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## Mr. Smith Goes to Washington

These days, you almost need a law degree to listen to the business news, in which the terms indictment and “perp walk” are heard more often than “price-earnings ratio.” Congress is getting into the act, holding hearings to determine how to protect investors. New schemes of legislation and regulation typically follow severe market declines, as political pressure to “do something” mounts. Since we are all too human, however, our focus is often drawn to areas other than the real underlying issues.

***While the pessimists were blamed for the Great Depression and investor losses, the real responsibility lay elsewhere.***

There was a similar round of Congressional hearings in the 1930s, leading up to the creation of the Securities and Exchange Commission. Our title does not refer to the 1939 film in which Jimmy Stewart plays Jefferson Smith, a crusading congressman, however -- we’re thinking of a different Mr. Smith, one of our favorite figures in Wall Street history, Bernard E. Smith.

Ben Smith was an organizer of some of the “pools” that ran up stocks in the great bull market of the 1920s, but he was able to maintain a detachment from the markets and the commotion surrounding the bubble. He became increasingly concerned in the late 1920s as prices levitated far away from underlying values. Watching a new generation of investors descend into unreality, Smith had increasing disdain for the Wall Street firms, politicians and media encouraging a blindly positive attitude towards investing, ignoring the risk of loss.

Smith made substantial profits selling short during the 1929 crash (a technique that allows a speculator to make money in market declines). Previously unknown to the public, Smith became notorious, a celebrity villain, portrayed in the media as making money when everyone else was losing. There was nothing secretive about Smith or his tactics – in fact, he once ran into a brokerage house shouting “Sell ‘em all! They’re not worth anything!” and was thereafter known as “Sell ‘em Ben” Smith.

A symbol of the stock market bears profiting amidst misery, Smith received death threats and his family had to have bodyguards. In 1931, the Senate, with the approval of the Hoover presidency, moved to investigate the short sellers who were being blamed for wrecking the stock market and the economy. Called to Washington to testify, Smith regaled the Senate with a description of his methods, which, although unpopular, were legal. Unapologetic, he refused to accept blame for investor losses, suggesting that the truly culpable parties were more “respectable” figures. The bears and short sellers had not

encouraged a credulous public to invest too much in overpriced stocks. That responsibility lay at the feet of the highly regarded heads of large investment firms, the media and politicians, who had acted as pied pipers for the investing public. Smith was a particularly vocal critic of the president of the New York Stock Exchange, Richard Whitney, the leading spokesman for Wall Street. While this infuriated the financial establishment, Whitney subsequently served time in Sing Sing prison for fraud. Smith is described by Matthew Josephson in *The Money Lords* (Weybright and Talley, 1972):

“The man was a paradox. Feared and hated for what he did by many persons in high places, he was one of the most honest of men, one who lived by the truth.... He was a superior soul who lived in a world of clear realities. Most people lived really in a papier-mâché world, furnished with much American buncombe that could suddenly fall apart, as it did in 1929. We got our misinformation from the press, City Hall, the Capitol at Washington, the White House, and the mouthpieces and flunkies of the supposedly great. We bought what we were told to buy, believed what we were told to believe, or lost everything and starved when we had to, docilely, unromantically. Smith felt under no compulsion to believe what he called hooley.” (p.121)

***If you lost more than you can afford to lose in the market, look in the mirror, not at the celebrity justice financial reports.***

We believe Smith’s sentiments are relevant to investors today who seem to be inclined to blame financial crooks for their misfortunes. While there were criminal acts in the financial world, they

were a relatively small and discrete subset of the bubble. After all, investors lost more money in Cisco Systems stock than in the alleged fraud surrounding WorldCom. Ben Smith would ask who caused more investor losses, the president of Enron, or the popular TV financial show moderator who refuses to book guests or panelists with a negative market view? Martha Stewart, or the prominent Wall Street firm strategist who belittles anyone applying traditional valuation measures to the market? A financial analyst on the take, or the editor of a financial magazine that constantly hypes whatever has been performing well lately? A too-compliant accountant, or the head of an investment firm who fires or silences an analyst who has become concerned about market valuations?

Persons committing crimes should be punished, but the current celebrity justice aspect of financial reporting should not distract investors from realizing who is truly responsible for their losses – themselves. For every innocent who lost money in an alleged fraud, there are a hundred investors who unthinkingly threw money at dramatically overpriced stocks, encouraged by the approving chorus of the financial products industry and the media, because they feared that everyone was getting rich but them. If you have too little money for retirement, it will be little consolation to claim that Martha made you do it. Where’s Ben Smith when you need him?

Smith showed that maintaining a rational, emotional detachment from the sensational news or villain *du jour* is important in any investment program. If you would like our help in achieving that objectivity, please contact us.