became the practice to invite other firms to join in moving the issue and sharing the risk. During the syndicate's life the commercial banks aided in carrying the securities with loans, the collateral being securities held by the syndicate. This was the case in the early telephone bond issues. The first two American Bell Telephone Company bond issues, amounting to $5 million, were offered publicly in 1899. Two New England houses — Estabrook and R. L. Day, and Vermilye & Company of New York with close Boston connections were co-originators, and it took the syndicates up to a year to market the bonds.

Beginning in 1900 Kidder, Peabody became one of the principal houses associated with the telephone company and this relationship continued even after the issues became so large that, beginning in 1906 with the $150 million bond issue, management of a number of AT&T issues was shared with J. P. Morgan and Kuhn, Loeb in New York. Kidder, Peabody carried the responsibility for distribution of telephone issues in New England. In the telephone syndicates which Kidder, Peabody headed in the early 1900's, the house would usually associate itself with five or six other New England houses in underwriting the issue. Baring Brothers & Company in London participated in some of these syndicates. This underwriting association continued in connection with the New England portions of the issues after the New York houses became members of the syndicate. Some 30-40 houses, including investment bankers in Chicago, Houston, and Atlanta, among other cities, would participate in the final sale of the issues. Individuals, banks, and insurance companies were also frequently members of the underwriting group on original terms. After the Armstrong investigation in 1906, insurance companies no longer participated in syndicates. On occasion individuals would participate in the purchase of bonds to the extent of $500 thousand; and at the dissolution of the syndicate, a number of these bonds, if no longer wanted, would be redistributed to other buyers.

Most of the early issues of bonds in various fields, particularly those originated by New England houses, were distributed to insurance companies, private trustees who traditionally controlled large aggregates of property in New England, endowed funds such as those of Harvard College, and individuals. Commercial banks had become important buyers of bonds and continued to devote an increasing portion of their resources to their purchase. In 1912 the amount of bonds held roughly equaled paid-in capital. Savings banks, particularly in Rhode Island and Maine, were large buyers of utility bonds. This market was developed in part by Perry, Coffin, and Burr. Since the mid-1880's some family fortunes, accumulated largely through promotions and management of railroad and industrial enterprises, became trustee-managed, and took shares in a variety of enterprises, both new and established, throughout the nation. For example, when J. M. Forbes withdrew from active business in the late 1800's his funds were distributed roughly by thirds among the securities of the Chicago, Burlington & Quincy Railroad, Calumet and Hecla Consolidated Copper, and in western lands. Forbes had maintained a personal and direct interest in all these enterprises. Subsequently, J. M. Forbes & Company, as trustee, gradually redistributed the Forbes fortune in investments in more enterprises. Between 1890 and 1910 Harvard College bought large blocks of securities originated by the region's houses. Among them were securities of Walter Baker cocoa, General Electric, AT&T, Detroit Edison, Long Island Railroad, United Electrical Securities, Chicago Junction Railway and Union Stockyards. Such distribution methods sufficed where a limited number of issues was sold to a limited number of investors.

As income and savings became more widely distributed through income groups, and secondary markets became better organized and more extensive, the market for securities began to broaden geographically. Securities markets arose as a means of raising new capital and have continued as markets for resale of outstanding securities and as sources for additional funds. Ownership of stocks by individuals in the early 1900's, however, probably did not exceed one-half million persons and was generally limited to the higher income groups.

Variety of Industries Served

The New England houses, like those elsewhere, also served a growing number of regional industries such as textile machinery, machine tool builders, shoes and leather and rubber goods, as well as the expanding utility, lighting and gas companies. Among these were such names as Hood Rubber, Wyman Gordon, Bigelow Sanford Carpet, and Connecticut Power. New England houses also offered issues of such other industries as Chevrolet Motor Car, Union Bag and Paper and New York Tanning Extract in addition to those of telephone companies and utilities located in other regions of the United States. As the telephone companies developed throughout the nation, Kidder, Peabody negotiated the sale of independent companies — commercial systems and mutual and rural lines — to the American Telephone & Telegraph Company. The house maintained trading positions in telephone securities and was also instrumental in getting AT&T stock listed on exchanges abroad. New England houses also managed the underwriting, in 1912, of the $25 million bond issue for the Virginian Railway.

The association of New England houses with companies like United Fruit, General Electric and General Motors continued. The firms underwrote $8.2 million of United Fruit Company securities offered between 1908 and 1911, a $10 million G.E. bond issue in 1912, and a $15 million G.M. five year note in 1910. Lee, Higginson laid the foundation for the reorganization in 1916 of General Motors with the now familiar federated divisions as constituents. In all these underwritings, new capital was supplied for expansion, as well as for some recasting of financial structures. In several cases the syndicates were shared with New York houses. In 1916 Lee, Higginson, acting in conjunction with Charles W. Nash, completed the purchase of the stock of the T. B. Jeffery Company and set up the Nash Motor Corporation.

After 1895 the reliance on foreign capital to finance industrial growth was materially lessened but it still played an important part in some flotations. The $20 million issue of AT&T bonds in 1905 and some of the later issues were shared by Kidder, Peabody with Baring Brothers of London and at times by Lee, Higginson's London affiliate. Between 1890 and 1914 the total volume of domestic securities held abroad increased by only $1.5 billion, reaching a total of $4.5 billion by the end of that period. The increase was not as steady as it had been in past periods, and at times securities held abroad were repatriated. The American investor was becoming increasingly able to provide funds for domestic enterprises without European assistance. Moreover, New England, like New York, began to export relatively small amounts of capital during this period. New York and Boston firms handled a part of the Boer War financing by the British Exchequer. Kidder, Peabody shared £30 million of the loan with J. P. Morgan, and Rothschild and Morgan took an additional £30 million. Foreign industrial flotation began to be introduced with a small volume of securities from Latin America, Canada, the Far East and Europe. In New York and Boston business in foreign securities was later to reach substantial proportions.

Municipal Finance

Even during the first years of this century, it was evident that the underwriting of state and municipal securities was becoming a specialty within the investment banking industry. Many of the firms active in underwriting municipals did not participate in the corporate market. During this period the volume of municipal bonds issued in New England was growing — from $19.5 million in 1903 to $31.7 million in 1915 — as indeed it was in every section of the nation. The need for better municipal services — street railways, waterworks, schools, and sewage systems — was the primary impetus for expanding indebtedness.

Most of the bonds issued by New England governmental units were purchased by buyers in the region, but they were not all underwritten by investment banking houses. Commercial banks, savings banks and insurance companies often purchased municipal issues, particularly those of the community in which they were located, for their own or their customers' accounts. Individual investors often purchased small issues. Purchases for sinking funds, retirement systems, or on behalf of other municipal or state accounts were fairly common, often indicating the desire of officials to avoid putting their securities to the market test. The changing character of investment banking was evidenced by the growth of the number of firms engaged in municipal business during this period and by the diminishing portion of New England issues purchased by non-investment banking institutions and individuals — from 25 per cent in 1903 to 10 per cent in 1915. In some cases New England issues were purchased outside the region, especially Connecticut municipal issues which were bought by firms in New York City, a practice which still continues.

Besides New England municipals, local firms handled such issues from parts of the country as far away as California and Oregon. Some were the issues of such large cities as Toledo, Ohio, or St. Paul, Minnesota. Others were from small towns such as Patton, Pennsylvania; South Omaha, Nebraska; Lewiston, Idaho; and Central City, West Virginia. In large measure this procedure reflected the undeveloped character of financial centers in other parts of the nation.

Contrary to the practice of more recent years, purchases of most municipal issues were made without the formation of a syndicate. The relatively small average size of the issues, which ranged from $25 thousand to $75 thousand, made that step unnecessary. An issue totaling as much as $2 million was a rarity. In addition, many municipalities in New England enjoyed a high credit rating and their issues sold easily. This was and is particularly true of college and historic towns.

Syndicates were formed, however, to purchase the larger issues and the securities of issuers whose credit ratings were not the best. The Boston house of Fisk & Robinson headed the syndicate formed to purchase two of the largest municipal issues of the period. One was a $37 million New York City issue in 1904 and the other a $16 million Philadelphia issue in 1906.

Municipal Bond Underwriting
(millions of dollars)

	1903	*1905*	*1910*	*1915*
Total N. E. Issues	19.5	22.5	23.5	31.7
Underwritten in N. E.	19.4	19.8	23.1	30.9
Underwritten Outside N. E.	.1	2.3	.4	.9
Underwritten by Mixed Syndicates	—	.4	—	—
Underwritings of Outside Issues by Investment Bankers in N. E.	.7	3.2	1.4	.7
Outside Issues Underwritten by Mixed Syndicates	.2	—	.8	—
Total of All State and Municipal Issues in the U. S.	n. a.	n. a.	324.4	492.6
New England Portion of this Total	n. a.	n. a.	7.2%	8.1%
Number of N. E. Investment Banking Houses which Underwrote Municipal Issues	19	36	32	31

n. a. = not available.
Source: *The Bond Buyer.*

World War I and U. S. Government Securities

By 1900 trading in U.S. government securities had shifted from brokerage houses, operating through the New York Stock Exchange, toward a specialized over-the-counter dealer market. The use of government bonds to secure public deposits and circulation provided opportunities for private banking houses to perform as dealers and supply the bonds needed by banks. In effect, they supplied a specialized service and volume was great enough to assure profits. This, then, was the principal function of the dealer in U.S. government securities during the first 15 years of the 1900's when the total Treasury debt held steadily at a level slightly greater than $1 billion.

From 1899 to 1910 the largest dealer in government securities in the United States was the Boston firm of Fisk & Robinson. When the Treasury offered to bidders $30 million of Panama Canal bonds in July 1906, most of the issue was awarded to Fisk & Robinson, and the firm reoffered the bonds to banks. From 1911 to 1917 only one bank, the National City Bank of New York, and one investment banking house, C. F. Childs & Company, continued to deal conspicuously throughout the country in government bonds.

The participation of the United States in World War I created an unprecedented need for broader financial markets and laid the foundations for the government securities market as we know it today. Beginning in 1917 the great volume of Liberty Loan bonds and Farm Loan bonds provided dealers with an almost unlimited field for operation in a new type of business of a less technical character than the increasing or decreasing circulation accounts of the banks.

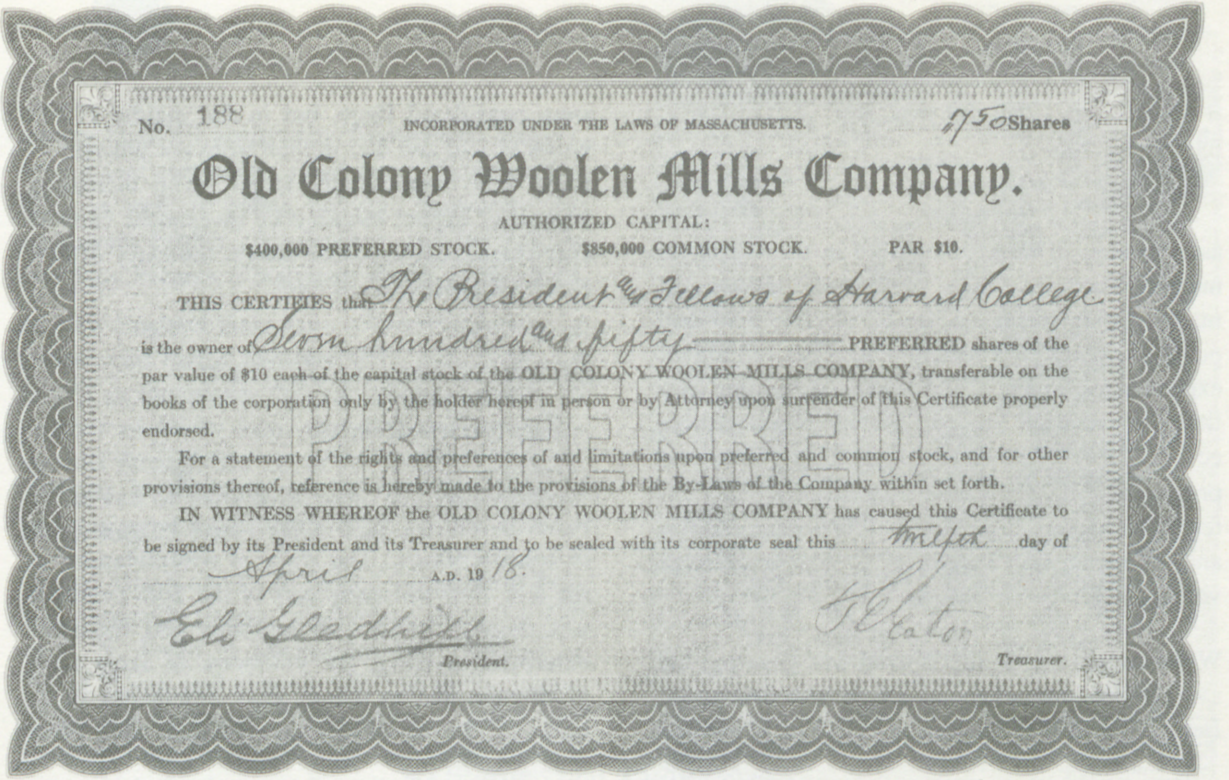
An active entrant into the U. S. securities market at this time was Salomon Bros. & Hutzler. The firm, organized in 1910, developed a business in short term and other investments suitable for bank portfolios, as well as stock exchange business. The over-the-counter market in governments grew at the expense of exchange trading and by 1925 the volume of trading exceeded that on the exchange by several times.

The declaration of war by Germany in the summer of 1914 and the entrance of the United States in 1917 placed a mountainous burden upon the American capital and credit markets and their supporting institutional framework of commercial and investment banks. The markets were called upon to finance war supplies of the Allies and later participation by the United States. Some $2 billion of securities of European nations associated in the war effort, the most notable of which was the $500 million Anglo-French loan of 1915, were absorbed in our market. New England houses contributed substantially to the effort. In addition about $2.3 billions of American securities were repatriated. The American war loans of 1917-1919 approached $7 billion in size and were floated first with borrowing by certificates of indebtedness and later funded through Liberty Loans.

The War Finance Corporation, created in 1918, acted somewhat as a dealer during and immediately after the war as it attempted to provide stability through a limited program of purchases.

War finance brought about a huge increase in popular ownership of securities. There were over 4 million subscriptions to the First Liberty Loan and 22 million to the Fourth. Ownership of securities became more widespread. Subsequently, however, about 18 million subscribers sold their holdings of Liberty bonds to four million buyers. Estimates place the number of security holders at 2 per cent of the population before the war and at about 10 per cent by 1919. The individual purchaser was cultivated intensively by investment bankers during the 1920's. Large personal gains from sustained national prosperity made it possible for persons to move from savings deposit and insurance policy holdings to direct investment. This practice grew into a financial habit and had been encouraged by the advertising of Liberty Bonds which for the first time taught the general public some of the terminology of investment.

With the war the United States changed from a debtor to a creditor nation and for the first time became an international investor on a large scale. The demand for funds by domestic industry and by state and local governments increased tremendously following the war. Investment bankers and brokers began to use modern advertising on a large scale — breaking tradition with the "tombstone" — with the intent of extending the number of direct investors by increasing the public's knowledge of the financial system. They were aided in this by increasing numbers of customer and employee security ownership plans sponsored by corporations.



No. 188 INCORPORATED UNDER THE LAWS OF MASSACHUSETTS. 750 Shares

Old Colony Woolen Mills Company.

AUTHORIZED CAPITAL:

$400,000 PREFERRED STOCK. $850,000 COMMON STOCK. PAR $10.

THIS CERTIFIES that The President and Fellows of Harvard College is the owner of Seven hundred and fifty PREFERRED shares of the par value of $10 each of the capital stock of the OLD COLONY WOOLEN MILLS COMPANY, transferable on the books of the corporation only by the holder hereof in person or by Attorney upon surrender of this Certificate properly endorsed.

PREFERRED

For a statement of the rights and preferences of and limitations upon preferred and common stock, and for other provisions thereof, reference is hereby made to the provisions of the By-Laws of the Company within set forth.

IN WITNESS WHEREOF the OLD COLONY WOOLEN MILLS COMPANY has caused this Certificate to be signed by its President and its Treasurer and to be sealed with its corporate seal this twelfth day of April A.D. 1918.

Eli Gledhill

President.

Treasurer.

Chapter IV

Developments of the 20's and 30's

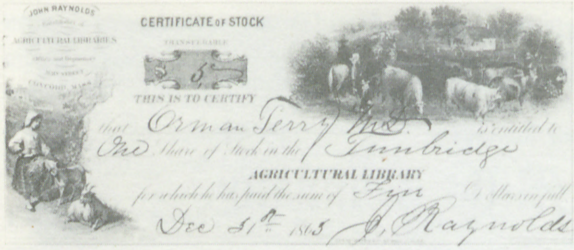
The activities of New England's investment bankers during the 1920's were influenced by the national character of the capital and money markets. Many business enterprises which had previously been identified with specific regions became divisions of national concerns while others sought more extensive markets in the nation or abroad. A larger number of investment banking firms established broader distributive facilities and sought underwritings on a national basis.

Demands on the Capital Markets

The growing volume and wide variety of demands on the capital markets during the 1920's taxed the capacity of the investment banking industry. Prosperity and economic expansion induced great demands by corporations — and especially by public utilities — for the means to finance fixed capital formation. The assumption by America of the role of capital exporter forced the investment banking industry to undertake the flotation of foreign issues.

The combination of demand by domestic and foreign corporations and governments made necessary further changes in the investment banking structure and the types of syndicates used. Gross issues of all types totaled about $6 billion in 1924. A peak for the decade came in 1929 when total issues exceeded $8 billion. From 1919 through 1930 nearly 1,800 foreign security issues were floated in the United States for a gross total of somewhat under $15 billion. Corporate new money issues shown in the chart on page 36 constituted the great bulk of the demand.

During the 1920's utilities dominated the new issues market, reflecting the large volume of capital expenditures in these industries, the assets of which doubled during the decade. For example, fixed



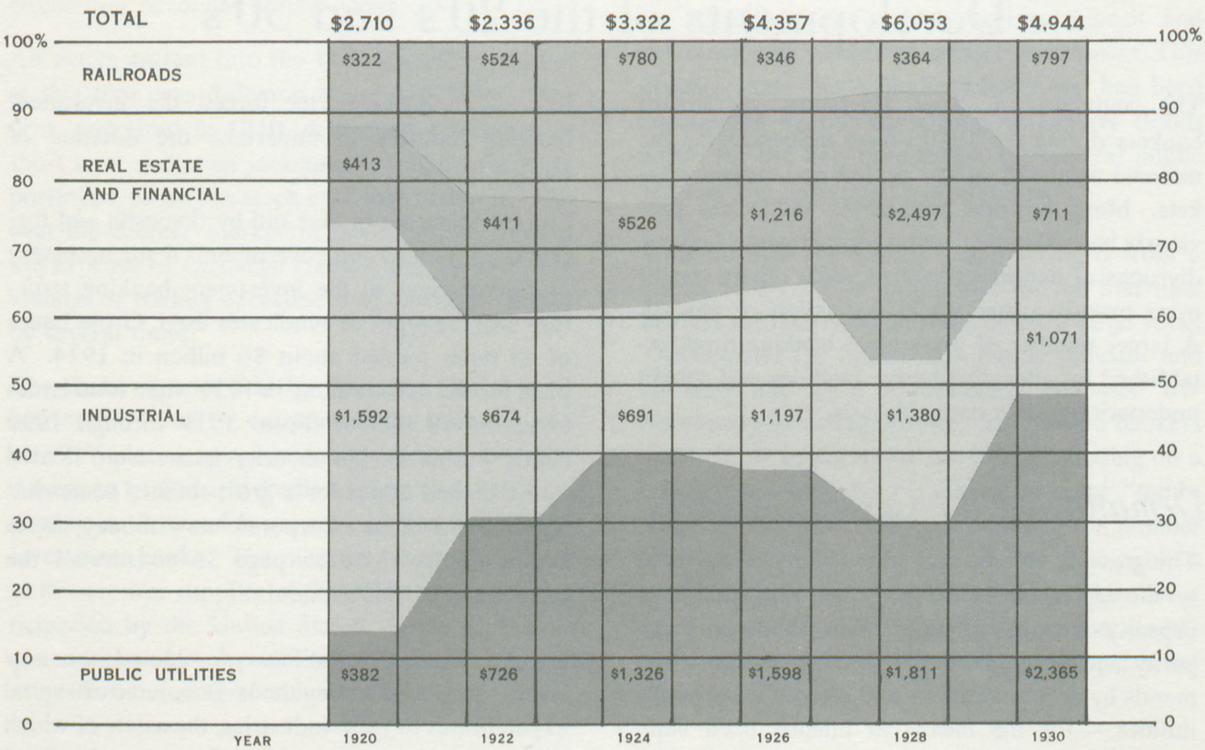
asset outlays of large companies in the telephone industry averaged a little under $400 million annually during the period. The electric light and power industry averaged about $700 million of expenditures, mainly for central generating stations. Fixed asset expenditures by manufacturing corporations were also heavy but a substantial proportion of these funds was supplied from internal sources. Railroad expenditures for additions and improvements continued to absorb a large volume of funds.

While annual aggregate demand was growing, the average size of individual issues also increased. Before World War I, issues in excess of $1 million were considered large, but in the middle 1920's issues of $20 and $25 million were not unusual — some were substantially larger. The increasing volume of capital required by investment bankers encouraged, among other things, the entry of new firms and growth of old ones.

Business and Industrial Consolidations

A substantial part of the proceeds of security issues in various fields supported a large number of consolidations. The wave of consolidations in the late 19th and early part of the 20th centuries was largely confined to railroads and industrial enterprises seeking the efficiency of large scale production and in a few cases dominance in an industry. In the 1920's consolidations took place

PERCENTAGE DISTRIBUTION OF
DOMESTIC AND FOREIGN CORPORATE SECURITY ISSUES FOR NEW CAPITAL
UNITED STATES, 1920—1930
(MILLIONS OF DOLLARS)



SOURCE: Statistical Abstract

among financial institutions (particularly banks), amusement companies, retail stores, food distributors, as well as public utilities. Railroads also underwent further consolidation and the holding company became a dominant device in this field.

In New England there were 172 consolidations of commercial banks between 1921 and 1936 — a record in the region for any 15-year period. A number of banks were also brought into group systems through the use of the holding company. At the end of 1930 there were 10 group systems, comprising 73 banks, in the region.

Jordan Marsh and C. F. Hovey Company in Boston, nationally known independent stores, as well as F. N. Joslin in Malden became members of Allied Stores; and Filene's, also nationally known, joined the Federated Stores system. Allied and Federated are two of the "big city" store associations which developed at the end of the 1920's.

First National Stores, which currently operates the largest grocery chain in New England, developed from a consolidation in 1925 of several long established food chains — the Ginter Company, J. T. Connor, and O'Keeffe's, Inc., operating several hundred stores each. The new corporation comprised about 1,600 neighborhood stores in Massachusetts and Maine. In 1929 the concern acquired the Mayflower Stores in Rhode Island and Economy Grocery chain in Connecticut. The Ginter Company and Connor systems had been established in 1895 and 1897 respectively. The Walter Baker chocolate firm and Minute Tapioca, both in Massachusetts, became divisions of the General Foods Corporation, which was formed to sell a number of nationally trademarked noncompeting brands of food products by its various divisions.

In the utility field associations of operating companies were developed through the use of holding companies. The New England Gas and Electric System and the New England Power Association are examples. After the mid-1920's, the holding company became a dominant device for centralizing the control and management of public utility operating companies. Many developed a complex

intercorporate organization involving the issue of securities of varying form and value.

A number of these combinations were promoted by investment bankers with the objective of securing economies of production and distribution, or a position of greater prestige for individual firms. In certain consolidations, investment bankers were advisers and in others they underwrote the whole issue or acted on a "stand-by" basis, purchasing any securities of the new firm which were not taken up by the security holders of the individual firms involved in the consolidation. In a few cases combinations were promoted largely for the profit resulting from the sale of securities.

Increased Variety of Securities

Before 1920 financing of business enterprise had generally taken the traditional forms of equity and debt. This continued to be the case but many of the securities involved developed new features and a number of variations, such as classes of equities, preferred stock in series, bonds with warrants and stock with rights and warrants. In the early 1920's the utility operating companies frequently followed the sale of bonds by issuance of preferred and common stock. Following the sale of securities of the operating companies came the nationwide distribution of securities of holding companies in the form of collateral trust bonds. Some of these holding companies controlled widely scattered enterprises which could not be classed as utilities. Toward the end of the 1920's there was a noticeable deterioration in quality of their securities issues. Meanwhile, the real estate construction industry turned from dependence solely on direct loans from financial institutions to the issuing of bonds for individual purchase. Finally, a new security, the investment trust share, made its appearance in volume. Investment trusts underwent a rapid development after 1924. Two of the oldest investment trusts still in existence were organized in Boston — Boston Personal Property Trust (1893) and the trust now named the Colonial Fund (1904). The "Boston type" or open end trust is widely known today.

Changing Syndicate Forms

As financial intermediaries became responsible for an increased proportion of the total supply of funds, the concentration of personal savings became a more powerful force in channeling investable funds. Individuals, however, continued as the important buyers of bonds and dominant suppliers of equity money despite the rise of institutions. Personal income taxation was not yet a strong force and the capital markets were not influenced by tax factors. Estimates of stock ownership provide one measure of individual interest in stocks. In 1920 there were two million stockholders in the nation; by 1930 the number was estimated at 10 million. As a consequence, investment bankers felt the need of devising sales machinery capable of reaching great numbers of individuals. In large part, the industry's response was to expand the network of branch offices. Houses which were successful distributors began to rely less and less on the originating house and sought originations themselves, thus combining the two functions. As stock financing assumed greater importance during this period, a number of firms which had engaged only in brokerage entered underwriting or became distributors.

The need for an extensive sales network also resulted in a change in the prevalent form of syndication. Before World War I investment bankers frequently used several syndicates in underwriting corporate issues. Usually an investment banker purchased an entire issue directly from an issuer at a stated price, and that banker alone would sign the purchase contract; he was known as the "originating banker" or "house of issue." As a second step, the originator immediately resold the entire issue to a "purchase syndicate" at an increase in price. Ordinarily, the originating house became a member and manager of the purchase syndicate. As the issues became larger, a third step might be employed involving a "banking syndicate" which would buy the securities from the purchase syndicate at still another increase in price, thus spreading risk even more widely. The originating banker and other members of the purchase group usually became members of the banking syndicate, with the originating banker as manager and supervisor of the final sale of the securities.

Beginning in the 1920's, as a result of the growth in number and size of security issues, a large number of additional underwriters was required. The syndicate in which they were included was called either a "selling syndicate" or a "selling group," and at times displaced the banking syndicate. These selling units differed only in the degree of liability assumed by the participants. A participant in a selling group was liable only to the extent of his individual subscription. The group's function was to reach large numbers of buyers; hence, it was constructed to achieve breadth in salesmen's contacts, and accordingly included underwriting houses widely distributed geographically and with diversified sales capabilities. The size, composition and liability of the selling unit varied with the size of the issue, the risk involved and the type of investor to be reached. The ability of a dealer to distribute certain kinds of securities was also a determinant. The problem of keeping the cost of distribution as low as possible became important because of the smaller average size of individual sales. Throughout the 1917-1933 period, officers and directors of issuing corporations, as well as other moneyed individuals, on occasion continued to be made participants on original terms in the underwriting of a number of issues. This was the much publicized "gravy train" which disappeared gradually because of the growth of the number of underwriting firms and also as a result of the passage of the Securities Act of 1933.

Periods for distribution became much shorter than before World War I. Usually the life of the syndicate was 30-60 days, with a provision to terminate or extend the period. In practice, they were much shorter. Risk of carrying unsold issues diminished and spreads became narrower than before World War I. A uniform offering price to the public became the general rule. Price stabilization in the secondary market during the offering period, a device which some earlier syndicates had used, became more common.

The increase in competition lessened the relative importance of houses dominant in a particular field before World War I, though they remained leaders in originating, managing or in taking ranking participations in issues. Dillon, Read & Co., and Blair & Company in New York, and Lee, Higginson and Kidder, Peabody in Boston were best known for underwriting "across the board" of industry groups. Kuhn, Loeb and J. P. Morgan in New York were leaders in railroads, as were older firms such as Speyer & Co., J. & W. Seligman and Ladenburg Thalmann. Bonbright & Co. in New York, Halsey, Stuart & Co. and Harris, Forbes in Chicago, and Coffin & Burr in Boston were leaders in public utilities. Lehman Brothers and Goldman, Sachs & Co. in New York were best known in the merchandising field.

The growing web of branch offices, the addition of the selling syndicates, and the standardization of the basic types of securities, combined to speed the nationalization of the primary and secondary markets for securities, especially corporate instruments. These developments led to a substantial broadening of the capital market. It is difficult to exaggerate the economic significance of a developing national market. Since very large issues could be accommodated, a growing number of corporations were able to utilize technology requiring substantial investment and to become national in scope. Also, an expanding market diminished the variance in prices and knowledge which characterize local markets. In the process of economic development, it signified that growing regions could draw upon savings generated in older regions.

Changes in Structure of Firms

New England, like other parts of the nation, experienced an increase in the number of firms in the securities business during the 1920's. Although there were shifts in the population of firms, the number of houses classified as underwriters which were domiciled in Boston remained stable. An increase in the number of underwriters did occur within the rest of the region. Between the close of World War I and the late 1920's, more than a half dozen New England commercial banks established security affiliates. Other banks also participated directly in syndicates.

Mergers of houses continued but the reasons for merging were more varied — to the desire to increase capital and to secure complementary types of business was added the necessity of strengthening management. Some brokers took on underwriting and distribution, and underwriters and distributors added or expanded brokerage. A number of firms also established branches within and outside the region by purchasing other firms and by opening new offices. Some Boston underwriters maintained branches in all of the region's principal cities. As the interior of the nation became important as a market for securities, Boston underwriters opened new offices outside New England. A number of these were strategically located in the developing regions — Midwest, Southwest and Pacific Coast. In most cases the dual purpose was to improve sales outlets and search for new business. Private wires and direct lines increased in number, thus linking offices in various centers more closely together. This expansion also increased the number of traveling representatives serving these regions.

Some firms moved more slowly than others, continuing to perform their original functions and handle only the kinds of issues which had become associated with their names. They consolidated their positions in the industry, however, became more clearly departmentalized and extended the range of services offered the issuers. Some added statistical and research and trading departments. New types of specialized knowledge and experience became necessary in dealing with issuers and developing their financial plans. A number of houses gradually built staffs of specialists which increased the firms' effectiveness in competing for new business, in managing underwritings or in securing desirable positions in syndicates. New capital was added to firms through an increase in the number of active and limited partners.

Census of Firms in the Securities Business

(Selected Years)

	1913	*1922*	*1929*	*1933*
Boston				
Underwriters	59	45	44	30
Firms with branch offices	27	22	26	18
Branches in New England	27	33	62	38
Branches elsewhere	58	43	97	34
Branch offices of New York underwriting firms	16	22	20	22
Branch offices of underwriting firms domiciled in Chicago (and other principal cities)	2	4	3	14
Additional firms with principal business as brokers, dealers, etc.	334	138	265	254
Elsewhere in New England				
Underwriters	13	28	38	23
Firms with branch offices	3	8	12	7
Branches in New England	7	10	34	16
Branches elsewhere	0	1	3	2
Branch offices of New York underwriting firms	17	21	34	19
Branch offices of underwriting firms domiciled in Chicago (and other principal cities)	2	10	1	6
Additional firms with principal business as brokers, dealers, etc.	86	56	171	179
Branch offices outside New England of New York (Chicago and other principal cities) underwriting firms with branches in New England	65	237	269	288

As the capital and money markets became more national in scope during the 1920's, with New York as their center, a few houses which had long been domiciled in New England shifted their head offices to New York City, retaining the Boston office as a branch. Usually, however, the branch was given some measure of autonomy and continued its relationship with industrial concerns domiciled in the region. The shift of the head offices to New York tended to increase the competitiveness and the volume of the firm's business.

In addition to the firms classified as underwriters and distributors, which dominated the investment banking business, there was a large number of firms engaged in other phases of the securities business as brokers and dealers. Many of these were individual enterprises or small partnerships with few employees and little capital invested in the business. Some of them played a minor part in distribution of securities, concentrating on retail sales to a limited customer list, and some conducted only an interfirm business. Between 1913 and 1929 there was sharp fluctuation as firms entered and withdrew from business according to chances for profit. Others failed, some merged.

New England cities other than Boston, particularly Hartford and New Haven, were entered by underwriting firms from outside the region, principally by New York houses. Their branches offered increased competition to firms domiciled in the region, not only in searching out new underwritings but more importantly in selling to the growing group of institutional buyers — insurance companies, banks, trust companies and investment trusts. Branching by these same firms, as might be expected, was also carried out aggressively in the other regions of the nation where the facilities were less fully developed. There was debate then as there is now as to whether business could be developed as satisfactorily by telephone and traveling representatives as by a branch office.

The principal cities in the Mid and Far West began to develop or refine investment banking facilities during the 1920's. Investment bankers in Chicago increased in number and ability to originate and manage the distribution of issues; their network of branch offices also expanded and by 1930 was nationwide. Growth of the volume of corporate issues handled by Chicago underwriters outpaced that of the country as a whole, indicating that competition offered in that city to established eastern houses was intensifying. This was also true in other regions as independent houses appeared in increasing numbers in all major cities.

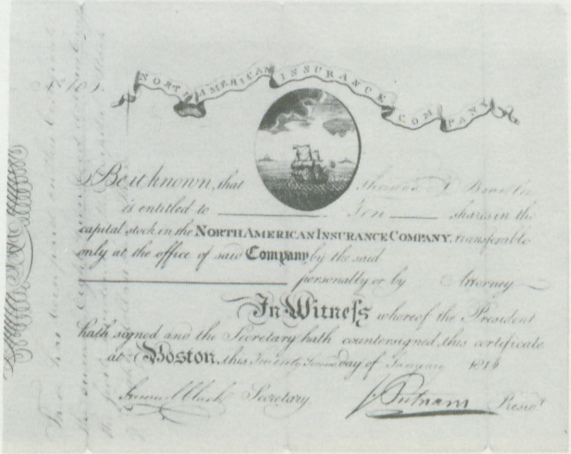
Commercial Bank Affiliates

Commercial banks had several incentives for competing aggressively for underwritings, and their activities in this field expanded substantially. Many functions performed by the commercial banks were associated quite closely with securities investment and underwriting seemed a natural extension of such departmental services as savings, corporate trusts and mortgage loans. Banks had many customers for whom they could originate securities, and there was a natural market for new issues among their correspondents. Securities could also be offered to their customers at a lower cost than when purchased from another underwriter. A more powerful influence, perhaps, was the sweeping change in the earning assets of commercial banks. Commercial loans, traditionally the preferred outlet for commercial banks' funds, declined steadily as a percentage of total earning assets after 1920, dropping from 57 per cent of the portfolios of national banks to approximately 35 per cent in 1929. The primary factor in this decline was the increasing number of businesses, chiefly in manufacturing, which reinvested earnings and financed expansion through the capital markets. Under the pressure to find outlets for their funds, banks turned more and more toward lending on securities, and partly as a result of the experience gained in this way, to the employment of funds in investment banking.

Underwriting was carried on either by a department within the bank or by an affiliated corporation. The affiliate was usually owned by the stockholders of the commercial bank on a pro rata basis. The first affiliate on record, the First Securities Company, was organized in 1908 by the First National Bank of New York. The National City Bank of New York followed suit in 1911, establishing the National City Company, and during the ensuing decade banks in the major centers, as well as some smaller areas, established affiliates. The number of national and state banks operating directly in the securities business rose from 262 in 1922 to a peak of 451 in 1929. Similarly, affiliates rose from 18 in 1922 to 180 in 1930. Among the banks in New England which formed affiliates in the late teens or early 1920's were Boston's Old Colony Trust Company, First National Bank of Boston, National Shawmut Bank, and Atlantic National Bank.

The increase in the number of larger banks more extensively and directly involved in underwriting supplied additional facilities for the expanding volume of securities. Banks and bank affiliates participated as distributors in 37 per cent of all bond issues by dollar volume in 1927 and in about 60 per cent in 1930. The old line houses continued to be the chief distributors of securities, but the larger affiliates like Chase, National City and Guaranty grew in importance and before 1920 had established branches in Boston.

The depression of the early 1930's led some banks to withdraw from the securities business, and subsequently the Banking Act of 1933 prohibited the banks from engaging directly or through affiliates in the corporate securities business. Banks were forced to choose between investment or deposit banking, which resulted in dissolution or severance


North American Insurance Company
Be it known, that
is entitled to Ten shares in the
capital stock in the North American Insurance Company, transferable
only at the office of said Company by the said
personally or by Attorney
In Witness whereof the President
hath signed and the Secretary hath countersigned this certificate
at Boston, this day of
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of the security affiliates. One of today's well-known houses, The First Boston Corporation, began as the security affiliate of a Boston commercial bank. The distinction between investment and deposit banking in American law, never hard and fast prior to 1933, had developed by usage or custom and the market tended to sharpen it through common practice. As the banking system developed, deposit banking became more and more a function of commercial banks; private bankers performed this function with diminishing frequency and investment bankers abandoned it entirely. The new legislation of 1933 formalized this specialization.

The tables which follow present the most comprehensive data available on the role of New England investment bankers as underwriters of domestic and foreign corporate and foreign government securities issues during the period 1922 to 1930. The data reflect both refunding and new money issues. The first table classifies by type of security the issues which New England investment bankers originated, purchased singly or purchased as head of an underwriting syndicate. The second shows the volume of issues with which New England investment bankers were associated as members of underwriting syndicates; they frequently occupied second or third position in the syndicate.

Origination of Corporate and Foreign Securities by New England Investment Bankers, 1922-1930
(millions of dollars)

Type of Securities	*1922*	*1925*	*1926*	*1927*	*1928*	*1929*	*1930*
Bonds							
Railroads	24	6	13	34	1	—	—
Utilities	123	122	111	85	69	102	49
Industrial & Miscellaneous	82	28	28	24	66	9	—
Financial & Real Estate	12	2	1	18	4	11	—
Foreign, Government and Private	15	—	84	16	92	—	—
Total [1]	256	158	236	176	231	122	49
Number of Issues	85	56	53	50	42	18	2
Preferred Stocks							
Railroads	—	1	—	—	—	—	—
Utilities	6	21	17	9	8	71	—
Industrial & Miscellaneous	36	2	8	12	53	13	—
Financial & Real Estate	2	—	10	5	15	22	—
Foreign	—	—	—	—	—	—	—
Total [1]	44	24	35	26	76	106	—
Number of Issues	7	17	17	26	22	14	0
Common Stocks							
Railroads	—	—	—	—	—	—	—
Utilities	—	—	—	—	4	7	—
Industrial & Miscellaneous	10	2	1	12	14	8	—
Financial & Real Estate	—	—	1	1	2	44	—
Foreign	—	—	—	—	—	—	—
Total [1]	10	2	2	14	20	59	—
Number of Issues	3	2	3	10	15	13	0
Total Number N. E. Issues	95	75	73	86	79	45	2
Total Volume of N.E. Originations	310	184	273	216	327	287	49
Total United States' Issues	3,706	5,529	5,924	8,232	8,507	10,157	6,093
New England as a per cent of United States	8.4	3.3	4.6	2.6	3.8	2.8	.8

[1] Details may not add due to rounding.

Source: For 1922 the *Commercial and Financial Chronicle*
For the years 1925-30 *American Underwriting Houses and Their Issues*
For United States totals *Statistical Abstract.*

Underwriting Originations and Participations

The issues of securities sponsored by houses headquartered in New England ranged from $100 thousand to $50 million and covered a variety of businesses. The financing included issues of a number of the region's small and medium as well as larger businesses. In 1920, for example, a $400 thousand preferred stock issue of the A. C. Gilbert Company, manufacturers of "Erector" sets and later of "American Flyer" trains, was offered by Charles W. Scranton of New Haven and Richter & Company in Hartford. For Shattuck Chocolates — now part of Schraffts — Estabrook & Co. offered an issue of $500 thousand of preferred stock. The New Britain Machine Company, now widely known in the machine tool industry, offered $500 thousand of preferred stock through Warren & Company of New Haven, and the New Bedford Gas and Edison Light Co. offered $572 thousand in bonds through E. H. Rollins & Sons.

The larger houses in the region made available to local enterprises the knowledge and experience gained from a diversified business and provided through their branches a broader market for the securities. Orpheum Circuit, Inc. offered $3.5 million of common stock through Richardson & Hill; and General Electric, $15 million of bonds through Lee, Higginson and J. P. Morgan. Union Twist Drill of Athol, Massachusetts, manufacturers of drills, taps, reamers and other metal

Corporate and Foreign Securities Offerings in which New England Investment Bankers Participated as Underwriters, 1922-1930
(millions of dollars)

Type of Securities	*1922*	*1925*	*1926*	*1927*	*1928*	*1929*	*1930*
Bonds							
Railroads	189	10	12	44	23	68	41
Utilities	236	348	438	770	574	321	773
Industrial & Miscellaneous	133	120	127	120	84	94	113
Financial & Real Estate	4	1	38	10	30	115	116
Foreign, Government and Private	242	344	244	471	412	124	431
Total [1]	804	823	859	1,414	1,124	721	1,475
Preferred Stocks							
Railroads	—	8	—	—	—	—	—
Utilities	16	174	40	66	60	102	64
Industrial & Miscellaneous	—	23	17	45	66	68	74
Financial & Real Estate	—	—	8	9	14	193	—
Foreign	—	—	—	1	4	—	—
Total [1]	16	205	65	121	144	362	137
Common Stocks							
Railroads	—	—	—	—	—	—	—
Utilities	—	—	—	4	—	8	—
Industrial & Miscellaneous	—	27	11	5	61	68	22
Financial & Real Estate	—	—	—	—	38	168	34
Foreign	—	—	—	—	—	3	—
Total [1]	—	27	11	9	100	248	57
Total New England Participations	820	1,055	935	1,544	1,368	1,331	1,669
Total United States' Issues	3,706	5,529	5,924	8,232	8,507	10,157	6,093
New England as a per cent of United States	22.1	19.1	15.8	18.8	16.1	13.1	27.4

[1] Details may not add due to rounding.

Source: For 1922 the *Commercial and Financial Chronicle*
For the years 1925-30 *American Underwriting Houses and Their Issues*
For United States totals *Statistical Abstract.*

trades equipment, offered $3.1 million of common stock through Estabrook & Co., Hayden, Stone & Co., and Parkinson & Burr.

Large companies outside the region were also financed. In the mid 1920's Coffin & Burr originated or participated in underwriting the issues of a great number of public utilities scattered over the United States, including large issues of Texas Light & Power Company. During this period E. H. Rollins & Sons did the largest volume of corporate underwriting of any Boston house and such leading houses as Kidder, Peabody; Lee, Higginson; Jackson & Curtis; F. S. Moseley & Company; Bond & Goodwin Inc.; Paine, Webber; Hayden, Stone; and Hornblower & Weeks were associated with one or another of a wide variety of issues. They included such names as Goodyear Tire & Rubber, Shell Union Oil, Victor Talking Machine, Marshall Field, Filene's, Gilchrist's, International Paper Company, S. D. Warren Paper, United Drug, Canadian Pacific Railroad, National Leather and Phillips Petroleum.

Bonds predominated among the securities originated by New England houses during the 1920's. The volume varied greatly from year to year, trending generally downward from a high of $297 million in 1922 to $122 million in 1929 and trickled off to nothing during the early 1930's. Foreign government and domestic public utility issues were the types of bonds most frequently offered. These included such large issues as those of $24, $11 and $41 million of the Province of Buenos Aires, Argentina, and such small ones as a $100 thousand issue of the Beaver Valley Water Company purchased singly by H. M. Payson & Company. The peak volume of equity issues came in 1929 when $106 million of preferred and $59 million of common stock were originated. Investment bankers in New England originated in various years during the 1920's between 3 and 10 per cent of the amount of securities issued in the United States. Since available data are incomplete they understate to some degree the volume originated in New England.

During this period, New England investment bankers were more active as members of syndicates formed to underwrite bonds than of those which purchased equity issues. Only in 1929 did the dollar volume of equity issues in which they participated approach the volume of bond offerings. Participations in preferred stock issues were larger in volume than in issues of common. It is estimated that in no year during the 1920's did New England houses participate in more than one-quarter of the national volume of corporate and foreign security issues. The extent of their participations, however, amounted to 60 per cent in 1931, a year of relatively small volume in the nation. In that year, public utility bond issues dominated the new issue market and New England houses participated in most of them.

Although commercial banks and their security affiliates originated only moderate amounts of bond issues during the 1920's, they participated in a large volume. Peak volume of issues with which they were associated reached over $537 million in 1927. In 1930 the volume in which New England banks participated as purchasers rose to two-thirds of a billion, and remained high in the following year. National banks were never permitted to deal in corporate stock but state banks did originate and participate in a considerable volume of stock issues — chiefly preferred. The total volume of common and preferred stock issues in which New England state banks and their affiliates participated reached $64 million in 1927 and a peak of nearly $124 million in 1930.

From 1934 to mid-1938 the Securities and Exchange Commission collected data on originations of and purchase group participations in registered corporate issues by location of underwriting houses. Over 80 per cent of the $7.6 billion of securities issued was bonds. Investment bankers in New England managed between 2 and 3 per cent of the issues and took purchase group participations amounting to about 5 per cent of the total. During this period Boston was the third ranking investment banking center in the country measured either in terms of the volume of issues managed or by the total amount of purchase group participations. Other evidence shows that public utility bonds was the type of security most commonly underwritten by New England's investment bankers during the late 1930's.

Underwriting of Corporate Issues in Excess of $1,000,000 Registered with the Securities and Exchange Commission from January 1, 1934 to June 30, 1938
(millions of dollars)

Location of Underwriting Firms	*Issues Managed* Number	*Issues Managed* Amount	*Amount of Purchase Group Participations*
New York City	524	6,686.4	5,861.4
Chicago	75	401.2	512.8
Boston	33	154.6	343.2
San Francisco	17	35.9	129.6
Philadelphia	14	32.6	154.4
Connecticut	7	31.5	22.8
Maine	3	5.2	5.1
Massachusetts (except Boston)	—	—	2.2
Rhode Island	—	—	10.6
New England Total	43	191.3	383.9
National Total	745	7,583.9	7,583.9
New England Total as a Per Cent of the National Total	5.8	2.5	5.1

Source: Securities and Exchange Commission, *Selected Statistics on Securities and on Exchange Markets*, Washington, D. C., August 1939.

Municipal Underwriting During the 1920's

Throughout the 1920's the annual volume of municipal bonds offered in the nation ranged between $1 billion and $1.5 billion. The previous peak of about $500 million was reached in 1916. Population increase, rising incomes, and improvement in standards of living led to a demand for public improvements. The volume of municipals issued in New England grew less rapidly than in the nation, however, and remained relatively small, ranging between $40 million and $70 million. The general framework of investment banking facilities for marketing municipals developed. The characteristics of the municipal market established before World War II continued through the 1950's but in more fully developed form.

In contrast to the corporate field, only a small percentage of the number of municipal issues had a principal amount of $1 million or more, but these issues accounted for a substantial part of the total principal amount of all issues. The market could be generally described as consisting of a large number of small issues, and provided business well suited to dealers in the smaller communities. Firms operating in this market fell into two groups—the relatively small number of houses which carried on a national business and who bid for the larger issues; and second, the large number of small houses with relatively small capital whose business was mainly the purchase and sale of many small issues but which participated to some extent in accounts bidding for the larger issues.

In municipal financing, the undivided account was generally used in the East while the divided account was frequently used in other sections of the country and commonly called a "western account." In contrast to corporate underwriting, there was no selling group. The use of these different types of accounts in the East and West continues today. In both types the participant obligates himself to purchase a fixed percentage of the issue. In an undivided account each participant continues to be liable for any unsold balance in the account in proportion to his underwriting interest, whether or not the participant has already sold more bonds than his original commitment. Each participant receives a concession on all sales made by him. In a divided account, the participant's liability is reduced dollar for dollar by his sales.

Participations in municipal accounts are usually determined on the basis of the capital resources of the participating dealers or underwriters, consideration being given to the selling ability of each in relation to his participation. The use of the divided account in the West was probably attributable to the smaller capital of the local houses operating in this field. In the East, on the other hand, widespread use of the undivided account had been characteristic of corporate underwriting, and this tradition has been continued. This method has advantages in that it puts a premium on the sales ability of a particular firm and improves the chance of attracting dealers to make up the syndicate, especially in the case of the larger issues handled by eastern houses. It is now used in the West in handling large issues, particularly by bank underwriters.

Although investment banking facilities in western parts of the nation expanded in the 1920's with the rapid rise in the number and volume of issues, they were still inadequate to meet the demands. New England houses accordingly underwrote a number of extra-regional issues as did firms in other eastern centers. In addition, the houses participated in syndicates with firms from outside the region in underwriting a growing volume of issues originated in various sections of the nation. As the larger cities in the Mid and Far West became financial centers in their own right during the latter part of the 1920's, local issues were underwritten for the most part by local investment bankers, and activities of outside houses were limited to participation in syndicates formed to underwrite the large state and city issues — "general market names" — of a given region.

Marketing Municipal Issues

The number of municipal underwriters domiciled in New England in the early 1920's was smaller than before the war, but the houses, generally because of merger, were larger in capital size. Several of the firms, including R. L. Day & Co., Merrill Oldham & Company, Edmunds Brothers, E. H. Rollins & Sons and Estabrook & Co. were active in the national market, regularly taking major positions in syndicates formed to handle large issues from various regions. The local New England business was well divided among the rest of the houses. Except for one or two firms, all 27 of the New England houses underwriting municipals in the early 1920's were located in Boston. By the mid-20's, however, firms doing a municipal business were established in other large cities in the region. There were eight houses located in Hartford or New Haven and a few firms in Portland and Providence which specialized in handling municipals issued in their own states. About 15 per cent of the total New England issues was underwritten in New York. As branch offices of New York houses increased in number in New England, they became more important as underwriters of New England issues. In the early 1930's these firms underwrote about one-fifth of the total dollar volume of the New England municipals issued. New York firms also joined with New England firms to underwrite the region's large issues. By 1933 more than one-third of the New England issues were purchased by syndicates of this kind, which had been almost unknown before World War I. This vigorous entry of New York firms into the New England market partly reflects the developing financial and trade relationships between New York and southern Connecticut, as well as the increasing centralization of the securities market in New York City. Some New England issues sold better outside the area and the nationwide distributive facilities of New York firms made them logical choices for participation in underwriting syndicates.

New England commercial banks and security affiliates offered increasing competition to investment banking firms in marketing regional issues during the late 1920's, and became an even more important market influence in the early 1930's. Investment banking houses felt the initial impact of the depression more acutely than the commercial banks and many of the houses were forced to retreat from overextended positions and were unable to continue to underwrite. Some houses failed. In effect, banks and their affiliates came to the aid of the units of local government, and underwrote about half the amount of the issues. As much as 20 per cent of the amount was bought outright by the banks and affiliates.

Municipals in the Depression

The 1930's depression sharply reduced local government revenues and many communities which had issued a large number of bonds in previous years were forced to default. By 1933 about $200 million of municipal securities were in default, and 3,238 of the nation's political subdivisions reported bonds in default on November 1, 1935 — the largest number for any of the depression years.

New England states and municipal governments experienced less than 10 defaults, a record superior to that of other regions and the result in part of conservative debt ratios and the fact that many expenditures had been financed from general revenues or with the aid of specific taxes. The region reported few emergency loans to liquidate tax titles and similar types of relief by legislative action. New England governments were thus able to issue new bonds in a period when those of other areas could not. In 1932 the volume of new issues in the region reached a record peak while the national total was at its lowest point for the decade. By the close of the 1930's investment bankers regained strength in the New England municipal market and commercial bank participation was reduced to pre-depression proportions.

By the opening of World War II municipal underwriting in New England was following a fairly distinct pattern. New England underwriters bought about one-quarter of the New England issues; and about three-fifths were purchased by syndicates which included members from both New England and New York City. A few New England issues were purchased entirely by New York City firms. Underwriters in New England frequently were members of syndicates formed to purchase the large issues originated in various parts of the country but seldom acted singly in the purchase of an entire issue.

Regulation of the Investment Banking Industry

Formal regulation of the securities business did not begin in the United States until shortly before World War I. Until then the sale of securities was conducted for the most part without restraint. Legal remedy was available in the case of fraud or misrepresentation but "let the buyer beware" was the generally accepted basis of procedure. The increasing investor class and the rising volume of securities offered led to a popular demand for protection in the pre-World War I period and again after 1929. The first response was a series of state laws popularly called "blue sky" — a

Municipal Bond Underwriting
(millions of dollars)

	1920	*1925*	*1930*	*1933*	*1940*
Total N. E. Issues	43.2	59.8	76.7	57.7	55.9
Underwritten in N. E.	32.4	42.8	54.2	17.4	14.6
Underwritten Outside N. E.	7.0	6.8	14.5	10.8	7.9
Underwritten by Mixed Syndicates	3.8	10.2	7.9	29.5	33.4
Underwritings of Outside Issues by Investment Bankers in N. E.	6.0	1.1	0.6	0.2	0.1
Outside Issues Underwritten by Mixed Syndicates	40.2	60.8	61.3	40.2	419.0
Total of All State and Municipal Issues in the U. S.	773.7	1,404.7	1,382.9	1,127.6	1,497.7
New England Portion of this Total	5.6%	4.3%	5.5%	5.1%	3.7%
Number of N. E. Investment Banking Houses which Underwrote Municipal Issues	27	42	33	41	40

Source: *The Bond Buyer.*

term based on a legislator's remark that some companies sought to "capitalize the blue sky."

Kansas, in 1911, was the first state to require a comprehensive licensing system applicable to securities and persons engaged in the securities business, and its legislation profoundly effected the development of blue sky laws elsewhere. As a result of the success of this act, 36 other states adopted similar legislation in the next nine years, though most was passed in 1912 and 1913. These statutes were of two main types — the punitive or "fraud" type, which provided penalties for fraud after securities had been sold, and the regulatory type which attempted to prevent sale of fraudulent securities. Kansas and the many states which followed its lead combined the English theory of full disclosure with the doctrine that an administrative agency should pass upon the soundness of a proposed issue. These laws also provided for careful examination of the business affairs of issuers before the granting of registration or licenses — so-called "registrations by qualification." Securities of railroads and public utilities were exempt from these laws as they were reviewed by the Interstate Commerce Commission and by state utility commissions. Government securities of all types were also excluded.

During the 1920's, the period of heavy investment and speculation in securities, progress was made toward agreement on uniform types of state securities legislation and toward developing standard financial and administrative procedures. This tended to benefit both issuers and dealers, as well as prevent and punish fraud. Every state except Nevada adopted some type of securities legislation. During the early depression, many state legislatures and regulatory commissions tightened their laws and administration. However, the system of state regulation proved unable to overcome its basic defects — lack of jurisdiction over interstate trading in securities, lack of facilities for maintaining adequate vigilance and failure to make generally available the information obtained from companies and dealers in their applications. The popular demand for additional protection against the sale of fraudulent securites led inevitably to federal legislation affecting the investment banking industry. Prior to this, however, many security houses had suggested federal legislation as a means of avoiding the conflicting requirements of the state statutes when business was done under several jurisdictions.

Before 1933, the federal government, under an Act of 1909, had exercised limited control over interstate sales of securities by prohibiting fraudulent use of the mails, and by controlling railroad issues through the I.C.C.

Beginning in 1933, Congress passed several acts affecting the investment banking industry directly — the Securities Act of 1933, the Banking Act of 1933, the Securities and Exchange Act of 1934, the Public Utility Holding Company Act of 1935, the Maloney Act of 1938, the Trust Indenture Act of 1939, the Investment Company Act of 1940 and the Investment Advisers Act of 1940. Through these acts the Securities and Exchange Commission was established and provided with broad powers for supervising the securities business. The connections between commercial banks and their security affiliates were dissolved, commercial banks were prohibited from underwriting or dealing in corporate securities and the size and structure of public utility holding companies were limited and defined. In 1940, utility underwriting was brought under S.E.C. control, leading eventually to public competitive bidding in most utility underwritings. The Maloney Act authorized the establishment of the National Association of Security Dealers with rules of fair practice approved by the S.E.C.

The Securities Act of 1933, as amended, does not attempt either to prevent the sale of speculative securities or judge the merits of particular issues; it simply provides that complete and accurate information regarding securities offered for sale in interstate commerce be made available to prospective purchasers, and that no fraud be practiced in such sales. Since fraud is unlikely when complete disclosure is made, the first of these two requirements is of primary importance in securities market control.

Chapter V

Financing Since World War II

The postwar period, except during its brief recessions, witnessed security flotations increasing rapidly in volume, exceeding by a considerable margin the heavy demands of the 1920's. This was particulary so during the boom of 1955-57. Capital was demanded by a broad range of new industries such as plastics, synthetic textiles, electronics and automated equipment, as well as by established manufacturers, utilities, service industries and financial institutions. New plants were built, older establishments modernized, and machinery purchased in record volume. Productivity improved as many processes were automated and capital investment per worker increased. Air transportation developed rapidly, railroad rolling stock was modernized, and a network of limited access highways was constructed.

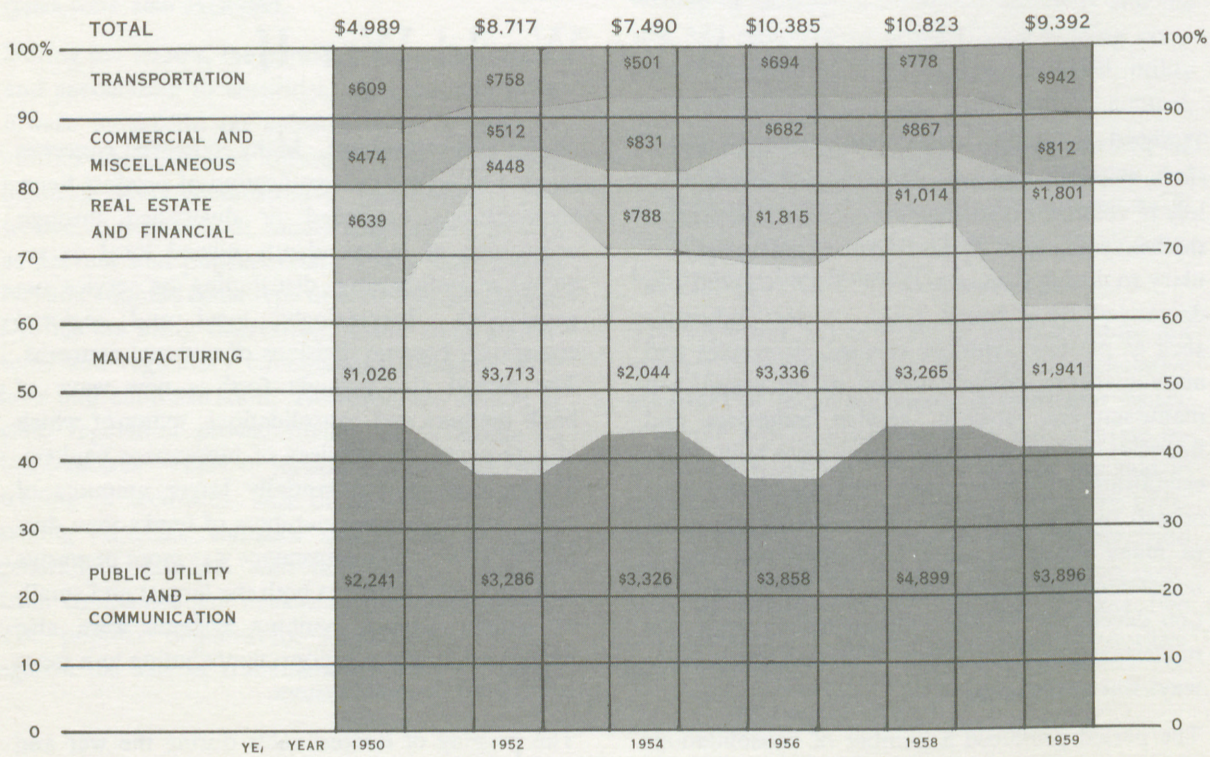
The period produced a number of consolidations and large scale chain enterprises such as hotels, motels and restaurants. Many industrial concerns merged to provide diversification of product lines. Corporations expanded or diversified through acquisition of independently owned local or regional manufacturing, distributing or service organizations. Increasingly, local and regional enterprises became divisions of national concerns. The period also brought forth a new wave of bank mergers and consolidations, many of which also required the services of investment bankers. These involved substantially larger amounts of assets although fewer numbers of banks than during the 1920's. The movement was more pervasive and embraced banks in both the largest and smallest cities. Branch banking systems were also developed in many regions, contributing to a more centralized financial system.

The pegging of interest rates during the war and early postwar period induced refunding of issues on a large scale. After flexibility in credit policy was restored with the Treasury-Federal Reserve Accord of 1951, refundings also appeared in volume during periods of monetary ease in 1954 and 1958. These offerings were thus added to new corporate issues, increasing the total volume. Privileged subscriptions, secondary distributions and the initial public marketing of stock by large established concerns, such as Ford Motor Company, increased, as did the stock of smaller, closely held corporations. In the public sector, there were mounting demands for capital by the federal government and by states and municipalities.

National Character of the Capital Market

During the period after World War II, the national character of the long term capital market centered in New York City underwent further refinement. This development is a product of slow evolution since the mid-1880's when markets were distinctly local or regional, differed markedly in size, and had relatively few connecting links. The influence on market development of the non-bank financial intermediaries — life and casualty insurance companies, investment trusts, pension funds, personal trusts, and savings institutions — has been striking, because of both their sources of funds and the type of securities they purchased. Specialization has developed to meet the needs of large classes of borrowers and lenders and transactions are now accomplished more rapidly and at low cost. These changes accompanied the improvements in communications systems, knowledge of markets and new provisions for the transfer of funds and other money market investments. The investment banking industry serves as one of the unifying forces in the national capital market.

PERCENTAGE DISTRIBUTION OF
DOMESTIC AND FOREIGN CORPORATE SECURITY ISSUES FOR NEW CAPITAL
UNITED STATES, 1950—1959
(MILLIONS OF DOLLARS)



SOURCE: Securities and Exchange Commission

Approximately 3,500 firms are now engaged in various branches of the securities business in the United States. Among these are 100 firms which play the leading role in originating and distributing new security issues and in making markets for unlisted securities. The various houses in this group regularly appear as managers, co-managers or major participants in large corporate and municipal offerings. At times, they bring large numbers of selected dealers in various parts of the country into the final placing of the issue.

Ranked in terms of capital, 9 of the first 10 of these houses, with capital ranging from $21 to $55 million, are located in New York City, as are a large number of the other 100 leaders. Approximately 20 firms with sufficient capital and reputation to originate and distribute securities and with staff facilities to conduct related business, are found in Chicago, San Francisco, Boston and Philadelphia. The rest of the leading firms are located in the principal cities of every region of the country. Most of the New York firms are also closely linked to the principal cities in the nation through branches, correspondents and direct wires. The firms outside, in turn, have similar direct links with New York and particularly with other cities in their regions. All facilities for trading the great bulk of corporate, federal government, and many municipal securities have come to be based in New York, both in respect to quotation and market breadth.

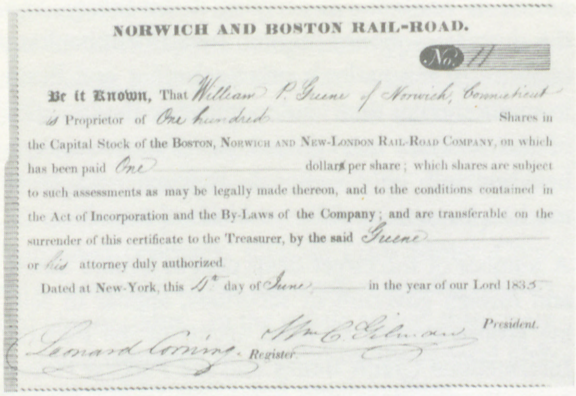
Links Among Markets

To the extent that regional markets remain, they have become quite closely tied to the national market, partly through the interrelationships which exist within particular investment banking firms. The fact that most houses have important interests in several markets assures a close relationship between the actual developments in local or regional and national markets. Shifting investor preferences among corporate bonds of differing quality and yields and among corporates and municipals or governments help to tie markets together. There is also a direct link between the house, as borrower in carrying its inventory, and the short term money market. Investment banking facilities in the nation's principal cities and those in smaller towns thus tend to integrate the facilities of the national market and provide connections between not only national, regional and local markets but among different kinds of securities.

A number of the larger firms deal in United States and foreign government securities, appear in selling groups formed by fiscal agents of the Federal Intermediate Credit Banks and the Federal Home Loan Bank, make markets in agency issues and participate in municipal underwriting. Some are among the leading dealers in the over-the-counter market and many have memberships on the New York or other exchanges. A few also deal in acceptances and commercial paper. Whether or not the firms participate in other markets, all are obliged to consider developments in these markets in dealing with customers who move from one market to another.

Of the total net debt in the nation, one third is composed of obligations of federal, state and local governments. These securities are exchanged in national markets at virtually uniform prices for a given security. The widespread ownership and convenient liquidity of government securities supply a common denominator for the entire credit system. Federal legislation creating lending authorities, loan guarantee programs and deposit insurance has also contributed a unifying influence in credit markets. For individual borrowers and lenders, there are relatively few areas in which access to markets is indirect. Rate relationships in the money market are more consistent and the differentials in rates have substantially diminished. All forms of domestic financing have become sensitive, whether preponderantly or marginally, to the influences of a national credit market.

Changes in the channels of supply of loanable funds have been a major factor promoting the national fluidity of credit. The number of investors who place their funds directly is relatively smaller. More and more reliance has been placed on major financial intermediaries. These institutions accumulate the great bulk of individual liquid savings and place them in broad regional or national pools. Each of the major types of inter-



NORWICH AND BOSTON RAIL-ROAD.

No. 11

Be it Known, That William P. Greene of Norwich, Connecticut is Proprietor of One hundred Shares in the Capital Stock of the Boston, Norwich and New-London Rail-Road Company, on which has been paid One dollars per share; which shares are subject to such assessments as may be legally made thereon, and to the conditions contained in the Act of Incorporation and the By-Laws of the Company; and are transferable on the surrender of this certificate to the Treasurer, by the said Greene or his attorney duly authorized.

Dated at New-York, this 15th day of June in the year of our Lord 1835

Leonard Corning, Register

President.

mediary is tied more closely than the smaller saver to the national credit market. Investment action of institutions is directed by informed persons who are sensitive to developing profit opportunities within the capital market; some of these institutions will switch from bonds to mortgages as yields become more attractive in one market as compared with another. They are the leading participants in evolving secondary markets for private credit instruments. Along with their wide reach of investment commitments, these institutions marshall savings over a considerable area by means of aggressive sales and promotional efforts. As a result, even the most geographically restricted of these institutions, savings and loan associations, are influenced by lending practices followed by their national competitors.

Long term debt held by all financial institutions, including public trust funds, increased from about $40 billion in 1920 to $250 billion in 1945 and to $540 billion in 1959. During the 1920-1959 period, the proportion of long term debt, public and private, held by these institutions rose from 49 to 78 per cent. Close to half of the long term debt not held by institutions, $48 billion, is represented by individual holdings of savings bonds. Much of the remainder consists of public and private marketable securities held by individuals.

Life insurance companies, with $94 billion of reserve funds, constitute the largest group of investing agents and are most importantly involved in redistributing the savings throughout the nation. In recent years, private and state and local government pension funds have become an increasingly important part of institutionalized savings.

Financial Intermediaries in New England

New England is the home of a large number of institutional investors whose assets and inflows of funds represent major fractions of the national totals held by such institutional groups. All forms of these institutions in the region have a long history extending back in some cases to the early 1800's. Their recent growth has paralleled that in the nation. This explains in part the dominance of New England investment banking houses in past periods, and in part the current position of the houses and branches domiciled in the region as a significant part of the national market.

The insurance firms headquartered in the region, the life, fire, marine and casualty groups, account for about a fifth of the assets of these institutions in the nation. The assets of the region's investment trusts represent over 31 per cent of the total assets of the open end trusts. The region's mutual savings banks hold 27 per cent of all mutual savings bank deposits, and personal trusts and agencies administered by the commercial banks approach 12 per cent of such property in the nation. In addition, about 5 per cent of both total bank administered and state and local government pension funds are located in New England. Boston also continues to be the home of a number of private or "Boston Trustees" estimated by the investment community to administer about $1 billion of trust assets.

The Individual Investor

Although the relative importance of institutional ownership of bonds and stocks has increased, with investment trusts taking about half of the net new stock issues in the last 5 years, individuals remain the most important holders of equities. At the end of 1959, individuals owned directly 70 per cent of the corporate stock not owned by another corporation. These holdings were valued at $210 billion. Personal trust funds administered by banks held another 14 per cent and nonprofit organizations, 6 per cent. The remaining 10 per cent was held by financial institutions, including investment companies, insurance companies, non-insured pension funds and mutual savings banks.

The number of stockholders in 1960 was approximately 13 million, or one adult in eight. This is a larger number than at any previous time; but the ratio is probably no higher than in 1930 when there were an estimated 10 million individual stockholders. The distribution, by size of holding, of specific stock issues became less concentrated during the last 10 years. In 1957 at least 40 per cent of dividends paid to individuals was received by those in the top 1 per cent of income bracket, while 60 per cent was received by those in the top 10 per cent bracket.

Stock Ownership in New England

New England continues to be a region where personal incomes and individual liquid asset holdings are high in comparison with the national averages. The individual purchaser accounts for an important portion of funds which flow into fixed capital throughout the nation, and is an important factor to be considered by investment banking houses when planning office location.

In 1959 the New York Stock Exchange estimated that slightly over one million individual stockholders live in New England. Over 10 per cent of the total population in New England held stock as compared with 7 per cent in the United States as a whole. In the New York, New Jersey and Pennsylvania area 10.5 per cent were stockholders, the only other region where this figure exceeded 8.5 per cent. Since 1956 the number of New England stockholders rose only 7 per cent while the total in the United States rose 45 per cent. On the other hand, the fraction of the region's residents who own stock rose from 9.9 per cent to 10.4 per cent. The recent spread of stock ownership in New England has been less than in other regions because it had proceeded farther here originally. Per capita dividend receipts in New England are higher than the national average by more than 50 per cent, suggesting that per capita ownership of stock is higher also. New England continues to be an important individual market, not only for outstanding securities but for new issues as well.

The Currently Active Individual Investor

In late 1959 the house of Merrill Lynch, Pierce, Fenner & Smith, Inc. gathered information from their active account holders by means of a mail questionnaire. The questionnaire was sent to all persons for whom the firm was holding cash or securities. Approximately 140,000 replies were received, 5,000 of them from New England. The accompanying tables show separately the characteristics of the respondents from New England and from the entire nation.

Analysis of these tables suggests that in New England the firm's customers are slightly younger than in the nation generally, perhaps because the Boston offices have a shorter history of activity than offices elsewhere. The tendencies for New England customers to report smaller portfolios than nationally, and to have lower incomes, are probably explained by the greater frequency of younger investors among the firm's customers in the region. The occupational characteristics of the customers are quite similar to the national group. To correct for the different age and income patterns, separate comparisons of the New England investor and the national investor were made for each age and income group as to value of security holdings and types of securities held. Corresponding comparisons were made in each occupation group. They reveal several noticeable differences.

In most age, income and occupation groups, the value of the securities owned by active New England investors is comparable to the value of the securities owned by active investors throughout the nation. There is some indication that active investors in the region in the 21 to 40 years of age group have larger portfolios than young investors elsewhere. New England investors over 60, on the other hand, reported comparatively smaller portfolios. It should be remembered that regardless of location, value of security holdings tends to

A Profile of the Currently Active Investor New England and the United States

	Per Cent of Investors United States	Per Cent of Investors New England
Age		
Under 40	37	46
40-60	45	40
Over 60	18	14
	100	100
Annual Income		
Under $10,000	56	62
$10,000-$20,000	31	28
Over $20,000	13	10
	100	100
Occupation		
Salaried Employee	46	45
Professional	21	23
Proprietor	9	9
Housewife	7	8
Retired	11	9
Other	6	6
	100	100
Value of Security Holdings		
Under $10,000	45	49
$10,000-$50,000	35	34
Over $50,000	20	17
	100	100
Period of Earliest Security Purchase		
1950-1959	61	66
1940-1949	19	18
pre 1940	20	16
	100	100
Percentage of Investors Owning Securities by Type		
U. S. Government Bonds	32	29
Municipal Bonds	6	5
Corporate Bonds	10	12
Preferred Stock	12	12
Common Stock	98	97
Mutual Funds	17	17

rise with age. Housewives in the region tend to hold smaller portfolios than housewives elsewhere. There is no noticeable regional difference in value of portfolio size among the other occupational groups and none among the various income groups. Figures on security ownership generally show that the value of securities held tends to increase as income increases. In this respect New England is no exception.

Practically every investor having an account with this firm has common stock as a part of his portfolio. In all areas the popularity of preferred stock, corporate bonds and municipal bonds increased with age and income, being most popular with retired persons. However, New England investors in almost all age, income and occupation groups show a stronger tendency to include corporate bonds in their portfolios than investors elsewhere. With the same uniformity of behavior, New England investors hold United States government bonds less frequently than investors in other parts of the country.

Investment Banking Houses in New England

At the close of 1960 the region's investment banking facilities comprised some 37 firms which could be classified as active underwriters — either originating or distributing corporate and municipal securities. There were 22 firms domiciled in Boston and 15 elsewhere in New England, chiefly in Connecticut, Rhode Island and Maine. These houses also engage to a greater or lesser extent in one or more of the related phases of the securities business. Approximately 129 branches of 58 New York City firms and 26 branches of 11 houses located in Chicago, San Francisco, St. Louis, and other cities were also situated in Boston and other principal cities of the region. Included among these branch offices are six of the 12 nonbank firms dealing primarily in United States securities— a larger representation of U. S. securities dealers than in any city of the nation outside New York except Chicago.

Ten of the firms now domiciled in the region trace their inception to 1900 or before. Only two of the houses presently active as underwriters were formed after 1940. The New England houses have also extended their branches and now operate a larger number than at any time since 1929.

The active underwriters with head offices in New England, like their counterparts elsewhere, originate and distribute issues of all types, carry an inventory of a fairly wide range of outstanding securities, and merchandise these securities on a wholesale and retail basis. The capital of these houses ranges in size from less than $100 thousand to more than $10 million; but the great majority have capital in the neighborhood of only $100 thousand. Nineteen firms had at least one branch office and seven of them have New York offices. Five of these firms operate branch networks in both the established and rapidly growing sections of the nation. Two of the firms are active on an international basis. Virtually all of the firms underwrite both corporate and municipal securities. Three or four of the firms specialize in certain types of corporate securities and two in municipals. Such specialization develops greater knowledge and better judgment in a particular field.

In addition to these facilities there were 238 additional firms engaged in various phases of the securities business. These firms are typically small in terms of both capital and number of employees. In capital size they vary from about $20 thousand to $100 thousand. A number are individual proprietorships or small partnerships with one or two employees in addition to the proprietor or partners. The principal business of these firms is brokerage; they carry limited inventories of securities and service a relatively small list of individual customers. On occasion, some of these firms will participate to a limited extent in large selling groups in which underwriters want to spread the risk widely and accomplish rapid and broad distribution of the offering. A few of these firms conduct only an interfirm business and in this way aid in making more continuous markets. Investment trust share distributors are also found in this group, but their work is more closely related to that of an issuer than to that of a dealer or underwriter.

Most of these firms have a high proportion of skilled or technically trained persons or officers and partners to total employees. The securities business is essentially a service industry. The success of a firm depends upon its members' broad knowledge and their ability to assess market and security values. A knowlege of clientele is equally essential. These are attributes which can not be easily passed along and the typical firm lives or dies with its management.

The financial industry as a whole is a large employer in the region and outranks a number of manufacturing lines in importance. Moreover, employment in the industry has increased during the postwar years from 74,000 to 110,000 persons. Employment in the securities business, however, has declined contrary to the trend in other branches of finance. Employment in the region has declined from about 4,500 persons in 1946 to 3,900 in 1960. This is the result of a change in character of the markets, particularly of the buying side as represented by the institutional investors. The sales to these buyers are uniformly large, and as noted below, issuers may not use the investment house for the full range of services as in the past. Other reductions in personnel have resulted from economies gained through increase in average firm size. In terms of divisions of business, retail selling still accounts for the largest proportion of employment; trading second and underwriting the smallest proportion.

Changes in Population of Underwriting Firms

The active underwriters domiciled in New England represent about half the number in existence in 1929. The region's reduction in number of firms parallels that of the nation as a whole but is contrary to that of the rapidly developing regions such as the Pacific Coast and the Southeast and Southwest, where there has been an increase in the number of independent firms able to originate and underwrite both national and local issues.

The reduction in population of firms resulted from a variety of factors. In part, this has come about by change in the domicile of firms. Six of the leading houses, Kidder, Peabody; Lee, Higginson; Tucker, Anthony and R. L. Day; First Boston; Hayden, Stone; and Hornblower & Weeks shifted their head offices to New York, retaining the Boston office as a branch. There have been several mergers involving some of both the larger and smaller houses. For example, Paine, Webber merged with Jackson and Curtis; Arthur Perry & Company and Whiting, Weeks and Stubbs joined F. S. Moseley & Company; and Chace, Whiteside merged with Perrin, West and Winslow. The firm of Parkinson and Burr became Burr, Gannett, which was later absorbed by Tucker, Anthony and Company. Subsequently, Tucker, Anthony merged with R. L. Day, becoming Tucker, Anthony and R. L. Day before removing their head office to New York. Finally, the withdrawal of other firms more than offset new entries.

Reasons for mergers of firms vary, not only within the region but also within the same community. Such reasons include the desire to increase capital, strengthen and assure continuity of management, increase size and prestige, enlarge facilities, acquire branches, reduce overhead costs and, in some cases, forestall failure. Mergers and the extension of branches since the war have reflected the need for reorienting the geographical structure of a firm in an attempt to follow shifting population centers and changes in administrative offices of large corporations.

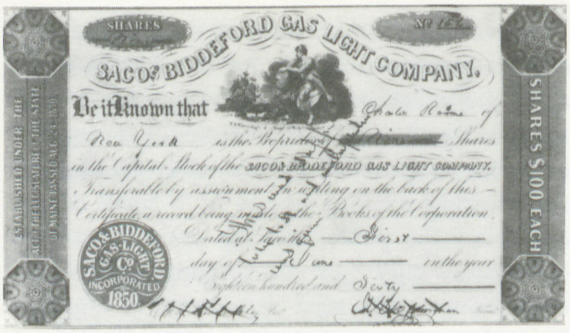
Census of Firms in the Securities Business
(Selected Years)

Boston	*1933*	*1940*	*1950*	*1960*
Underwriters	30	29	25	22
Firms with branch offices	18	12	12	12
Branches in New England	38	25	26	38
Branches elsewhere	34	35	31	51
Branch offices of New York underwriting firms	22	22	19	46
Branch offices of underwriting firms domiciled in Chicago (and other principal cities)	14	3	2	5
Additional firms with principal business as brokers, dealers, etc.	254	235	156	117
Elsewhere in New England				
Underwriters	23	19	25	15
Firms with branch offices	7	8	7	8
Branches in New England	16	17	18	18
Branches elsewhere	2	5	2	1
Branch offices of New York underwriting firms	19	33	23	83
Branch offices of underwriting firms domiciled in Chicago (and other principal cities)	6	1	2	21
Additional firms with principal business as brokers, dealers, etc.	179	164	117	121
Branch offices outside New England				
of New York (Chicago and other principal cities) underwriting firms with branches in New England	288	177	190	831

Branches of Outside Houses

There has been a steady increase since the early 1900's in the number of branches placed in Boston by outside houses. Presently, there are more branch offices in this area than in any other principal city in the nation other than New York and Chicago. Some of the branches were opened as new offices and others appeared through acquisition of firms domiciled in the region. E. H. Rollins, very active in originating public utility securities in the 1920's, was absorbed by Blair and Company of New York, which retained Rollins' offices in Boston and other areas as branches. G. H. Walker & Company of St. Louis absorbed Bodell & Company in Providence. Branch offices conduct a variety of business including brokerage, commodity dealings and investment advice. In addition, they seek contacts with industrial firms which are prospects for underwriting and negotiate private placements with institutional investors. Some of the offices are granted varying degrees of autonomy in originating and underwriting corporate securities. In one firm, each office affords its others an option to participate in their respective security purchases. In other firms, autonomy is accorded the branch only in municipals.

More particularly, the branch provides a continuous personal relationship with the large institutional buyers of securities. Some state and local pension funds and other institutional buyers will conduct business only with firms which maintain an office within their state. In some instances, the region was first serviced by traveling representatives who maintained associations with institutional buyers. The branch, however, enables the firm to make this contact more secure and allows development of the individual market which cannot be serviced satisfactorily by travelers. The



volume of potential business more than offsets the higher initial cost of the branch. The narrow market ties between local dealers and New England's institutional investors, which existed at one time, have been broken to a considerably greater extent than in such other cities as Philadelphia and St. Louis. Branch office costs are generally less than the expenses of an independent firm in the same area. Machine bookkeeping and centralized billing in the main office permit the branch to concentrate on sales and new business.

The branches of firms which previously had their headquarters in the region fall into a special category. Some of these firms have been among the leading originators and distributors for a long period of years. The transfer of head offices to New York reflects an adaptation to the changed character of the capital market and the more centralized nature of the industry. The Boston branches of these firms often continue to seek originations and maintain syndicate departments as well as serving as sales offices. They may do a substantial part of the work of originating a new issue. The territory for seeking new business may or may not be restricted, depending on the policy of the house. In most cases, the resident officers actively participate in making the firm's decisions.

Other firms with headquarters outside New England also actively solicit business in the region by telephone and regular visits of traveling representatives. These firms seek business principally with the large institutional accounts. The necessity to maintain extreme breadth in market ties inclines some institutional investors to make a practice of purchasing from distributors throughout the nation, even to the extent of purchasing small amounts of the same issue from all or nearly all members of an underwriting syndicate. Nationwide purchasing of this sort means, of course, that the total of securities absorbed in New England cannot be equated to the sales of home and branch offices here.

Organization of the Underwriting Firm

As modern investment banking initially developed, it retained some degree of functional separation of houses as wholesaler or retailer in underwriting new issues, and in conducting brokerage of outstanding securities. Varying combinations of functions performed by the same house became more frequent. Some wholesalers developed retail departments which distributed to ultimate investors the securities originated in their own wholesale department along with securities purchased from or sold on commission by other investment bankers. The retail house bought large blocks of securities from corporations or public bodies and resold part to other houses. Today, except for four or five houses which confine their activities exclusively to originating and arranging syndicates for the distribution of securities, the typical house performs a variety of services.

These services have become generally departmentalized in three areas of operation — purchasing, syndicating and retail selling. The formality and extent of departmentalization depend upon the capital size of the house and the business which it customarily handles. In purchasing securities, the house either works by itself with the issuer or joins with one or two others in an agreement to share responsibilities. Houses which make a specialty of negotiating issues, particularly those of firms making initial or infrequent public offerings or issues which are to be privately placed with institutional buyers, have a staff of professional and technical personnel. They work with the executives and financial advisers of the issuer, becoming familiar with the industry and the firm's history, current operating position and prospects. On the basis of this study, a detailed financial plan is discussed with the issuer covering the type of security and terms of the offering. Final decisions must then be made about pricing and timing the issue for the market if a public offering has been decided upon. This work is reduced in scope if the house handles only issues of established firms or if it participates in offerings under public sealed bids. Generally, the purchasing department either approves or disapproves participation of the house in moving an issue originated by another firm. Buying consists of formulating investment judgment on the soundness of the commitment, considering profitable use of capital of the house, the ability to market the securities and the suitability of the issue for customer accounts.

In the case of securities offered for competitive bidding by an issuer, the purchasing department will have to familiarize itself with the details and features of the issue. The participating underwriters then confer at "price meetings" in order to determine the final setup of the underwriting account and the bid to be submitted on their behalf by the manager. The bid reflects the price at which the entire issue can be safely underwritten and, when decided upon at the final "price meeting," the participants still in the account have agreed on the spread and offering price to the public. The difference between the bid and public offering price is the spread or gross compensation of the participants and manager. After the bids are opened, and usually without reference to the issuer, the underwriters winning the account decide on the method of sale and amount of concessions and allowances. The problem of distributing securities won in competitive bidding differs from that of a negotiated offering because there is no chance for extended preliminary discussions with prospective buyers. In many cases, the quality of securities offered under sealed bids is high and large group sales to institutions are made by the manager on behalf of the syndicate members.

The syndicate department cooperates closely with the purchasing department, planning and organizing syndicates and selling groups to underwrite and distribute the security issues. In carrying out this work, the department prepares lists of possible participants, confirms participations, prepares and accepts syndicate agreements.

The sales department resells to the public the securities purchased by the house. Except in the case of smaller houses, sales are made at both wholesale and retail levels. Wholesale transactions represent sizable blocks of securities sold to non-underwriting retailing houses at a small concession from the public offering price or to large institutional buyers for the account of the several underwriters. The sales department is organized in much the same way as the selling department of any merchandising firm. A sales manager is placed in charge of the department and salesmen are employed according to the volume of business.

The house may also have one or two other departments such as trading or statistical and research. Although all houses do some trading, generally only the larger houses have sufficient volume to justify a separate department. The work of the department arises from several sources — buying or selling securities for the accounts of the house or its customers, maintaining markets for the house's own originations now outstanding, and on occasion, supporting the market during offerings.

The work of the statistical and research department is varied. Originally established to assist the purchasing department in making appraisals of proposed issues and in following the position of the market, the department's range of operations has broadened. It may service customer inquiries for investment information, evaluate privately held securities or supply periodic market and investment letters. In some cases, it provides a detailed advisory service for issuers and investors. Some houses also offer custody and agency arrangements for both individual and institutional investors. In addition to statistical work, the department prepares prospectuses for registered issues, news releases and material used in advertising.

Since the new issue business fluctuates from year to year, and in some firms comprises a variable portion of total business, many firms develop other related business to make the activity of the firm more stable. The most important of these is brokerage and frequently the house is a member of the New York Stock Exchange, the American Stock Exchange and one or more regional exchanges. Others conduct extensive business in unlisted securities in the over-the-counter market.

The Corporation and the Investment Banker

In no period of the nation's financial history can the scope of markets and financial institutions compare with those of the post World War II period. The corporate issuer today has a wide choice of methods of supplementing retained earnings to secure funds for capital spending. The corporation's financial officers may or may not use the services of an investment banker, or they may use those services only in a limited way. The corporation may place its issues directly with an insurance company or it may meet its needs for medium and long term funds through a combined use of commercial banks and insurance companies in the form of term loans. Many corporations have also developed departments which perform financial marketing functions at various times to meet certain needs.

When the corporation uses services of an investment banker, the available types of transactions include: (1) a negotiated underwritten public offering; (2) an underwritten public offering awarded on the basis of publicly invited sealed bids, with an investment banker sometimes having been retained on a fee basis to shape up the issue; (3) the so-called "stand-by" offering, a negotiated underwritten offering to existing security holders with the investment banker taking up the securities not subscribed for or exchanged; (4) an underwritten offering to existing stockholders awarded on the basis of publicly invited sealed bids, with an investment banker having been retained on a fee basis to render professional assistance; (5) a non-underwritten offering to existing stockholders with an investment banker acting as agent on a negotiated basis; (6) a private placement or a sale and lease back with an investment banker acting as agent of the seller on a negotiated basis; (7) assistance to companies in programs of expansion or diversification by means of merger or acquisition with the investment banker acting as agent.

Regional business and industrial firms have excellent facilities for marketing security issues and no lack of buyers; but they generally must meet the test of the national market. New England's investing institutions have a superior knowledge of local conditions, although they have no specific local responsibility since they draw their funds from all over the nation. This is particularly true of insurance companies and investment trusts. These institutions are sources of long- and medium-term credit and it can be expected that they will continue to consider opportunities for investment in the area as carefully as they will those of any other region. Keen competition exists among these institutions in making investments, and the competition for their funds is equally keen among issuers scattered over the nation.

Private Placements

Privately placed securities have long played a part in the financing of corporations, but it is only in recent years that they have assumed an important role. The increased use of the private placement process is due to two underlying causes: the decline in importance of the individual investor and concurrent rise of institutional investors, and the decline in the supply of corporate securities relative to the institutional demand. Insurance companies have found it difficult to obtain enough corporate securities to meet their increasing needs. Thus, in order to be able to assure themselves of suitably-sized blocks of new securities, many insurance companies take aggressive steps to arrange for the direct placement of entire issues privately.

Other reasons have been cited for the growing popularity of private placements. Probably the one most frequently encountered is that such issues do not require registration with the Securities and Exchange Commission. The importance of the registration question is debatable. The direct expense involved in registration is a very small percentage of the money raised, although the cost of preparing and submitting the initial registration statement may well be substantial. At the same time, the statements and reports required by lenders in private-placement financing are also exhaustive, so that the net saving in this direction may be small. However, there is usually a cost saving to small borrowers who deal directly with insurance companies.

From the close of World War II through 1951 the proportion of direct placements increased each year to a peak in 1951 of nearly three-fifths of total corporate debt offerings. Since then, there has been little change in the proportion, and direct placement continues today an important competitor of underwritten offerings. Generally, these placements have been with insurance companies, with or without the assistance of an investment banker. In both cases, however, the securities are bought directly from the issuer and either eliminate all of the functions of the investment house or require only certain services by a single firm.

New England life insurance companies purchased directly from the issuers nearly 70 per cent of the $2.8 billion of securities which they acquired in 1959. The proportion was much higher in the case of some companies and of some types of securities. Private purchases were of greatest importance in the acquisition of industrial bonds; more than 97 per cent of the dollar volume was purchased directly from the issuer. In the public utility field, direct deals accounted for four-fifths of total purchases. Few direct deals were reported in connection with railroad securities or municipals.

The initiative in private placements now seems to rest with the borrowers. New England insurance companies report little solicitation of such deals on their part, stating that from 60 to 70 per cent of their prospective borrowers come to them through agents. In practically all other cases, borrowers approach the companies directly.

Influence of Taxes in Capital Markets

Tax factors have split the capital markets since the beginning of World War II. Personal income and inheritance taxes, along with certain corporate taxes, have led both individuals and some institutions to seek the shelter of tax exempt yields of state and local government bonds. Tax-privileged intermediaries, on the other hand, found the higher yields of fully taxable corporate and United States government bonds strongly attractive. Thus, the bond markets tended to align (1) state and local government bonds with individuals and institutions subject to highly progressive rates of taxation and (2) fully taxable corporate and United States government bonds with institutions enjoying tax privileges. The combination of saving and tax forces led financial intermediaries to dominate the supply of funds in the corporate bond market. After 1950 tax exempt corporate and state and local government pension funds also became important purchasers of fully taxable corporate bonds.

In part, the recent preference for bond rather than stock financing lies in United States tax legislation. Over the postwar period, corporate issues of bonds comprised about 90 per cent of the total security issues. Corporations are allowed to deduct bond interest from taxable income but there is no exemption for dividends. Other reasons include the ability to fit the definite commitment of the interest cost on bonds into long range corporate financial plans. Stock has less certain financial effects. Under inflationary conditions which have characterized much of the postwar period, the fixed cost of bond interest becomes relatively smaller. Increases in stock prices and earnings under inflation impose pressure to pay out earnings. Decisions on the form of financing are influenced by the relative cost of bond vs. stock financing in any year, and by market demand as well as corporate policy toward stockholders and the public.

The general developments cited earlier along with the legislation of the early 1930's forced the investment banking industry to adapt its operations to new conditions. In this connection, a fundamental change in the structure of the industry as contrasted with the pre-1930's was produced by the withdrawal from the field of the commercial banks and their affiliates which had engaged directly in the underwriting business. The Securities Act of 1934 imposed on each underwriter a civil liability for omission or misstatement of a material fact in the registration statement equal to the "total price at which the securities underwritten by him and distributed to the public were offered to the public." This liability, plus a transfer tax on bonds and an increase in the transfer tax on stocks which had been imposed in 1932, virtually forced underwriters to abandon the purchase of security issues jointly, or jointly and severally, as had been customary in the 1920's. Purchases, consequently, came to be made by the various underwriters in severalty — that is, with each underwriter liable only to the extent of his own participation. The banking and purchasing syndicates characteristic of earlier years disappeared.

Marketing Security Issues

During the postwar period a corporate issue of $5 million has been considered small. Frequently issues have exceeded $50 million and several have produced more than $250 million. The largest flotation since World War II has been the initial offering of Ford Motor Company's common stock amounting to about $640 million. Generally, the size of the syndicates is much larger and at times involves 200 or 300 houses in the final distribution. The trend toward larger syndicates began after 1937, when several houses found some issues so unsuccessful that the resources of a number of underwriters were seriously strained. Thereafter, participants in most issues were increased in number to spread the risk as widely as possible.

Currently underwritings are handled on the basis of an "underwriting agreement" between the issuer and the underwriters, represented by the manager, and an agreement among the underwriters. The manager, like the originating banker or manager of earlier periods, handles the negotiations with the issuer and supervises the whole process of underwriting and distribution. Dealer and group sales are still made under the authority of the manager. In making sales for the account of the underwriters, both to dealers and institutions, the manager "sells out of the pot".

The maximum life of the syndicate has grown shorter, and usually runs 15, 20, or 30 days. Some offerings have been closed out within a few hours. Depending upon the terms of the agreement, some syndicates can be extended by the manager to 60 days with or without the unanimous consent of the members. The business has become even more competitive than in the 1920's. Houses have become increasingly conscious of their position and many aggressively seek managerships or co-managerships both in negotiated issues and in issues bid competitively.

The complex of developments after World War II, along with further standardization of securities, lower interest rates during the 1940's and the increased importance of specialized institutional investors, led to further reductions in gross spreads obtained by underwriters. Negotiated underwritings of industrial bonds are accomplished much more cheaply than at any time in the past. In comparison with the 1930's, the spread has declined about 50 per cent and on high grade negotiated issues the gross spread is now frequently less than one point. Of course, underwriting costs rise as issues increase in risk or decline in marketability. Competitively bid utility and railroad securities' spreads also show a decline.

In earlier periods there were relatively few corporate issues offered at competitive bidding. Public sealed bidding increased substantially after the adoption of S. E. C. Rule U-50 in 1941 for securities of utilities affected by the Public Utility Holding Company act, and the ruling of the Interstate Commerce Commission covering all debt issues of railroads.

In addition to companies subject to these requirements, competitive bidding has been used in recent years by certain telephone, electric and gas companies without legal or regulatory requirement in making offerings. As yet, competitive bidding has not been used in industrial security offerings. Securities sold under public sealed bidding have fluctuated at around 50 per cent of the total amount of securities underwritten during the last three years.

Underwriting Originations and Participations

In the two decades following 1940 originations of corporate and foreign offerings by New England investment bankers were highly variable in dollar volume and, in contrast to earlier periods, represented only a very small proportion of the national total. More than any other phase of the investment banking business, origination of issues and management of syndicates has been concentrated in New York and to a lesser extent in Chicago. Utility and industrial securities have dominated the originations of New England houses. In recent years there has been an increase in proportion of common stock offerings as compared with bonds and preferred. The issues have included those of firms in various industries, especially the region's research-based firms engaged in electronics, atomics, automated equipment, stroboscopy and other fields. Amusement and recreation industries — among them professional football and bowling — have also been represented along with supermarket food stores. The large houses domiciled in Boston continue to view the branches of

Corporate and Foreign Securities in which New England Investment Bankers Participated as Underwriters 1940-1959

(millions of dollars)

	1940	*1946*	*1948*	*1950*	*1953*	*1956*	*1959*
Bonds							
Railroads	110	13	195	58	—	35	—
Utilities	645	283	1,312	735	704	1,329	1,100
Foreign Government and Private	—	—	—	5	96	245	66
Industrial and Miscellaneous	507	221	117	127	972	1,307	536
Financial and Real Estate	16	—	—	67	476	335	114
Total [1]	1,278	517	1,624	992	2,248	3,251	1,816
Preferred Stocks							
Railroads	—	—	—	—	—	—	—
Utilities	126	29	150	204	230	235	95
Foreign	—	—	—	—	—	3	90
Industrial and Miscellaneous	63	546	225	156	35	261	99
Financial and Real Estate	2	—	24	28	16	1	27
Total [1]	191	575	399	388	281	500	221
Common Stocks							
Railroads	—	—	—	—	—	—	—
Utilities	2	43	77	162	513	219	556
Foreign	—	—	—	19	2	—	—
Industrial and Miscellaneous	65	263	30	65	79	372	414
Financial and Real Estate	7	—	3	9	23	—	130
Total [1]	74	306	110	255	617	591	1,100
Total New England participations	1,543	1,398	2,133	1,635	3,146	4,342	3,137
Total United States [2]	2,677	6,953	7,228	6,624	9,181	13,939	10,361
New England as per cent of United States	57.6	20.1	29.5	24.7	34.3	31.2	30.3
Estimated extent of participations	133	162	119	168	295	248	216
per cent of the national total	5.0	2.3	1.6	2.5	3.2	1.8	2.1

[1] Detail may not add to total because of rounding.
[2] *Annual Reports* of the Securities and Exchange Commission.
Source: *Commercial and Financial Chronicle.*

firms which have shifted their head offices to New York as regional houses and these generally become participants in Boston underwritings.

Firms domiciled in the region have continued to be active in syndicates headed by outside houses and have participated in between 20 and 35 per cent of the volume of all corporate and foreign issues. The amount of their participation has ranged between 6 and 13 per cent of the total value of the securities purchased by those syndicates. This percentage is comparable to that reported as distributed in the region by branches of outside firms for those issues which their head office originates or in which they take a major position.

Although the syndicate participations by local firms have diminished relative to the 1920's they remain substantial and have included many of the nation's large and small corporations. They have taken large positions in issues of Detroit Edison, Boston Edison, Kansas Power and Light, Electro Voice, Minute Maid, General Motors, Ford, Sylvania Electric, Foxboro Instruments, Dewey and Almy, Pitney-Bowes, Transitron, Tracerlab, Raytheon, Trans-Sonics, American Can, American Telephone, Pacific Finance, Green Shoe, New Hampshire Ball Bearings, Allegheny Airlines, American Airlines, Phillips Petroleum, Tennessee Gas Transmission, Commonwealth of Australia and Dominion of Canada.

Frequency Distribution, by Size, of New England Municipal Bond Issues 1959

Size of Issue Dollar Volume (in thousands of dollars)	*Number*
0-$49	9
$50-$99	27
$100-$249	72
$250-$499	45
$500-$749	34
$750-$999	20
$1,000-$1,999	50
$2,000-$4,999	28
$5,000-$9,999	4
$10,000-$19,999	3
$20,000 and over	5
Total Dollar Volume of Issues	$608,308
Total Number of Issues	297

Source: *The Bond Buyer.*

Municipal Underwriting since World War II

One of the most significant postwar changes in the capital markets has been the six-fold increase in the annual volume of new state and local government bonds, bringing with it national and regional alterations in the structure of the municipal market. Postponement of state and municipal construction programs during the war created a large backlog of public works projects. While many governments had accumulated financial reserves during the war, these proved inadequate in a period of rising prices to meet the demand for schools, roads, hospitals and other public facilities. The annual volume of municipal bonds thus rose rapidly from $1.2 billion in 1946 to a record of $7.7 billion in 1959. The volume of New England issues has approximated 8 per cent of the national total during the postwar years — about double the prewar proportion.

Some 300 New England municipal issues are offered in a typical year. In dollar size their distribution conforms closely to the national pattern, exhibiting a wide range with the smallest at about $50 thousand and the largest exceeding $50 million. Most of the issues are small, over half the number are less than $500 thousand, 70 per cent less than $1 million, and only 4 per cent of the number exceed $5 million in size. Thus a small percentage of the number of issues accounts for 60 per cent of the total principal amount. This contrasts sharply with the corporate field where about 90 per cent of the issues usually exceed $1 million in size. Small issues in the corporate field constitute a distinctly lower proportion of the aggregate principal amount than do small municipals.

The number of investment banking houses underwriting municipal issues in New England was about the same at the close of World War II as it had been during the 1930's. As the number of issues increased, more firms entered the field, including a large number of branch offices of outside firms. By 1950, one-third of the 33 New England houses which underwrote municipals were branches of firms with headquarters in New York or elsewhere. In 1959 these branches represented half of the 64 underwriters in the region. Branch offices placed in the region began to participate in locally formed underwriting syndicates or purchase singly issues of some New England units of government. These offices are generally granted more autonomy in their municipal operations, both with respect to underwriting and trading accounts, than in the corporate field.

Commercial banks in the region play a limited role as underwriters of municipal issues in comparison with banks in other regions. Nationally, the banks underwrite over half of the general obligation municipal bonds issued in a typical year. Banks in New England generally underwrite only issues of the smaller towns and most of these are held in the banks' portfolios. A few of the larger banks, however, join syndicates established to offer the general market names. In 1946 New England banks underwrote singly about 6 per cent of the total volume of New England issues; this portion fell to about 1 per cent in 1959. They participated however, in syndicates which marketed 7 per cent of the New England total.

Massachusetts Turnpike Authority $239,000,000
3.30 Per Cent 40 Year Revenue Bonds,
Dated May 1, 1954
(millions of dollars)

Geographical Area	*Amount of Underwriters' Participations*	*Sales for Group Account*
New York City	$137.9	$ 41.9
Boston	19.8	18.4
Chicago	18.6	1.9
New England States (excluding Boston)	1.8	28.2
Mid Atlantic States (excluding New York City, including Washington, D. C.)	19.5	18.0
Southeastern States	11.8	1.2
Great Lakes States (excluding Chicago)	16.5	3.0
Mid Western States	5.3	2.0
Southwestern States	1.6	0
Pacific Coast States	6.2	2.7
Canada	0	2.2
	$239.0	$119.5

Several reasons may be advanced to account for this difference in New England bank participation in municipal underwriting. Unlike governments in other regions, many local units issue short term tax anticipation notes and most of these are purchased by the banks. In addition to purchasing and holding the tax notes, the banks like those elsewhere perform other services for local governments. They advise on technical details of the issue and act as certifying and paying agents for the bonds. By helping to present municipal data in an orderly fashion the banks have increased the number of bids received by communities when an issue is offered. Historical relations between the region's financial institutions also form part of the explanation. The region early developed a number of investment houses which became active in this field, combining it with other underwriting business.

Most of the small issues are underwritten entirely in the region, either singly by an investment banker, or by a small syndicate formed entirely of local firms. The bulk of the larger issues are underwritten by syndicates managed in New York City, often by firms which maintain branch offices in the New England region. While larger issues are sold in all parts of the country, smaller issues are sold predominantly to local investors. Local investment banking firms enter into the national market for municipal issues to the extent that they participate in the large syndicates formed to purchase issues originating elsewhere. The local houses are important distributive links to the commercial banks and other institutional investors in the region.

The portion of New England issues underwritten entirely in New England has increased from 15 to 20 per cent during the postwar period; but this proportion is small when compared with earlier years when practically all New England issues were underwritten within the region. Syndicates which include both New England and outside firms have underwritten a growing portion of all New England issues. This practice reflects the increased competition for large issues and the necessity to guarantee adequate distributive capacity. Generally, New York City houses or New York banks with dealer departments head these syndicates.

There are important exceptions to this pattern, however. One of the large houses domiciled in Boston, F. S. Moseley & Company, originated the two revenue bond issues of the Massachusetts Turnpike Authority. The $239 million negotiated issue of the Authority in 1954 is the largest issue ever originated in New England. The Boston firm headed the syndicate with three co-managers. The participants included 382 firms with domicile in all parts of the nation; no one firm had a participation of more than $4 million and the smallest participants took $100 thousand. The composition of the underwriting syndicate reflects the geographical spread of a large underwriting.

Participation in Municipal Syndicates

Municipal underwriters in New England (domiciled firms or branches of outside firms) generally manage syndicates formed to underwrite New England issues whose average size is somewhat over $1 million. The managers of these accounts usually take a participation as large as 25-30 per cent, but on occasion they may have the privilege of increasing their participation. The other New England houses participating in syndicates managed in New England typically take a 20 per cent participation. Issues for which New York and Chicago banks act as manager or co-manager average $15.5 million in size and their participations in these issues are about 10 per cent.

Investment banking houses in New England participate in most of the large syndicates headed by New York banks or firms which are formed to purchase the large issues of New England cities, states or special authorities. Each New England house takes as its participation about 2 per cent of the entire issue. The exact extent of a firm's participation in one of the larger mixed syndicates depends upon the particular issue and the size and prominence of the house. If it is expected

Municipal Bond Underwriting
(millions of dollars)

	1946	*1950*	*1955*	*1959*
Total N. E. Issues	96.0	299.3	433.2	608.3
Underwritten in N. E.	15.8	43.9	83.3	123.4
Underwritten Outside N. E.	26.9	62.0	74.1	15.8
Underwritten by Mixed Syndicates	53.4	193.5	275.8	469.2
Underwritings of Outside Issues by Investment Bankers in N. E.	0	0	0	0
Outside Issues Underwritten by Mixed Syndicates	131.5	652.5	366.1	n. a.
Total of All State and Municipal Issues in the U. S.	1,203.6	3,693.6	5,976.5	7,681.1
New England Portion of this Total	8.0%	8.1%	7.3%	7.9%
Number of N. E. Investment Banking Houses which Underwrote Municipal Issues	40	33	45	64

n. a. = not available.

Source: *The Bond Buyer.*

that an issue will not have a favorable market in New England, local firms without outside distribution facilities will not participate in the syndicate. But firms with branch offices in other parts of the country generally join with the expectation that their participation would be sold through those branch offices.

The New York City banks which purchase New England issues singly, buy issues whose average size is about $250 thousand. Boston investment banking houses buy singly issues whose average size is $170 thousand and the few underwriters in other New England cities buy entire issues whose average size is $100 thousand.

Buyers of Municipals in New England

The amount of a New England municipal sold to investors in the region is estimated by individual firms to range from 40 to 100 per cent. The figure 90 per cent was given as typical for the smaller issues. The large New York banks which underwrite New England's general market issues rely only to a small degree on the region's investors. It is estimated that about two-thirds of the region's outstanding municipal debt in locally held, largely by commercial banks, fire, marine and casualty companies which are subject to the full corporate tax rate and individuals subject to high personal income tax rates.

Municipals issued elsewhere in the nation are also sold by local investment bankers to regional customers. In making these sales they may be helping to distribute a new issue or they may be acting in the capacity of broker. The portion of New England bonds in the total of all municipal bonds sold by the region's investment banking houses varies widely, from 10-90 per cent. Larger firms usually sell a wider range of municipal issues, hence only a small portion of their total municipal sales represents bonds issued in New England.

While there are several small firms which purchase only a few issues during a year there is no group of firms which dominates the business. Some New England firms specialize in issues of units of government within their own state; this is particularly true of the firms domiciled in cities outside Boston. The advent of special kinds of government securities during the past decade has led to the development of specialties within the municipal business. The Massachusetts state guarantee of local housing authority bonds led to the formation of a few fairly large syndicates which make a special practice of bidding on all of these issues. Regional school district bonds find their buyers among some rather than all investment bankers. One firm makes a specialty of the bonds of territorial possessions of the United States.

New England's Position in the Capital Market

New England's current position in the structure of the long term capital market is third, ranking behind New York and Chicago as measured by the origination and distribution of security issues and by the number of large buyers, both institutional and individual, located in the region. For a period prior to the Civil War the region represented the nation's primary long term capital market and during the late 1800's held a dominant position in the origination and distribution of securities of issuers from all parts of the country. Until the depression of the 1930's the region's investment banking houses maintained a distinctive position in the distribution of securities. As early as 1905 two Boston houses were among five in the nation which could provide national distribution of an issue while others were leading specialists in the securities of particular industries. Dominant houses at this time were in a position to offer specialized services to issuers.

As industrial development spread, as the number of investors and savers increased, and as the classification of institutional lenders became clear cut, corporate financial plans and security issues became more standardized. The independent manufacturing concern became a division of a national concern with headquarters elsewhere as part of a vertical, horizontal, or circular combination or merely through outright consolidation. As divisions of labor became more specialized, industry migrated from one region to another in search of lower labor costs or other competitive advantages. Most of the regions in the nation came to contain a variety of business interests similar to the nation as a whole and an increasing number of goods and services was traded in a single market. Public utilities developed financial structures which were closely similar because of the nature of the business and the influence of regulatory commissions. The requirements of other issuers became more standardized. Security issues came to be arranged by the administrative and financial officers of the concern. With increasing frequency, these officers are headquartered in New York or Chicago, or regularly visit these cities.

These developments contributed to the breaking of established ties with investment bankers, and to the growth of a large number of investment houses in all sections of the nation able to offer basic underwriting services to any issuer. Investment houses shifted head offices to New York or established branches in that city to improve their competitive position. Financial centers in San Francisco and the Southeast and Southwest developed independent houses which competed with the larger houses for underwriting of growing local firms. Outside houses tended to limit establishment of offices in a region unless there was an attractive concentration of institutional and individual buyers. The underwriting business has become so highly competitive that establishment of a branch office for underwriting purposes only is no longer considered feasible.

New England's investment banking structure reflects and was affected by all of these developments. The region in 1960 no longer holds a distinctive place in the originating of securities. Its identity has been merged with the national market. Houses continuing domicile in New England, with several exceptions, now generally originate only relatively small local issues, many of which are for growing research-based industries in electronics and related fields or for concerns such as food supermarket chains with regional markets. They also originate medium and smaller sized municipal issues. Contrary to practice in other regions, most New England banks do not underwrite municipal issues to any extent. The distinctive position of the region in the investment banking field today is found on the buying side as a result of the growth of the institutional market and the better than average individual market. New England's facilities thus emphasize distribution, which is reflected by the large number of branches of outside firms ranking high in capital size which have opened offices in Boston and other New England cities.

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