BENJAMIN GRAHAM

1894–1976

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DEDICATION TO GEORGE M. HANSEN

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BENJAMIN GRAHAM

THE FATHER OF FINANCIAL ANALYSIS

Benjamin Graham died on September 21, 1976 at his home in Aix-en-Provence, France at age 82. When a pioneer in a profession dies at an advanced age, one generally has to go back many decades to find his last contributions. This was not the case with Ben Graham. The cover of the then current issue of the *Financial Analysts Journal* (the September/October issue had gone to press only shortly before his death) had the portrait that adorns this publication. The lead article ended with Ben's exhortation consistently stressed for half a century: "True investors can exploit the recurrent excessive optimism and excessive apprehension of the speculative public."

The profession of financial analysis was built on the pioneering book *Security Analysis*, published in 1934 and in its fourth edition still is used in the Chartered Financial Analysts Candidate Study Program. More than 100,000 copies of "Graham & Dodd" have brought his concepts about the merits of investment over speculation to two generations of our profession. The financial success of Ben and his clients dramatically demonstrated the practical value of his thorough approach to the evaluation of investments.

Students of *Security Analysis* recognized that the masterpiece did not spring into life in one outburst of genius. Rather it was the result of much hard work and the experience of two decades before the first edition. Over a year ago The Financial Analysts Research Foundation became interested in the preparation of a biographical sketch of the professional development of Benjamin Graham as a contribution to the history of the development of financial analysis. Ben was most enthusiastic about this project and supplied nearly 200 pages of an unpublished draft of his memoirs written in 1956. The transcript of the March 1976 interview by the Foundation's Research Coordinator, Hartman L. Butler, Jr., C.F.A., helped Ben to review some of the parts in his active life not covered in his memoirs. One of the co-authors of this sketch, Irving Kahn, had the experience of working extensively and teaching under Ben for over four decades.

The reader should understand that the enduring portions of this biography are among Ben's many contributions that have both enriched our lives and enhanced our understanding of the early development of the profession of financial analysis.

HIS EARLY LIFE

Benjamin Graham was born on May 9, 1894 in London, the youngest of three children, all boys. His father was in the family business of importing china and bric-a-brac from Austria and Germany. When he was just a year old, the family moved to New York to open an American branch of the firm. Ben began the normal life of a boy in New York, attending P.S. 10 at 117th Street and St. Nicholas Avenue. His father died at only 35, leaving his widow to bring up three boys ages 9, 10, and 11.

Various efforts were made to continue the business but, without an active adult, it failed in little more than a year. Nor did his mother's two-year experiment running a boarding house prove any more successful. When Ben was 13, his mother opened a margin account to buy an odd lot of U. S. Steel. The panic of 1907 wiped out the small margin account. This was Ben's first contact with the stock market.

Despite dwindling family resources, Ben graduated near the top of his class at Boys High School in Brooklyn. A clerical error delayed his scholarship to Columbia for one semester. The need to help support the family forced him to drop his daytime classes to take a full-time job with United States Express. Yet, he continued his studies with such great success that he graduated second in the Class of 1914.

During his final month at Columbia, three departments—Philosophy, Mathematics, and English—each invited him to join their faculties as an instructor. Each of the department heads pointed out the satisfactions of an academic career, despite low starting salaries and slow prospects for advancement. Bewildered by this wealth of offers, Ben conferred with Columbia's Dean, Frederick Keppel, who had a strong prediliction for sending bright graduates into business instead of an academic life. By coincidence, a member of the New York Stock Exchange came in to see Dean Keppel about his son's woeful grades and, in the course of the interview, asked the Dean to recommend one of his best students.

THE BEGINNING OF A CAREER

Thus, Ben began his career with Newburger, Henderson & Loeb as an assistant in the bond department at $12 per week ($68 in 1977 dollars). Although Ben never studied economics at Columbia, he was eager to participate in the "mysterious rites and momentous events" alluded to in novels about the world of finance. After a month as a runner delivering securities and checks, he became the assistant to a two-man bond department. His main task was to prepare thumbnail

descriptions of each bond in their daily lists of recommendations. After six weeks, Ben was assigned the additional task of writing the daily market-letter for their Philadelphia office.

A few months later, World War I broke out and European investors' heavy sales of their American securities caused the panic that forced the New York Stock Exchange to close for several months. When trading resumed on a limited basis, investor confidence gradually returned and the big wartime rise began. His firm, caught shorthanded by this increased activity, used Ben to fill many gaps, including helping the "boardboy" put up stock quotations. Other days he operated the telephone switchboard, helped out in the back office, and even made an occasional delivery of securities. These routine jobs gave Ben an understanding of all aspects of the investment world.

When the market settled down, the partners decided to send Ben out to call on customers. This was then a pleasant occupation, because in those days the average businessman was flattered to be called upon by a bond salesman and even his "No" was invariably polite. Although these calls turned out to be fruitless, Ben was learning about the limited understanding most clients had of the securities they bought or owned.

Ben began to study railroad reports, then the major industry with bonds outstanding. He applied himself diligently to the then standard textbook: *The Principles of Bond Investment* by Lawrence Chamberlain. One of his earliest studies was an analysis of the Missouri Pacific Railroad. Its report for the year ended in June 1914 convinced him that the company was in poor physical and financial condition and that its bonds should not be held by investors. He showed the report to a friend who was a floor broker on the Exchange. The floor broker in turn showed the report to a partner in Bache & Co. As a result, Ben was asked to become a "statistician"—as security analysts were then called—at a salary of $18 per week, a 50 percent raise.

Ben assumed that Newburger, Henderson & Loeb would not object, as he had brought in no bond commissions to offset his salary. Samuel Newburger instead was outraged that his employee could be so disloyal as to consider leaving. To his surprise, this conversation ensued:

> "But, I thought I wasn't earning my salt here."
>
> "That's for us to decide, not you."
>
> "But I'm not cut out for a bond salesman; I'd do better at statistical work."
>
> "That's fine. It's time we had a statistical department. You can be it."

Investment activity in that era was almost entirely limited to bonds. Common stocks, with a relatively few exceptions for the major railroads and utilities, were viewed as speculations. Nonetheless, a growing supply of corporate information had begun to appear. Operating and financial information was supplied by corporations, either voluntarily to attract investors, or else to conform with stock exchange regulations. The financial services took advantage of this information, reprinting it in convenient form in their manuals and current publications. In addition, the ICC and various regulatory bodies were gathering enormous quantities of data, all of which were open for inspection and study.

Most of this financial information, however, was neglected in common stock analysis. The figures were considered to have limited current interest. What really counted was "insider information"—some of it related to a company's operations, but much relating to the plans of stock market pools. Market manipulators were held responsible for most of the moves, up or down, in major stocks. The improved financial position of industrial companies—resulting from World War I expansion—developed those factors of intrinsic value and investment merit that were to become the dominant concepts in future market moves. Thus, the Wall Street of the early 1920's became virgin territory for exploitation by genuine, penetrating analysis of security values, especially among industrial issues.

Ben's career as a distinctive professional Wall Street analyst dates back to the 1915 plan for the dissolution of the Guggenheim Exploration Company. This holding company had large interests in several copper mining companies actively trading on the New York Stock Exchange. When Guggenheim Exploration proposed to dissolve and to distribute its various holdings to its shareholders on a pro rata basis, Ben calculated the arbitrage values as follows:

		Market Value September 1, 1915
1 share Guggenheim Exploration		$68.88
Equivalent Securities Held		
.7277 share Kennecott Copper @ 52.50	=	$38.20
.1172 share Chino Copper @ 46.00	=	5.39
.0833 share Amer. Smelting @ 81.75	=	6.81
.185 share Ray Cons. Copper @ 22.88	=	4.23
Other assets	=	21.60
Total		$76.23

These calculations meant an assured arbitrage profit of $7.35 for each share of Guggenheim Exploration purchased, provided that simultaneous sales were made of the underlying copper companies. The risks lay in the possibility that the shareholders might not approve the dissolution, or that litigation might delay it. Another potential problem might arise in maintaining a "short" position in the copper stocks until the distribution was made to Guggenheim shareholders. Because none of these risks appeared substantial, the firm arbitraged a large number of shares. One of Ben's associates proposed that he manage his venture in Guggenheim in return for a 20 percent share in the profits. When the dissolution went through on January 17, 1916, Ben's reputation and his net worth both grew.

The years 1915-1916 saw the big bull market of World War I. The typical U. S. corporation, still lightly taxed, benefitted hugely from war orders for munitions and supplies for England and France. Common stocks rose to unprecedented heights; the brokerage community prospered mightily; and Ben's salary did, too.

In April 1917, when the United States entered the war, Ben applied for the Officer Candidate Training Camp, but he received a curt rejection because he was still a British subject. Ben joined Company M of the New York State Guard, whose most active participation was marching to the Guard's band led by Victor Herbert!

Ben's success with the Guggenheim Exploration Co. dissolution encouraged him to buy common stocks that appeared to be underpriced while simultaneously selling overpriced stocks. His good friend, Algernon Tassin, Professor of English at Columbia, agreed to supply $10,000 of capital, with the profits or losses of the trading account to be divided equally between the professor and Ben. The account prospered famously during the first year with several thousand dollars of profit for each. Ben used his share to invest $7,000 in "The Broadway Phonograph Shop" at Broadway and 98th Street, with his brother Leon operating the store. The store was kept going for several years before selling out.

Beginning with a so-called "peace scare" in the Fall of 1916 and continuing for a year after America entered the war in early 1917, security prices suffered a persistent decline. The Tassin account was generally in obscure issues that actually were worth more than their market quotations. But, these stocks also dropped in the general weakness and, even worse, bids for such obscure issues tended to disappear. The account was called for more margin, and it was necessary to make sales at a considerable loss. Ben was unable to repay his share of the loss since his funds were tied up in the phonograph shop. The unsuspecting Algernon was shocked to hear the results, but

sympathetically allowed Ben to make up the deficiency at $60 per month. After two years the market strengthened sufficiently to make up the deficiency, and in later years Ben was able to build up Professor Tassin's fortune to a "quite respectable figure."

During the war years Ben submitted to the *Magazine of Wall Street* an article entitled "Bargains in Bonds." This was a thorough study showing the disparities among the prices of a number of quite comparable issues. From then on, he became a frequent contributor to the magazine. At one point he was asked to join the staff and later he was asked to become editor with an attractive salary. Mr. Newburger again talked Ben out of leaving the firm, this time promising him a junior partnership. Instead, Ben's brother, Victor, became an advertising salesman for the *Magazine of Wall Street,* where he had a great success, becoming the vice president in charge of the department.

THE NEW ERA BEGINS

Between 1919 and 1929, Ben's upward progress in Wall Street was so rapid as to verge on the spectacular. At the beginning of 1920 he was made a partner in Newburger, Henderson & Loeb, retaining his salary and gaining a 2½ percent interest in the profits, without any liability for losses.

One of Ben's friends was with the important public utility bond house, Bonbright & Co. He introduced Ben to a young man, Junkichi Miki, who had tried to interest Bonbright & Co. in acting as agent for his employer, the Fujimoto Bill Broker Bank of Osaka, active in acquiring Japanese Government bonds. Bonbright & Co. was too busy with its own underwritings, but Ben was able to offer Miki his firm's comprehensive and energetic service. Various issues of Japanese Government bonds had been placed in Europe and America in 1906 during the Russo-Japanese War. These bonds were payable, at the option of the holder, either in a European currency or in yen. The prosperity of Japan combined with the currency problems of Europe following World War I meant that these bonds became very attractive for Japanese investors.

Ben arranged for the purchase of these bonds on a large scale through his firm's correspondents in London, Paris, and Amsterdam. The bonds were then shipped to Japan, draft attached. The two percent commission provided over $100,000 during the two years that Newburger, Henderson & Loeb was the exclusive agent. The back office was less enthusiastic, however, because a large portion of the Japanese bonds had been sold in $100 denominations or equivalent pieces in Paris and London. These "small pieces" were considered a nuisance in

Western markets, selling at a substantial discount. As the Japanese had no prejudice against these bonds, his back office was inundated with reams of documents. The typical purchase of $100,000 face amount would usually result in the appearance of one thousand separate bonds. The special safe deposit box for these bonds was known, not too favorably, as the "Ben Graham" box.

After two years, the Fujimoto Bank set up its own New York office, with Miki in charge, to buy these bonds. Two other Japanese banking firms then became customers and made up for some of the lost business.

Ben's main work was in handling all inquiries about security lists or individual issues. He was given an assistant, Leo Stern, later a senior partner in the firm and the father of Walter P. Stern—whose own distinguished career has included terms as President of The Financial Analysts Federation and of The Institute of Chartered Financial Analysts. Periodically, they issued "circulars" analyzing one or more securities in detail.

For example, in May of 1921 they recommended the sale of the U. S. Victory 4¾'s due in 1923 and selling at 97¾ and reinvestment in the U. S. 4¼'s of 1938 then selling at 87½. They believed that the then high level of interest rates would subside and thus the longer term bonds had better appreciation possibilities. This circular was advertised in the newspapers under the title "Memorandum to Holders of Victory Bonds." The New York Stock Exchange promptly asked for a copy, as an unwritten rule prohibited Stock Exchange Members from recommending switches out of Government Bonds into corporate securities. Fortunately, the circular did not recommend any unpatriotic act—and it proved to be a profitable recommendation.

Another circular was more notable for teaching Ben a lesson. That circular was a detailed statistical comparison of all the listed tire and rubber stocks. The study duly noted that Ajax Tire common appeared to be the most attractive. A few days later the president of Ajax Tire appeared at Ben's office. Ben subsequently wished he had met him before the circular was issued. Ajax Tire flourished only a little while and then declined into bankruptcy. Thus, a lesson in the importance of meeting top management was learned.

In 1919, Ben prepared a detailed comparison of the Chicago, Milwaukee & St. Paul Railroad with the St. Louis & Southwestern Railroad. Because his analysis portrayed the Milwaukee Railroad in a highly unfavorable light, he felt it best to submit it to the company before publication. An appointment was made with the Financial Vice-President, Robert J. Marony. Marony looked over the material rather rapidly and said: "I don't quarrel with your facts or your

conclusions. I wish our showing was a better one, but it isn't and that's that." This episode led to a long-lasting business and personal association in which Mr. Marony became a substantial investor and director in Graham-Newman Corporation and in Government Employees Insurance Company.

The same year Ben wrote three pamphlets "Lessons for Investors," giving the wisdom of this precocious 25-year old. A strong argument was made for the purchase of sound common stocks at reasonable prices. It also contained the novel statement that "if a common stock is a good investment, it is also an attractive speculation."

Beginning in 1913 and throughout World War I, tax laws and tax regulations became increasingly complicated as well as onerous. Ben realized that it was necessary to study tax laws thoroughly to see their effect on corporations' results. This led to an unexpected use of the tax figures. At that time the typical corporate balance sheet contained a large amount of "goodwill," almost always lumped together with actual tangible investments in the "property account" as published. The extent of "goodwill" or "water" was a jealously-guarded secret.

The Excess Profits Tax of 1917, however, allowed a credit of a certain percentage on tangible invested capital, but only a minor allowance for intangibles such as goodwill, patents and so forth. Ben devised a series of formulas to work back from three items—taxes, pretax income, and the property account—to determine how much of the property account was in the goodwill category. These findings were the basis for an article in *The Magazine of Wall Street.* Editor Powers said: "Ben, nobody around here can make head or tail of your formulas. It looks as if you've done the whole thing with mirrors. But, we'll publish it anyway."

Although the published figures available could have been misleading, Ben's computations proved remarkably correct. The accuracy of his calculations was not publicly available for many years—until most corporations finally started to write off the more imaginary intangibles embedded in their balance sheets. By then, earning power had begun to become the most significant factor affecting a stock's price and asset values were much less important. Ben's computations, for example, revealed that all the $508 million par value of the U. S. Steel common stock and even a good part of its $360 million of preferred had originally been "water." Subsequently U. S. Steel wrote down $769 million of "goodwill" and similar intangibles by using many years of retained earnings.

Word of Ben's success with arbitrage and hedging operations spread, and several clients opened accounts that allowed him, as sole manager, a 25 percent share in the cumulative net profits. A standard

operation was the purchase of convertible bonds near par value and the simultaneous sale of calls on an equivalent amount of common. At times the market would be stronger for puts and then the bonds would be bought, the stock sold short and a put also sold. As the premium prices then received for puts and calls were substantial, this procedure guaranteed a satisfactory profit no matter whether the stock rose, fell, or remained constant.

The postwar bull market of 1919 was a typical bull market of the times—marked by manipulations by insiders, plus the usual greed, ignorance, and enthusiasm on the part of the public. Ben came through the dangerous period of 1919-1921 quite well, remembering his experience with the Tassin account. His accounts concentrated on arbitrage and hedging operations. One of the speculative favorites of the time was Consolidated Textile, a recent conglomeration of cotton mills whose convertible seven percent bonds appeared sufficiently safe to buy. Later, as the common rose in price, corresponding amounts of stock were sold short, assuring a good profit. One of the firm's senior partners, an enthusiastic bull on the stock, had purchased large quantities of the common for his customers. Ben pointed out that the convertible bonds had the same potential for profit as the stock, plus less risk of loss. The partner said his customers liked an active stock rather than a bond. Within a year, Consolidated Textile common fell from 70 to 20, while the seven percent convertible bonds were refinanced and redeemed at a premium above par value. This valuable lesson has yet to be learned by amateur investors.

Ben was not completely immune to the then current nonsense. A friend had been in a syndicate that bought privately Ertel Oil common at $3 per share and after a few weeks began trading the stock publicly in the over-the-counter market at $8 per share. The friend good naturedly offered to let him in on the next deal. In April of 1919, the next deal came along. Savold Tire was formed to exploit a patented process for retreading automobile tires. Ben put in $2,500, and the syndicate subscribed at 10. A few days later trading began at 24 and then rose to 37 amid considerable excitement. The syndicate sold out and Ben's share was nearly $7,500.

In spite of his usual common sense, greed prevailed. The parent decided to license its process to affiliates in the various states and these companies would sell stock to the public. Four weeks after the original Savold Tire deal, New York Savold Tire was organized. This time some of Ben's friends joined in a $20,000 participation in the syndicate that subscribed to shares at 20 and saw the stock open on the Curb Exchange at 50 and then rise to 60. This happened during the week of Ben's 25th birthday. Promptly a check was received for the initial

contribution plus 150 percent in profits. No accounting came with the check, and Ben said he wouldn't have dreamt of asking for one. A third company, Ohio Savold, came the next month, but this was a small one with no room for Ben's group.

Then a very large deal was concocted, Pennsylvania Savold. This was to be the last in the series with rights to the process in the remaining 46 states, as it had been decided that more than four Savold companies would be cumbersome. Ben "neither understood nor approved of this artistic restraint, but prepared to profit to the hilt from this last gorgeous opportunity." Ben's circle of friends combined to send in $60,000 for this venture. It is now August 1919, and the bull market continues strong with great emphasis on stocks of the rankest speculative flavor. The original Savold was strong, reaching a peak of 77¾. In a week, however, it fell by 30 percent. The group waited for Pennsylvania Savold to begin trading. There was a slight delay. This continued for a few weeks until all the Savold issues collapsed completely, disappearing forever. The friend brought Ben along to a meeting with the Savold promoter, who was pressured into turning over cash and shares in some other promotions that at least gave back to the victims of the Savold Tire promotion one-third of their "investment".

Apparently nobody complained to the district attorney's office about this swindle—nor about similar swindles. Wall Street firms behaved ethically in the execution of their customer's orders and in their dealings with other firms. Most of the brokerage firms, however, condoned manipulation and did virtually nothing to protect the public or often themselves against gross abuses similar to the Savold Tire swindle.

Ironically, the subsequent success of retreading companies, such as Bandag, justified the product's legitimacy.

BEN BECOMES A PORTFOLIO MANAGER

Some of Ben's friends were so impressed with his approach to investments that in early 1923 they proposed a $250,000 account and, if the results warranted it, this would be increased greatly. Ben could bring in other accounts as part of the original capital. He would receive a salary of $10,000 per year ($34,200 in 1977 dollars). Then the investors would be entitled to a six percent return. Ben would be entitled to a 20 percent share in profits beyond that.

Newburger, Henderson & Loeb agreed, this time, to let Ben leave. The New York Stock Exchange had tightened its rules on the amount of capital required by member firms. Their volume of business had been greatly expanding and Ben's arbitrage operations required more capital

than they could now supply. They agreed to let Ben continue to use an office at the firm, in return for doing his business through Newburger, Henderson & Loeb.

Thus the new business was incorporated as Grahar Corporation (Louis Harris being the major investor). It began operations on June 1, 1923 when the Dow Jones Industrial Average was 95.

Grahar Corporation operated for two and one-half years until the end of 1925, and then dissolved with a good percentage appreciation—the Dow Jones Industrials having risen 79 percent during the period. Investments were limited to arbitrage operations and to the purchase of securities that appeared to be greatly undervalued.

The first trades were the purchase of Du Pont common, and the simultaneous short sale of seven times as many shares of General Motors common. At that time Du Pont was selling for no more than the value of its General Motors holdings. The market in effect placed no value on DD's large chemical business and other assets. In time, this anomaly ended with the market price of Du Pont rising to reflect the value of the chemical business as well as its GM holding. Grahar then took its profits by selling DD and closing out the GM short position.

Ben prided himself on his ability to recognize overvalued stocks as well as undervalued issues. He would sell short an overvalued stock and buy an undervalued one. Accordingly, it was decided to sell short a few hundred shares of Shattuck Corp., the owner of the Schrafft's restaurant chain. Ben had his regular weekly luncheon with the major investors at a Schrafft restaurant. After the short sale, they all felt that it was not right to support Schrafft's with their business. Time went by, but Shattuck common continued to go up. The group grew tired of fighting the trend, closing out the short at a $10,000 loss.

One of the characteristics of popular issues is that such a stock may continue to remain popular and, therefore, overvalued instead of returning to a more normal price. The only consolation was that Ben and his group were able to go back to eating lunch at Schrafft's.

By 1925 the bull market was well under way. Ben had reached the ripe age of 31. Many of the customers' men (today called registered representatives) ran discretionary accounts—some with profits being evenly split, but any net loss being absorbed by the customer. They told Ben he was foolish to settle for 20 percent of the profits and that they could bring him accounts on a fifty-fifty basis. He proposed a new arrangement to Lou Harris. Ben would give up his salary but, after the six percent allowed on capital, Ben would receive 20 percent of the first 20 percent return, 30 percent of the next 30 percent, and 50 percent on the balance. This would have worked out as follows:

Return on Capital	Investors' Share	Graham's Share
6%	6%	—
26	22	4%
56	43	13
100	65	35

Mr. Harris rejected this proposal, and they mutually agreed to dissolve Grahar Corporation at the year end.

On January 1, 1926, the "Benjamin Graham Joint Account" began with capital contributed by old friends plus Ben's own funds. The profit-sharing terms were those Ben had proposed for Grahar. The original capital was $450,000 and grew to $2,500,000 in three years by the start of 1929, with much of the gain reflecting appreciation rather than capital additions. Towards the end of 1926, Jerome Newman joined Ben. Jerry Newman remained as an ever more active and valuable associate for the next 30 years until Ben retired in 1956.

THE NORTHERN PIPE LINE CONTEST

One day in 1926, Ben was looking through an annual report of the Interstate Commerce Commission (ICC) to obtain data on a railroad. At the end of the volume he found some statistics about pipeline companies that had the notation: "taken from their annual reports to the Commission." Ben wondered if the reports filed with the ICC might have interesting details and wrote for a blank copy of the ICC report form to see what details were asked for. The ICC sent a 50-page blank form showing that complete details were required. Ben took the train to Washington the next day.

Eight pipeline companies were carrying crude oil to various refineries. Originally part of the Standard Oil Trust, they were spun off in 1911 as part of the U. S. Supreme Court antitrust decision to split up the trust. Each of the companies was relatively small and published a

one line "income account" and a very abbreviated balance sheet. Two large Wall Street firms specialized in the markets for all the 31 former Standard Oil subsidiaries, but they gave no data for the eight pipeline companies except their brief annual reports.

At the ICC, Ben found that all of the pipeline companies owned large amounts of investment-grade railroad bonds, often exceeding their own market value. Moreover, no business reason seemed needed for keeping these bonds. The companies had relatively small gross revenues, but wide profit margins. The outstanding value was Northern Pipe Line, selling at 65 and holding $95 per share of cash assets, mostly in good railroad bonds. It earned and paid a $6 dividend to yield nine percent.

The pipeline companies had paid even larger dividends a few years earlier before the advent of large railroad tank cars that began cutting into their business. Investors thought that the downtrend in earnings and dividends would continue and, despite nine percent yields, only trouble was ahead.

By careful and persistent buying, Ben was able to buy 2,000 shares of Northern Pipe Line's 40,000 shares, making him the largest shareholder except for the Rockefeller Foundation's 23 percent interest. He met the president of Northern Pipe Line at the company's office in the Standard Oil Building. Ben pointed out how unnecessary it was for Northern Pipe Line to carry $3,600,000 in bond investments when its gross revenues were only $300,000. These surplus cash resources of $90 per share should be distributed to the shareholders. The president raised a number of specious arguments as to why this was not possible: the railroad bonds were needed to cover the stock's $100 per share par value; they might be needed as a source of funds when the present line would have to be replaced; and finally, they might want to extend the line. His parting comment was one that Ben came to hear many times. "The pipeline business is a complex and specialized business about which you know very little; but in which we have spent a lifetime. We know better than you what is best for the company and the stockholders. If you don't approve of our policies, you should sell your shares."

Old Wall Street hands would have regarded Ben's efforts to change management's policies as either naive or suspect. Many years ago one man, Clarence Venner, had made quite a lot of money (and an unenviable reputation) by bringing suits against managements for alleged financial misdeeds, some being only minor technical errors. Therefore, anyone attempting to challenge management would be characterized as a "hold-up artist."

Having failed to impress the Northern Pipe Line management with the logic of the case for distributing the surplus cash assets to the

shareholders, Ben asked if he could present his argument at the annual meeting. Accordingly, he attended the meeting in January 1927 at Oil City, Pennsylvania. Ben had neglected, however, to bring someone to second his motion to present the memorandum, and the meeting was adjourned after a few perfunctory actions.

Ben began preparing for next year's meeting by buying more shares of Northern Pipe Line with the partnership's increased capital. A lawyer of great ability and prominence was retained. Pennsylvania corporations had mandatory cumulative voting so that it would be necessary to have the votes of one-sixth of the shares in order to elect one director to the five-person board. Ben decided to solicit proxies in favor of a resolution to reduce the capitalization and to pay the surplus cash to shareholders. He also sought to elect two members to the board.

Surprisingly, Northern Pipe Line thought so little of his chances that the shareholders' list was furnished without a lawsuit. Each side sent out letters requesting proxies, with the arguments for both sides being the same as at Ben's first meeting with the president. Because proxy solicitation firms did not exist, management utilized its employees. Ben and his associates visited the larger shareholders. He was even able to arrange an interview with the financial advisor to the Rockefeller Foundation, which owned 23 percent of the stock. He listened courteously, but said the Foundation never interfered in the operations of any of the companies in which it held investments.

At the 1928 annual meeting, Ben came supplied with proxies for 38 percent of the shares, guaranteeing the election of two directors. The president suggested that a single slate of directors be named, including any two from the rebels, except Ben. As this was unacceptable, the single slate included Ben and one of the lawyers. Thus, Ben became the first person not directly affiliated with the Standard Oil system to be elected a director of one of the affiliates.

A few weeks after the meeting, the president invited Ben to his office and told him: "We really were never opposed to your idea of returning capital to the stockholders; we merely felt the time wasn't appropriate." He agreed to distribute $70 per share. It was later learned that when the Rockefeller Foundation returned their proxy to management, they indicated that they would favor a distribution of as much capital as the business could spare. Subsequently, the other pipeline companies made similar distributions of surplus capital to shareholders, no doubt since the Rockefeller Foundation had a number of uses for the surplus funds. The $70 distribution plus the value of Northern Pipe Line afterwards exceeded $100 per share, compared with the initial market price of 65 when Ben began his campaign.

MEETING THE BARUCHS

As the Benjamin Graham Joint Account continued to prosper in other operations, it was necessary to move from the small office at Newburger, Henderson & Loeb into its own offices. These were in the same building with the main office of H. Hentz & Co., one of whose senior partners was Dr. Herman Baruch. All three of Bernard Baruch's brothers made the not surprising choice of becoming Wall Street brokers. At this time Ben began buying shares in another former Standard Oil subsidiary, National Transit Company. National Transit operated a pipeline and also manufactured pumps. To counter Ben's proposal to distribute their surplus cash, management came up with a plan to use it in a rather unproductive manner. Herman Baruch and his clients joined in the purchase of National Transit shares and, after some prodding from the Rockefeller Foundation, a substantial distribution of cash was made to shareholders. In gratitude Dr. Baruch gave Ben the use of his fully manned yacht for a week—with Ben inviting some of his friends for a luxurious week.

Ben's special interests became well known on Wall Street. One day a trader from a large over-the-counter firm came to Ben with an elaborate proposition to buy a large block of Unexcelled Manufacturing Company, the nation's leading fireworks company. The price of 9 was less than working capital and only 6 times earnings. The purchase of this block would also enable a change in control, with the old president being replaced by a capable vice president and Ben joining the company as a part-time Financial Vice President. The partnership took 10,000 shares and sought to place the balance in "good hands." Bernard Baruch had become increasingly interested in Ben's type of operations and agreed to buy the balance of the block of Unexcelled. At the annual meeting he saw for the first time the president of Unexcelled, who had founded the company and run it for 25 years, and Ben felt uneasy at being part of a conspiracy to end the career of a man who had never done him any harm. The change in control took place as scheduled, yet shifting demand and legal restrictions on the use of fireworks kept this investment from being a success.

Ben recommended a number of other issues to Bernard M. Baruch, which appealed to his keen sense of security values. During the bull market of the late 1920's, emphasis was focused on certain popular issues. Lesser-known stocks in promising industries, such as electric utilities and chemicals, became as popular as the giant companies. Also, many smaller companies with short but exceptional growth records received the attention of speculators and manipulators. Other

substantial companies, however, fell outside these favored categories and sold at bargain-counter prices, even below their minimum values as judged by ordinary standards. Among these were Plymouth Cordage, Pepperell Manufacturing Co., and Heywood & Wakefield, the leader in the baby carriage industry, each selling below working capital. Bernard Baruch bought substantial amounts of these issues, confirming the soundness of Ben's analyses. Baruch egotistically believed that his concurrence was a sufficient reward for Ben's efforts.

Both agreed that the market had advanced to inordinate heights and, with such frenzied speculation, it would ultimately end in a major crash. Baruch commented that it was ridiculous for short-term interest rates to be eight percent while the Dow Jones Industrials provided only a two percent yield. Ben replied: "By the law of compensation, someday the reverse should happen." Some years later after the crash when the law of compensation took effect, Ben realized that it was strange that, despite his accurate projection, he did not realize that all operations involving borrowing, including his own, would be affected by the ultimate collapse.

One day in 1929, Baruch invited Ben to his office. For the first time in his life he wanted a partner. "I'm now 57 and it's time to slow up a bit and let a younger man like you share my burdens and my profits." Although this was most gratifying to one's ego, Ben had just completed a year in which his personal net profit was over $600,000 and thus saw no reason to be a junior partner even to the eminent Bernard M. Baruch.

THE DELUGE

The Benjamin Graham Joint Account began with $450,000 at the start of 1926 when the Dow Jones Industrial Average was 157. In 1926, the Dow had only a nominal gain, but 1927 provided an encouraging 32 percent return. The Benjamin Graham Joint Account ended that year at $1,500,000, with new capital coming into the account, as well as capital gains.

The year 1928 was the last full year of the bull market, with a 51 percent return for the Dow Jones Industrials and a 60 percent return for the Joint Account, after Ben's share that exceeded $600,000.

This excellent record led to an even more exciting proposal, one to manage a large new investment trust. Many major investment trusts were formed in the 1920's. The first were fixed trusts with a specified and fixed portfolio of common stocks, with the shareholder holding a pro rata share in this unchanging list. Actually, this was really not greatly different from the index funds of today.

Next, investment trusts were formed that could be managed, patterned after the investment trusts that had long operated successfully in England. The speculative atmosphere of the late 1920's led many investment banking firms to launch their own investment trusts—to obtain management fees, as well as commissions on the sale of shares in the trust plus commissions on the trust's business.

The H. Hentz partners thought they should have an investment trust and that Ben Graham should run it. They were planning a $25 million fund, which would supply adequate compensation for all concerned. The details of organizing the trust delayed the initial sale for some months and when September came, the 1929 stock market crash ended any possibility for establishing the Hentz-Graham Fund.

Ben had enough to do to keep up with the Joint Account. At mid-1929, the capital was $2.5 million, about where it was at the start of the year. The Account had a large number of arbitrage and hedging operations involving long positions of $2.5 million and an equal amount of short positions. In addition, $4.5 million of other securities were held on which $2 million was borrowed, leaving $2.5 million of equity. These securities were not Wall Street favorites, but rather issues that had intrinsic values above their market prices.

The hedge operations generally involved the purchase of a convertible preferred and a short sale of the equivalent amount of common. In weak markets the common would decline faster than the preferred stock and they would undo the hedge at a good profit. However, they found that oftentimes the market would recover and they would reinstate the position by buying the convertible preferred once again and selling more common. This would usually involve the purchase of the preferred at a higher price than the price at which it was sold earlier. Thus they came to adopt a policy of only partially undoing the hedging operation when the stocks declined, closing out the short positions in the common, but holding on to the preferred. In addition, they began to go in for partial hedges, selling short only half as much common as would be required for a complete hedge. These adaptations of the basic hedging operation increased profits during a bull market, but also created risks that were not present in fully hedged positions.

As the market collapsed in the final months of 1929, Ben covered a large part of the short position, recording large profits. In most cases, however, Ben did not sell the related convertible preferreds since their prices seemed too low. The Joint Account ended the year with a loss of 20 percent, as compared with a 15 percent decline for the Dow Jones Industrials. Many of the participants in the fund had their own margin

accounts that had experienced much greater losses. Near the close of the year, some recovery developed and most investors believed the worst was over.

In early 1930, the market continued its recovery, but soon the economic picture clouded over. Ben went down to Florida in January. He met a 93 year old man, John Dix, a successful retired businessman. Mr. Dix asked a great number of penetrating questions, displaying a keen mind, and then said with great earnestness:

> Mr. Graham, I want you to do something of the greatest importance. Get on the train to New York tomorrow. Sell out your securities. Pay off your debts and return the capital to the partners in the Joint Account. I wouldn't be able to sleep at night if I were in your position.

Ben thanked the old gentleman and said he would consider his advice. Actually, he then thought the advice was preposterous, as Mr. Dix was probably not far from his dotage and could not possibly have really understood Ben's methods. It turned out, of course, that Mr. Dix was absolutely right and Ben should have been content to keep his position as a "near-millionaire."

The market recovery continued through April but then the market headed down again. Thus, 1930 was to prove to be the most disastrous year in all of Ben's active career. He had already covered nearly all of the short positions, leaving a large long position in securities whose declining market values were accentuated by the substantial margin debt of the Joint Account. The record of the account during the crash was as follows:

	Benjamin Graham Joint Account	Dow Jones Industrials	S&P 500
1929	-20%	-15%	- 7%
1930	-50	-29	-25
1931	-16	-48	-44
1932	- 3	-17	- 8
For entire period	-70%	-74%	-64%

From 1930 on, Ben's main effort was to reduce the margin debt without sacrificing too much of the values inherent in the portfolio. All through this period, quarterly distributions of 1¼ percent of capital were made. A number of the participants withdrew all or part of their capital at various year-ends. The only one to make a new investment in the fund during these difficult years was Jerry Newman's father-in-law.

Since this was near the low point, his show of confidence enabled him to reap a large reward when the recovery began. Considering the fact that the Benjamin Graham Joint Account began this period with approximately 44 percent margin debt, performance equal to the Standard & Poor's would have wiped out the account sometime in 1930. Thus, keeping the fund alive was a great achievement. The small losses of 1931 and 1932 were especially impressive.

A TEACHING CAREER BEGINS

In 1925, after eleven years on Wall Street, Ben decided to write a book to impart his knowledge of the investment world. However, he thought it would first be best to organize his material and to see how it could be used most effectively. He had the inspiration to start teaching if he could. Most Wall Streeters who were interested in teaching became associated with New York University's Graduate School of Finance, because of the convenient location. Ben, however, applied at his alma mater, Columbia, and in 1928 began a 28-year career as a lecturer in the evening division of the School of Business Administration.

Ben taught a two-hour course one evening a week on current investments using rigorous security analysis. Most of his students worked on Wall Street and attended because Ben's teaching worked in actual practice. A number of finance majors attended, as well as faculty members such as David L. Dodd, who enrolled in Ben's first class in order to gain practical insights. As stock market volume and prices rose, news of the practical value of the class spread and enrollment grew rapidly. By 1929, the class reached its peak attendance of over 150 students, a fairly important fraction of the working statisticians or analysts then on Wall Street.

Some of the students returned year after year in order to ask questions about important topics of the day. Ben enjoyed being challenged by a wide range of questions, which he used to present to the class the general principles of finance and security analysis. He presented actual case studies only to develop proven theorems. Typically, both popular and unpopular securities were used as illustrations, fully documented with relevant data.

For example, in one 1929 class a student, bullish on American and Foreign Power Co. warrants, was directed to the blackboard to compute the total market value for the outstanding warrants. When this calculation indicated that the market value for the warrants exceeded the market value for the entire Pennsylvania Railroad, the degree of speculative distortion was brought home to the entire class. At that time the Pennsylvania Railroad common was an investment quality

stock, while American and Foreign Power was a holding company newly formed to pyramid a leveraged public utility empire.

Around 1931, Irving Kahn became Ben's assistant, preparing statistical analyses for use in classroom discussions as well as guiding and marking studies and exams. Often, when a question was asked, Ben chose to withhold his own reply. He knew the superior results that would come from study and participation on the part of the student. Thus, a question on the merits of land trust certificates might result in a team of four or five students being assigned to prepare an evaluation report. Irving would organize the team to prepare a plan for a thorough review of the topic and would coordinate preparation of the written report. Then Ben would bring it before the entire class, adding his penetrating questions and comments with everyone free to attack or defend the methods and conclusions.

Ben understood the merits of the Socratic method, using it to re-examine his own conclusions as harshly as those of the students. He believed that a teacher should stimulate and guide the student with questions, so that the student not only was exposed to the answer but remembered how the answer was reached. Even in as mundane a topic as definitions, Ben never believed in supplying a ready answer. One day Irving asked: "This ad shows a $10 million tranche of a French Government issue being offered. What does tranche mean?" Ben pointed to the dictionary, which defined "tranche" as a slice, such as a slice of cake. Ben said: "If I told you the answer, you might have soon forgotten it." Some 45 years later, the senior author of this sketch still remembers that a tranche is a portion of an underwriting.

The depression years thinned the ranks of bankers, brokers, and analysts. Shrewd Wall Streeters, however, realized that the disoriented markets of those times were creating many buying opportunities. Over the years thousands came to Ben's class and to hear him analyze undervalued securities. Many wanted his keen mind to review issues they believed worthy of consideration. Ben so enjoyed teaching that often he would remain after class for half an hour or longer responding to questions from his fascinated students.

These classes in security analysis were held continuously until Ben's retirement from Wall Street in 1956. So many successful people from the world of finance were attracted to this class that Columbia's Business School grew in stature as the achievements of the faculty became better known in the financial community.

Simultaneously Ben found time to teach for a decade at the New York Stock Exchange's School, now known as the New York Institute of Finance. His lectures on security analysis were adapted into a correspondence course by Walter Morris, Steve Jaquith, and Irving

Kahn. This material remains as the heart of the course still being offered by the New York Institute of Finance. No other single course reached or held so large a student body as this one.

During 1931-1933, Ben also presented a series of lectures at the New School for Social Research. He became a friend of the New School's President, Alvin Johnson, participating in an informal group meeting weekly to discuss possible solutions to the economic crisis. Among the members of the group were William McChesney Martin, A. A. Berle, and a great many other distinguished and thoughtful leaders. These efforts led to Ben's development of an important economic theory, described later in this narrative.

SECURITY ANALYSIS

By 1932, Ben had adjusted the Joint Account to a secure position and began searching for lessons from the stock market crash. In June 1932, he wrote a series of three articles for *Forbes* magazine under the title "Is American Business Worth More Dead Than Alive?" Over 40 percent of the stocks listed on the New York Stock Exchange were selling at less than their net working capital and many were selling below even their cash assets. Ben concluded that the stock market was placing an inordinately low value on American business.

It was time to set to work on the writing of the textbook that he had first projected six years earlier. Professor Dodd agreed to collaborate on the book. Ben would be the senior author and write the entire text in his style. Professor Dodd would make suggestions, check the numerous facts and references, and work up tables. The authors prepared a Table of Contents and a sample chapter. McGraw-Hill retained a Harvard professor of finance to review this proposal and were so impressed with his recommendation that they offered a straight 15 percent royalty, rather than the standard contract that started at 10 percent. The contract was signed near the close of 1932. The authors began work and, with Irving as a research assistant, much of the comparative analysis done by students at Columbia was incorporated into the book.

In 1934, a year and a half later, the first edition of *Security Analysis* was printed. It would be hard to overestimate the significance of this text that has sold over 100,000 copies to date (the Graham/Dodd/Cottle fourth edition was printed in 1962). It has become the basic text for the teaching and practice of two generations of security analysts. Despite the economic, financial, and political chaos at home and abroad, and the overwhelming disillusionment at that time with American enterprise and the investment community, *Security*

Analysis presented a well-reasoned and well-organized case for the great investment opportunities then open to those competent to learn its teachings.

Typical of Ben's wide erudition and sense of the timeless qualities of great philosophy is its opening quotation from Horace: "Many shall be restored that now are fallen and many shall fall that are now in favor." It is beyond the scope of this biographical sketch to examine all the original and radical concepts outlined in this pioneering book, most of which have become so well accepted that it is difficult to imagine why they once were not obvious to the entire investment community.

EARNING A LIVING

The halcyon days of 1928, when Ben's share of the Joint Account's profits exceeded $600,000, were long past. Because their unique profit sharing arrangement was a cumulative one, Ben and Jerry Newman went five years without any payment for their work. Because of the drastic price decline, the fund's capital would have to triple before they would be eligible to start sharing again. One partner suggested a revision be made and, following discussion with some of the larger investors, the terms were revised, reducing the share of Ben and Jerry to a straight 20 percent of profits earned after January 1, 1934. By the end of 1935, all past losses had been made good.

In that year, because the Internal Revenue Service questioned whether the Joint Account really qualified as a partnership or whether it was a quasi-corporation, Graham-Newman Corporation was formed to succeed the partnership as of January 1, 1936.

During these difficult years, Ben spent a considerable amount of time as an expert witness, preparing studies and testifying on complicated cases requiring professional valuation. The U. S. Treasury Department had asked the School of Business at Columbia to recommend an expert. The case involved the valuation for the Federal estate tax of the controlling block of stock in Whitney Manufacturing Co., a maker of chains. The executors claimed that the stock market quotation at the date of the owner's death in 1932 was the proper basis for determining the value. Ben testified that the shares should be valued as a private business, because they represented the controlling interest. He estimated that the minimum liquidating value of the business was its net working capital, with no allowance for plant or equipment. This figure was substantially in excess of the stock market quotation. The Tax Court agreed with Ben.

Because of his obvious abilities in valuation cases, Ben served as an expert witness in some 40 cases. Professor James Bonbright of

Columbia had written the standard text on property valuation and often asked that Ben serve as a companion witness in complicated cases where Ben's practical experience confirmed the professor's theory. The standard compensation was $100 per day for preparation ($460 in 1977 dollars) and $250 for each day in court. Ben regarded these rates as generous. Many of the cases involved the valuation of railroad property for property taxes or reorganizations and were most complex, requiring days of preparation. Since the dollar amounts at stake were large, Ben was often subjected to several days of extensive cross-examination by the opposition as they tried to expose any errors or uncertainties in his presentation. Ben's thorough preparation gave him the sound basis for confident rebuttal of these courtroom attempts.

BEN BECOMES AN ECONOMIC THEORETICIAN

Everyone in the investment community is forced to pay attention to broad economic developments. During the depression of 1921-1922, Ben thought a great deal about the origins of business cycles and possible ways of ameliorating them. He came to the conclusion that the chief cause was the lack of sufficient purchasing power to absorb the increased production that had resulted from the previous boom. Then Ben came across J. A. Hobson's classic *The Economics of Unemployment,* which had set forth this thesis some years earlier. (Hobson's book was an important precursor of John Maynard Keynes.)

Prices, after a sharp rise during World War I and in that postwar boom, fell precipitously in 1921-1922. Many plans were advanced for stabilizing the general level of prices. The best known was Irving Fisher's proposal for a compensated dollar. The gold content of the dollar would be changed under this plan to compensate for changes in purchasing power. Ben decided that a preferable approach would be to give monetary status to a designated "market basket" of some 21 worldwide basic raw materials. Producers of these commodities could sell them as a package to the Treasury Department in much the same manner as gold, then exchangeable for the dollar at a fixed rate or gold point.

Ben did nothing to promote his plan. Some months later, Thomas A. Edison devised a somewhat similar plan based upon farm commodities that would be sold to the Treasury at a fixed price. The economic recovery of the mid-1920's then got under way, with a great expansion in business volume, and accompanied by unusual stability in prices. Ben was busy with his investment activities.

During the deep depression years of 1931 and 1932, Ben restudied his commodity-reserve plan. As mentioned, President Alvin Johnson of the New School had formed a small group who met weekly to consider ways to improve "the sorry scheme of things," a phrase from the *Rubaiyat* they chose to describe the situation. Ben circulated a mimeographed memorandum to the group advocating four plans:

1. The Commodity-Reserve Plan.
2. Slum clearance and subsidized low-cost housing.
3. Low interest rate loans from the Federal Government to the unemployed.
4. Provision for France to meet its World War I debts with 40 million bottles of wine per year—providing one bottle for each American voter.

These were certainly innovative and radical plans for the laissez-faire philosophy of those years. Ben was disappointed that his fourth plan did not receive much consideration, as he believed that it would have added elements of both reality and gaiety into the rather metaphysical financial relations of the two countries.

Two of the young men in the group, Joseph Mead and William McChesney Martin, launched a quarterly journal, *The Economic Forum*. Ben in a 1933 issue of the journal expanded upon his Commodity-Reserve Plan in an article "Stabilized Reflation." While this concept had not been presented in the United States before then, it had been independently arrived at by a Professor of Economics at the University of Rotterdam, Jan Goudriaan, in a 1932 pamphlet "How to Stop Deflation." This pamphlet was little known and Ben did not hear of it for several years. In time, Ben became friends with Professor Goudriaan.

Ben gave a copy of his plan to a friend of Franklin D. Roosevelt. The friend sent word that it was receiving serious consideration in Washington. Nothing happened for two years. Then Louis Bean, economic adviser to Secretary of Agriculture Henry Wallace, visited Ben. The Commodity Credit Corporation had been formed to support farm prices and had acquired large quantities of farm products. Bean thought that Ben's plan might be used as a method of financing the food surpluses, with the added benefit of stimulating prices, in general, by increasing the quantity of money in circulation.

Ben continued to work on the plan, compiling a sizable statistical base to lend credence to its practicality. Finally he was satisfied,

publishing in 1937 the book *Storage and Stability.* McGraw-Hill had justifiable doubts about the commercial success of the book but, in any case, were glad to accommodate the senior author of *Security Analysis.* Bernard Baruch discussed the plan most enthusiastically, and Ben provided him with a set of galley proofs so that Baruch could speed these to President Roosevelt.

The plan received considerable attention from economists. Ben exchanged a number of letters with John Maynard Keynes on this and other economic topics. Keynes agreed with the main goals of Ben's plan. The plan's chief merit was in providing a link between the real world in which major commodities are used and the world of money creation. It also avoided the problem of trying to stabilize the price of a single commodity, because each commodity could fluctuate in price, becoming a larger or smaller component of the "market basket" reflecting supply and demand changes. While the plan has not been adopted, it remains as one of the basic concepts in this area of economic theory, referred to from time to time by eminent economists. In preparation for World War II, the Federal Government started building stockpiles of strategic materials, a policy still maintained.

Ben continued his studies in economics and in 1944 published *World Commodities and World Currency,* a volume detailing many of the problems with world currencies. If this plan for linking commodities and currencies had been adopted, it might have helped to avoid the extremes of price inflation in the mid-1970's.

BROADWAY

Ben's love of reading the world's classics—often in their original language—led him to write a play. In the same year (1934) that the first edition of *Security Analysis* was published, his play "Baby Pompadour" appeared on Broadway. The critic for the *New York Times* had the following comments to make:

> If one of Mr. Graham's students at Columbia University were to turn in an essay on security analysis as trite and diffused in its substance as this little play of his about a nationally famous journalist whose editorial policies are influenced by a moronic chorus-girl mistress, then the student would undoubtedly receive a D minus—and for very good reason, too.
>
> As a well-known figure in the financial world, Mr. Graham should know that neither businessmen with millions of dollars invested in Nicaraguan bananas nor

> Under-Secretaries of State act and talk like a cartoonist's caricature—not even when they're serious. Alas, the only humor in his comedy comes during those pathetic moments when the unfortunate actors—who are here spared the humiliation of identification—find themselves with nothing more to do than laugh at their own pitiful jokes.
>
> Mr. Graham had better stick to one thing or the other—or find himself a new hobby.

The play ran for only four performances and its second try, under the title "True to the Marines," was not successful.

BUILDING A PROFESSION

Over the 50-year period from the start of his teaching career at Columbia and continuing up until his death, Ben devoted most of his waking hours to the education of the "new generation of security analysts" to whom his text was dedicated. Finance students throughout the nation had to absorb the Benjamin Graham approach during their university years and, after entering the investment world, they reread the "Bible" of Graham & Dodd to renew their analytical fundamentals during periods of adversity. Its cases and conclusions restored their sense of proportion when the market went into speculative excesses.

Ben was a prolific writer. He wrote the popular *The Interpretation of Financial Statements* in 1937, the same year that *Storage and Stability* appeared. The *Interpretation* text was written with Charles McGolrick and was aimed at helping the businessman interpret financial statements. It also proved useful to security analysts and others working in the investment world. *Security Analysis* continued to do well, and in 1940 the second edition was published, with extensive revisions and the addition of new current case studies. New materials further increased its usefulness.

Ben was encouraged by the growing number of analysts who made thorough and objective studies of companies and industries. He contributed profusely to *The Analysts Journal (Financial Analysts Journal* beginning in 1960). His writing appeared in the first few issues in 1946 under the pseudonym of "Cogitator" and thereafter at frequent intervals under his own name. Helen Slade was the guiding spirit behind the *Journal*. Her brilliant mind encouraged a number of contributions from Ben. Also, both shared a weakness for cats. Helen had a particular favorite, Alexander, in whose name she purchased several stocks. After the cat's demise, she established an award for the

year's best article in the *Journal* and titled it the "Alexander Award." In later years after Helen Slade's death, the title of the award was changed to the "Graham & Dodd Award." Ben never did make his mind up as to whether or not it was an honor to ascend to Alexander's place.

The Financial Analysts Federation held its first annual conference in 1947. Ben addressed the conference on the need for greater professionalism. He pointed out the necessity of an organized study program, probably culminating in an examination to qualify candidates for a professional designation such as was the case in other professions. He addressed a number of F.A.F. conferences in the years following, often refining his presentation in the *Financial Analysts Journal.*

Recognizing the need to bring his approach to the attention of the astute layman, Ben in 1949 wrote *The Intelligent Investor.* Then he worked on the Third Edition of *Security Analysis,* which came out in 1951. Again the text was brought up-to-date with new and original material covering situations confronting investors at that time.

The stock market was in a general uptrend from 1942 until Ben retired in 1956, except for a basic reaction in 1946 and downward drift to 1949. Ben kept uncovering undervalued special situations. The two lists of special situations in the 1940 edition of *Security Analysis* advanced an average of 252 percent in the following eight years, as compared with a 33 percent advance for the Standard & Poor's Industrials.

THE GEICO STORY

In 1948, a Washington lawyer and a bond salesman from Baltimore called at the Graham-Newman Corporation office with a special situation for sale. After negotiations, the fund bought a half-interest in the company offered for sale, Government Employees Insurance Company. The cost was $720,000, or nearly one-quarter of the Graham-Newman assets. It was necessary to spin off 1.08 shares of GEICO for each share of Graham-Newman Corp. because, under the Investment Company Act, it was not permissible to own more than 10 percent of an insurance company. The market value at that time (July 2, 1948) was $27 for the 1.08 shares. This eventually grew to $16,349 at the peak in 1972 and still stood at $2,407 at the close of 1976—nearly 90 times the starting point.

GEICO had been founded in 1936 in Texas by Leo Goodwin, who had a 25 percent interest, with the balance owned by a Fort Worth banker who was the anxious seller to the Graham-Newman Corporation. The basic concept was that automobile insurance could be

sold by direct mail to the consumer at a reduced rate, as no commissions had to be paid to insurance agents. The policies were available only to government employees, a group that fortunately averaged fewer claims than most. The company had exceptional growth during its first dozen years and this continued after the Graham-Newman purchase. In 1958, it was decided to offer insurance to professional, managerial, technical and administrative workers, as well as government employees. This broadened the market from 15 percent of car owners to 50 percent. Again, these new policyholders also turned out to be preferred risks.

In the following years, growth and profitability continued at an exceptional pace until GEICO became the nation's fifth largest automobile insurer. However, the days of 15 percent underwriting profit margins were over; GEICO was now so large that insurance commissioners would grant rates aimed at producing only a five percent underwriting margin, the same rates granted to other large insurance companies. Starting in 1974 costs rose as inflation accelerated. Adding in the problems of no-fault insurance and low rates, losses skyrocketed and GEICO's net worth dropped from $144 million at the start of 1975 to $37 million at the end of the year.

A great many changes have been made and it is expected that 1977 will see GEICO return to profitability. GEICO continues to have one of the lowest cost distribution systems in the industry, with expense ratios at 14 percent as compared with the industry's 28 percent ratio. The long-term future of the company still has to be determined, but for Graham-Newman investors it has been most profitable with very substantial dividends over the years plus interests in three GEICO affiliates (Government Employees Life Insurance Company, Government Employees Financial Corp., and Criterion Insurance). Ben summed up the fact that the decision to buy the half-interest in GEICO brought in vastly more profits than all of his other investments combined as follows: "An obvious (moral) is that there are several different ways to make and keep money in Wall Street."

FAREWELL TO NEW YORK

Ben's personality required a stream of new challenges. The Graham-Newman Corporation continued to prosper, essentially repeating the same processes for selecting undervalued securities. The fabulous success of the Government Employees Insurance Co. investment also blunted much of his never very great desire for financial success. None of Ben's five children were interested in entering the investment world and Jerry Newman's son, Howard Newman, had

become the chief executive officer of Philadelphia and Reading Company, preferring a life in active corporate management. Thus, in 1956, they decided to liquidate the Graham-Newman Corporation.

Ben never regretted his move to California in 1956. At age 62, he began a new association as an Adjunct Professor of Finance at the University of California at Los Angeles. Professor John Shelton tells the story about his first meeting with Ben. He had a rather jaundiced view of the intellectual capacities of most Wall Streeters and assumed that Ben was a typical example but felt an obligation to take Ben to lunch. At the UCLA Faculty Club, while moving to their table, Professor Shelton introduced one of his colleagues, mentioning that he was writing a book on one of the modern Spanish poets. Ben burst out enthusiastically: "He's one of my favorites," and then proceeded to recite in Spanish one of the poet's works. Professor Shelton decided on the spot that there must be more to security analysis than he thought.

Nearly a decade was spent in Los Angeles and at UCLA before the final move to apartments in La Jolla, California for half the year and Aix-en-Provence for the balance. As Ben phrased it, each of the apartments had a "glimpse of the sea" rather than a full view.

He continued to devote a part of his time to the investment world. When asked in 1974 to be the main speaker at a C.F.A. Seminar entitled *The Renaissance of Value*, Ben accepted enthusiastically. The Seminar was scheduled to meet at his convenience on his fall trip from California by way of New York to Europe, visiting children and friends along the way. The Dow Jones Industrial Average had fallen to near the 600 level in September 1974. Ben's message was to select some of the many issues then available at prices clearly low by all reasonable valuation standards. "How long will such 'fire-sale stocks' continue to be given away?"

The concluding question at the session was: "Mr. Graham, are you amused or disappointed that it takes a real bear market for analysts to be interested in your value approach towards investment?". Ben immediately replied: "Walpole said that the thinking man looks at the world and sees a comedy; the feeling man looks at the world and sees a tragedy."

The following year saw the highest award of the profession, the Molodovsky Award, presented to Ben at the Annual Conference of The Financial Analysts Federation. The cash grant that went with the award was devoted to a research project that Ben was interested in and which he hoped might eventually develop into a project for publication by The Financial Analysts Research Foundation. This research was aimed at developing rough filters or screens for narrowing down the universe of common stocks to a representative group of likely candidates for

purchase. Ben began to test this new approach in a modest way with some California friends. While death brought this phase of his research to an end, it nonetheless did show his continued devotion to research as displayed so well in *Security Analysis* and *The Intelligent Investor.*

Irving Kahn arranged a memorial service for Benjamin Graham at the Chapel of Columbia University. A hundred old and close friends of Ben attended—his partner Jerome Newman, Columbia's President, William McGill, David Dodd, Professor James Bonbright, Ben's colleagues for half a century, and many from the investment and academic communities. Friends from other areas of his life also attended. A group of ten blacks from the Mt. Zion Baptist Church of Bridgeport, Connecticut gave homage to the stranger who made it possible for them to worship in their own church.

Ben's life has affected many. All financial analysts owe so much to the pioneering efforts and works of Benjamin Graham—truly, the Dean of our profession.

SOME REFLECTIONS ON BEN GRAHAM'S PERSONALITY

By Irving Kahn

Most people knew Ben through his writings. Those who were his students or worked with him got to know the man as well as the legend. Physically, Ben was quite short, but his massive head and penetrating blue eyes made people forget his diminutive stature.

He had several outstanding characteristics. His speed of thought was so great that most people were puzzled at how he could resolve a complicated question directly after having heard it. His mental training came from his rigorous study of mathematics, particularly geometry, which required close and exact reasoning before accepting or rejecting either a premise or a conclusion.

He had another extraordinary characteristic in the breadth and depth of his memory. This explains why he could read Greek, Latin, Spanish and German. Even more remarkable, without having studied Spanish formally, he was able to translate a Spanish novel into literary English so professionally that it was accepted by an American publisher.

In his early years, Ben was both a skier and a tennis player. But his real pleasure was to exercise his mind over a wide range of subjects far beyond his specialties in the world of finance. He loved music, especially the major operas for the wisdom of their lyrics, as well as their melodies. He had a private, but serious hobby of making improvements in the field of plane geometry. He actually patented several versions of a simplified protractor and a circular slide rule.

With so many interests, it is understandable that, while Ben was a devoted father, he was really more married to his business and cultural interests than the normal husband. Despite these many and varied interests, he had time to give to worthy charities. He became the president of the Jewish Guild for the Blind, attracting many devoted benefactors to their good works.

He helped numerous refugees from Hitler's Germany with advice, recommendations, and money to get them started in America. Many of these men later became important faculty members and authors in some of our major universities.

In addition to this tremendous range of interests and talents, he was a very warm man in personal relations. A needy colleague would always be helped—and always anonymously. He loved to make others

laugh by means of his quick wit and large inventory of puns. Everyone that ever had dealings with Ben came away with certain strong reactions. These included the uplift that comes from someone who shares your enthusiasms and hopes, as well as the strong sense of a very fair mind, entirely objective, in distinguishing between what was fair rather than what was self-serving. In sum, Ben Graham was such a rare combination of qualities, only those who knew him well over the years can do full justice to presenting the whole man.

In the world of finance Ben's epitaph will be as was Christopher Wren's in St. Paul's, "If you seek his monument—look about you."

AN HOUR WITH MR. GRAHAM

by Hartman L. Butler, Jr., C.F.A.

La Jolla, California

March 6, 1976

HB: Mr. Graham, I do appreciate so much being able to come and visit with you this afternoon. When Bob Milne learned that Mrs. Butler and I would be in La Jolla, he suggested that I not only visit with you but also bring along my cassette tape recorder. We have much I would like to cover. First, could we start with a topical question—Government Employees Insurance Company—with GEICO being very much in the headlines.

Graham: Yes, what happened was the team came into our office and after some negotiating, we bought half the company for $720,000. It turned out later that we were worth—the whole company—over a billion dollars in the stock market. This was a very extraordinary thing. But we were forced by the SEC to distribute the stock among our stockholders because, according to a technicality in the law, an investment fund was not allowed more than 10 percent of an insurance company. Jerry Newman and I became active in the conduct of GEICO, although we both retired a number of years ago. I am glad I am not connected with it now because of the terrific losses.

HB: Do you think GEICO will survive?

Graham: Yes, I think it will survive. There is no basic reason why it won't survive, but naturally I ask myself whether the company did expand much too fast without taking into account the possibilities of these big losses. It makes me shudder to think of the amounts of money they were able to lose in one year. Incredible! It is surprising how many of the large companies have managed to turn in losses of $50 million or $100 million in one year, in these last few years. Something unheard of in the old days. You have to be a genius to lose that much money.

HB: Looking back at your own life in the investment field, what are some of the key developments or key happenings, would you say? You went to Wall Street in 1914?

Graham: Well, the first thing that happened was typical. As a special favor, I was paid $12 a week instead of $10 to begin. The next thing that happened was World War I broke out two months later and the stock exchange was closed. My salary was reduced to $10—that is one of the things more or less typical of any young man's beginnings. The next thing that was really important to me—outside of having made a rather continuous success for 15 years—was the market crash of 1929.

HB: Did you see that coming at all—were you scared?

Graham: No. All I knew was that prices were too high. I stayed away from the speculative favorites. I felt I had good investments. But I owed money, which was a mistake, and I had to sweat through the period 1929-1932. I didn't repeat that error after that.

HB: Did anybody really see this coming—the crash of 1929?

Graham: Babson did, but he started selling five years earlier.

HB: Then in 1932, you began to come back?

Graham: Well, we sweated through that period. By 1937, we had restored our financial position as it was in 1929. From then on, we went along pretty smoothly.

HB: The 1937-1938 decline, were you better prepared for that?

Graham: Well, that led us to make some changes in our procedures that one of our directors had suggested to us, which was sound, and we followed his advice. We gave up certain things we had been trying to do and concentrated more on others that had been more consistently successful. We went along fine. In 1948, we made our GEICO investment and from then on, we seemed to be very brilliant people.

HB: What happened in the only other interim bear market—1940-1941?

Graham: Oh, that was only a typical setback period. We earned money in those years.

HB: You earned money after World War II broke out?

Graham: Yes, we did. We had no real problems in running our business. That's why I kind of lost interest. We were no longer very challenged after 1950. About 1956, I decided to quit and to come out here to California to live.

I felt that I had established a way of doing business to a point where it no longer presented any basic problems to be solved. We were going along on what I thought was a satisfactory basis, and the things that presented themselves were typically repetitions of old problems which I found no special interest in solving.

About six years later, we decided to liquidate Graham-Newman Corporation—to end it primarily because the succession of management had not been satisfactorily established. We felt we had nothing special to look forward to that interested us. We could have built up an enormous business had we wanted to, but we limited ourselves to a maximum of $15 million of capital—only a drop in the bucket these days. The question of whether we could earn the maximum percentage per year was what interested us. It was not the question of total sums, but annual rates of return that we were able to accomplish.

HB: When did you decide to write your classic text, *Security Analysis*?

Graham: What happened was that in about 1925, I thought that I knew enough about Wall Street after 11 years to write a book about it. But fortunately, I had the inspiration instead to learn more on the subject before I wrote the book, so I decided I would start teaching if I could. I became a Lecturer at the Columbia School of Business for the extension courses. In 1928, we had a course in security analysis and finance—I think it was called Investments—and I had 150 students. That was the time Wall Street was really booming.

The result was it took until 1934 before I actually wrote the book with Dave Dodd. He was a student of mine in the first year. Dave was then Assistant Professor at Columbia and was anxious to learn more. Naturally, he was indispensable to me in writing the book. The First Edition appeared in 1934. Actually, it came out the same time as a play of mine which was produced on Broadway and lasted only one week.

HB: You had a play on Broadway?

Graham: Yes. "Baby Pompadour" or "True to the Marines." It was produced twice under two titles. It was not successful. Fortunately, *Security Analysis* was much more successful.

HB: That was *the* book, wasn't it?

Graham: They called it the "Bible of Graham and Dodd." Yes, well now I have lost most of the interest I had in the details of security analysis which I devoted myself to so strenuously for many years. I feel that they are relatively unimportant, which, in a sense, has put me opposed to developments in the whole profession. I think we can do it successfully with a few techniques and simple principles. The main point is to have the right general principles and the character to stick to them.

HB: My own experience is that you have to be a student of industries to realize the great differences in managements. I think that this is one thing an analyst can bring to the solution.

Graham: Well, I would not deny that. But I have a considerable amount of doubt on the question of how successful analysts can be overall when applying these selectivity approaches. The thing that I have been emphasizing in my own work for the last few years has been the group approach. To try to buy groups of stocks that meet some simple criterion for being undervalued—regardless of the industry and with very little attention to the individual company. My recent article on three simple methods applied to common stocks was published in one of your Seminar Proceedings.

I am just finishing a 50-year study—the application of these simple methods to groups of stocks, actually, to all the stocks

in the Moody's Industrial Stock Group. I found the results were very good for 50 years. They certainly did twice as well as the Dow Jones. And so my enthusiasm has been transferred from the selective to the group approach. What I want is an earnings ratio twice as good as the bond interest ratio typically for most years. One can also apply a dividend criterion or an asset value criterion and get good results. My research indicates the best results come from simple earnings criterions.

HB: I have always thought it was too bad that we use the price/earnings ratio rather than the earnings yield measurement. It would be so much easier to realize that a stock is selling at a 2.5 percent earnings yield rather than 40 times earnings.

Graham: Yes. The earnings yield would be more scientific and a more logical approach.

HB: Then with roughly a 50 percent dividend payout, you can take half of the earnings yield to estimate a substainable dividend yield.

Graham: Yes. Basically, I want to double the interest rate in terms of earnings return. However, in most years the interest rate was less than five percent on AAA bonds. Consequently, I have set two limits. A maximum multiple of 10 even when interest rates are under five percent, and a maximum multiple of 7 times even when interest rates are above seven percent as they are now. So typically my buying point would be double the current AAA interest rate with a maximum multiplier between 10 and 7. My research has been based on that.

I received in Chicago last year the Molodovsky Award.

HB: I understand that you have about completed this research.

Graham: Imagine—there seems to be practically a foolproof way of getting good results out of common stock investment with a minimum of work. It seems too good to be true. But all I can tell you after 60 years of experience, it seems to stand up under any of the tests that I would make up. I would try to get other people to criticize it.

HB: By some coincidence as you were becoming less active as a writer, a number of professors started to work on the random walk. What do you think about this?

Graham: Well, I am sure they are all very hardworking and serious. It's hard for me to find a good connection between what they do and practical investment results. In fact, they say that the market is efficient in the sense that there is no particular point in getting more information than people already have. That might be true, but the idea of saying that the fact that the information is so widely spread that the resulting prices are logical prices—that is all wrong. I don't see how you can say that the prices made in Wall Street are the right prices in any intelligent definition of what right prices would be.

HB: It is too bad there have not been more contributions from practicing analysts to provide some balance to the brilliant work of the academic community.

Graham: Well, when we talk about buying stocks, as I do, I am talking very practically in terms of dollars and cents, profits and losses, mainly profits. I would say that if a stock with $50 working capital sells at $32, that would be an interesting stock. If you buy 30 companies of that sort, you're bound to make money. You can't lose when you do that. There are two questions about this approach. One is, am I right in saying if you buy stocks at two-thirds of the working capital value, you have a dependable indication of group undervaluation? That's what our own business experience proved to us. The second question, are there other ways of doing this?

HB: Are there any other ways?

Graham: Well, naturally, the thing that I have been talking about so much this afternoon is applying a simple criterion of the value of a security. But what everybody else is trying to do pretty much is pick out the "Xerox" companies, the "3M's", because of their long-term futures or to decide that next year the semiconductor industry would be a good industry. These don't seem to be dependable ways to do it. There are certainly a lot of ways to keep busy.

HB: Would you have said that 30 years ago?

Graham: Well, no, I would not have taken as negative an attitude 30 years ago. But my positive attitude would have been to say, rather, that you could have found sufficient examples of individual companies that were undervalued.

HB: The efficient market people have kind of muddied the waters, haven't they, in a way?

Graham: Well, they would claim that if they are correct in their basic contentions about the efficient market, the thing for people to do is to try to study the behavior of stock prices and try to profit from these interpretations. To me, that is not a very encouraging conclusion because if I have noticed anything over these 60 years on Wall Street, it is that people do not succeed in forecasting what's going to happen to the stock market.

HB: That is certainly true.

Graham: And all you have to do is to listen to "Wall Street Week" and you can see that none of them has any particular claim to authority or opinions as to what will happen in the stock market. They, and economists, all have opinions and they are willing to express them if you ask them. But I don't think they insist that their opinions are correct, though.

HB: What thoughts do you have on index funds?

Graham: I have very definite views on that. I have a feeling that the way in which institutional funds should be managed, at least a number of them, would be to start with the index concept—the equivalent of index results, say 100 or 150 stocks out of the *Standard & Poor's 500.* Then turn over to managers the privilege of making a variation, provided they would accept personal responsibility for the success of the variation that they introduced. I assume that basically the compensation ought to be measured by the results either in terms of equaling the index, say Standard & Poor's results, or to the extent by which you improve it. Now in the group discussions of this thing, the typical money managers don't accept the idea and the reason for non-acceptance is chiefly

that they say—not that it isn't practical—but that it isn't sound because different investors have different requirements. They have never been able to convince me that that's true in any significant degree—that different investors have different requirements. All investments require satisfactory results, and I think satisfactory results are pretty much the same for everybody. So I think any experience of the last 20 years, let's say, would indicate that one could have done as well with Standard & Poor's than with a great deal of work, intelligence, and talk.

HB: Mr. Graham, what advice would you have to a young man or woman coming along now who wants to be a security analyst and a Chartered Financial Analyst?

Graham: I would tell them to study the past record of the stock market, study their own capabilities, and find out whether they can identify an approach to investment they feel would be satisfactory in their own case. And if they have done that, pursue that without any reference to what other people do or think or say. Stick to their own methods. That's what we did with our own business. We never followed the crowd, and I think that's favorable for the young analyst. If he or she reads *The Intelligent Investor*—which I feel would be more useful than *Security Analysis* of the two books—and selects from what we say some approach which one thinks would be profitable, then I say that one should do this and stick to it. I had a nephew who started in Wall Street a number of years ago and came to me for some advice. I said to him, "Dick, I have some practical advice to give you which is this. You can buy closed-end investment companies at 15 percent discounts on an average. Get your friends to put "x" amount of dollars a month in these closed-end companies at discounts and you will start ahead of the game and you will make out all right." Well, he did do that—he had no great difficulty in starting his business on that basis. It did work out all right and then the big bull market came along and, of course, he moved over to other fields and did an enormous amount of speculative business later. But at least he started, I think, on a sound basis. And if you start on a sound basis, you are half-way along.

HB: Do you think that Wall Street or the typical analyst or portfolio managers have learned their lessons of the "Go-Go" funds, the growth cult, the one-decision stocks, the two-tier market, and all?

Graham: No. They used to say about the Bourbons that they forgot nothing and they learned nothing, and I'll say about the Wall Street people, typically, is that they learn nothing, and they forget everything. I have no confidence whatever in the future behavior of the Wall Street people. I think this business of greed—the excessive hopes and fears and so on—will be with us as long as there will be people. There is a famous passage in Bagehot, the English economist, in which he describes how panics come about. Typically, if people have money, it is available to be lost and they speculate with it and they lose it—that's how panics are done. I am very cynical about Wall Street.

HB: But there are independent thinkers on Wall Street and throughout the country who do well, aren't there?

Graham: Yes. There are two requirements for success in Wall Street. One, you have to think correctly; and secondly, you have to think independently.

HB: Yes, correctly and independently. The sun is trying to come out now, literally, here in La Jolla. What do you see of the sunshine on Wall Street?

Graham: Well, there has been plenty of sunshine since the middle of 1974 when the bottom of the market was reached. And my guess is that Wall Street hasn't changed at all. The present optimism is going to be overdone, and the next pessimism will be overdone, and you are back on the Ferris Wheel—whatever you want to call it—Seesaw, Merry-Go-Round. You will be back on that. Right now, stocks as a whole are not overvalued, in my opinion. But nobody seems concerned with what are the possibilities that 1970 and 1973-1974 will be duplicated in the next five years. Apparently, nobody has given any thought to that question. But that such experiences will be duplicated in the next five years or so, you can bet your Dow Jones Average on that.

HB: This has been a most pleasant and stimulative visit. We will look forward to receiving in Charlottesville your memoirs manuscript. Thank you so much, Mr. Graham!

In these days of sophisticated techniques for measuring portfolio performance, it is interesting to read Ben's impressionistic comments about the profits of the investment funds that he managed. No information is available on the Grahar Corporation except that the two and a half years ended with "a substantial profit," after providing him with a salary that amounted to four percent of the starting capital plus six percent annually for distributions to the investors. Thus, the total annual return must have exceeded 10 percent. The return for the Dow Jones Industrial Average would have been as follows:

	Dow Jones	Dividend	Index Including Reinvested Dividends
6-1-23	95.36	–	100.00
12-31-23	95.52	2.30	102.58
12-31-24	120.51	4.27	134.00
12-31-25	156.66	4.17	178.84
	Annual compounded rate of return	=	26.2%

The record of the Benjamin Graham Joint Account can only be approximated for the intermediate years, from references supplied in Ben's memoirs. The record for the entire period of ten years is, however, reasonably correct since it was not until the tenth year, 1935, that the ravages of the crash were recovered in full and, for the first time since 1928, Ben became eligible for profit-sharing. The following figures are only approximations:

	Indexes—Including Reinvested Dividends		
12-31	Ben Graham Joint Account*	S&P 500	Dow Jones Industrials
1925	100	100.00	100.00
1926	110	111.60	104.40
1927	150	153.56	138.10
1928	250	220.83	208.73
1929	200	202.05	177.80
1930	100	151.54	125.73
1931	80	85.62	65.93
1932	75	78.51	54.63
1933	115	121.15	94.16
1934	120	119.33	101.51
1935	180	176.13	145.06
Annual rate of return	6%	5.8%	3.8%

*Approximate figures

This decade of operations produced performance for the investors modestly greater than that of the market—even after providing Ben and Jerry with very substantial profit sharing in the first three years—and fairly substantial profit sharing in the final two years.

The record of Graham-Newman Corporation is documented in the following tables covering the period from January 31, 1945, when figures were first published in *Moody's Manual of Banks and Finance Companies*, until 1956. Table 1 consists of the raw data indicating the basic record of Graham-Newman Corporation during its final dozen years of operation except for the Government Employees Insurance Company shares.

TABLE 1

Investment Performance of the Graham-Newman Corp. (Excluding GEICO)

	Asset Value	Dividend	Value of Rights	Index	Total Return	S&P 500 Total Return	S&P 500 Index
1-31-45	140.84	31.18	4.08	100.00			100.00
1-31-46	140.51	33.20	5.00	126.89	26.89%	42.76%	142.76
1-31-47	116.84	12.20		116.53	- 8.16	-11.85	125.85
1-31-48	114.13	17.10		130.88	12.31	- .83	124.80
1-31-49	97.56	5.20	28.00*	149.95	14.57	9.94	137.21
1-31-50	106.57	10.55		180.02	20.05	19.51	163.98
**1-31-51	123.25	12.00		228.46	26.91	35.66	222.45
**1-31-52	125.79	17.75		266.07	16.46	17.96	262.40
**1-31-53	136.11	9.24		307.44	15.55	15.12	302.08
**1-31-54	128.67	9.03		311.04	1.17	14.36	345.46
**1-31-55	101.82	44.42		353.51	13.65	46.36	505.61
**1-31-56	89.61	32.77		424.89	20.19	24.11	627.52
**8-20-56	93.11	20.27		537.60	26.53	12.32	704.82

* Includes $27.00 market value of 1.08 sh. Government Employees Insurance Co.
**Adjusted for 1-for-10 reverse split.

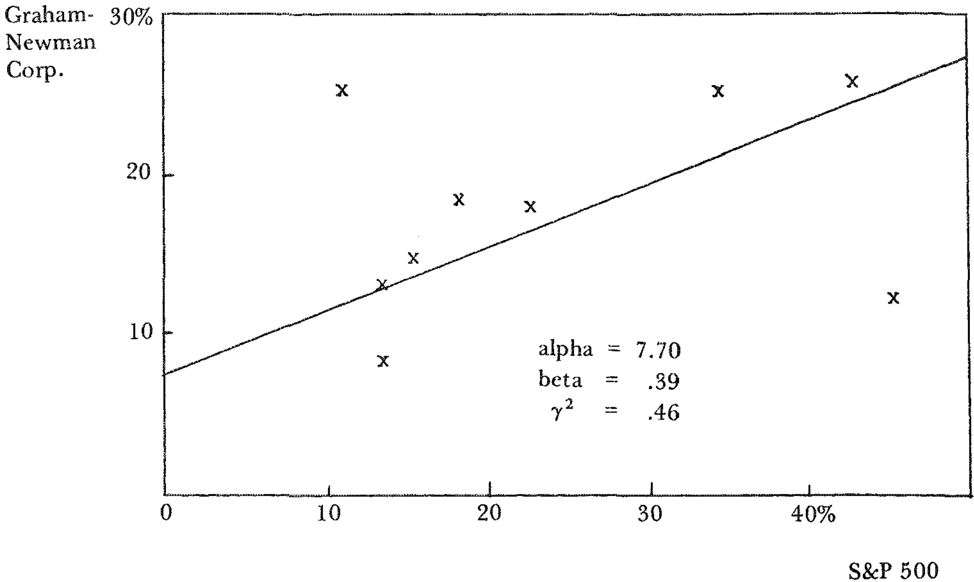
These performance results can be summarized as follows:

	Graham-Newman Corp.	S&P 500
Annual rate of return	17.4%	18.3%
Management fee	-1.9	
Annual return to shareholders	15.5%	

This rate of return was not exceptional, but its character can be seen from Figure 1 which shows the risk-adjusted rates of return earned by the fund and by the S&P 500.

FIGURE 1

Risk-Adjusted Rates of Return; Graham-Newman Corp. and S&P 500



The relationship depicted in Figure 1 indicates a beta coefficient of .39 and an alpha coefficient of 7.70. The data are adjusted for the risk-free rate of return as measured by the interest rate on 91-day U.S. Treasury Bills. The performance of Graham-Newman Corporation during these dozen years indicates a very low sensitivity to market risks—with returns more directly related to the maturing of the special situations that Ben kept finding. The risk characteristics illustrated in Figure 1 are summarized as follows:

S&P 500 performance	18.3% per year
Risk-free rate of return	- 1.2
S&P 500 Premium for risk	17.1%
Graham-Newman Corp.	
Expected risk premium	6.6%
Risk-free rate of return	1.2
Expected return	7.8%
Actual return	15.5%
Excess return	+ 7.7%

In summary, the fund did 7.7 percent per year better than would have been expected considering its low beta (sensitivity to market fluctuations). It is doubtful, however, that very many of the investors in the Graham-Newman Corporation used this approach to measure the success of their investment. The fabulous success of the GEICO investment far overshadowed everything else.

Table 2 shows the market values for the holdings of the two main GEICO companies that were distributed; GEICO itself, and Government Employees Life Insurance Company. Two other affiliates, Government Employees Financial Corporation and Criterion Insurance Company, are not shown, although they would have added modestly to the profits received if the rights to these issues had been exercised. As this table makes no provision for the reinvestment of dividends, total returns would have been larger than those indicated.

TABLE 2

Market Values of the GEICO and GEICO Life Shares

	GEICO			GEICO Life		
	Shares	Price	Value	Shares	Price	Value
1-31-49	1.80	28.50	$ 51			
1-31-50	2.16	57.25	124	2.16	15.25	$ 33
1-31-51	2.52	39.75	100	2.16	17.50	38
1-31-52	3.60	38.50	139	2.16	14.88	32
1-31-53	3.60	58.50	211	2.16	18.00	39
1-31-54	3.96	88.25	349	2.16	28.35	61
1-31-55	7.92	70.50	558	2.16	34.00	73
1-31-56	8.55	66.50	569	2.16	42.50	92
8-20-56	9.20	55.00	506	2.21	49.00	108
12-31-60	29.40	90.88	2,672	4.77	63.00	301
12-31-65	46.34	105.75	4,900	14.59	51.00	744
12-31-70	111.14	51.94	5,773	30.96	30.00	929
1972 High	222.27	63.75	14,170	31.89	66.25	2,113
12-31-76	231.16	7.31	1,690	47.83	15.00	717

The results of an investment in 100 shares of Graham-Newman Corporation common at 1-31-48, costing $11,413, compared with an equivalent investment in the Standard & Poor's 500, are presented below. Neither series has been adjusted for dividends, but the proceeds from the 1956 liquidation of Graham-Newman were assumed to have been reinvested in the S&P 500. These results certainly speak for themselves.

	Graham-Newman and GEICO	S&P 500
1-31-48	$ 11,413	$11,413
8-20-56	70,413	30,968
1972 Peak	1,658,989	93,181
12-31-76	262,490	84,060
1948-76 Appreciation	11.4% per year	7.1% per year

QUOTATIONS FROM BENJAMIN GRAHAM

We have stressed theory not for itself alone but for its value in practice. We have tried to avoid prescribing standards which are too stringent to follow, or technical methods which are more trouble than they are worth.

It is the conservative investor who will need most of all to be reminded constantly of the lessons of 1931-1933 and of previous collapses. For what we shall call fixed-value investments can be soundly chosen only if they are approached—in the Spinozan phase—'from the viewpoint of calamity.' In dealing with other types of security commitments, we have striven throughout to guard the student against overemphasis upon the superficial and the temporary. Twenty years of varied experience in Wall Street have taught the senior author that this overemphasis is at once the delusion and the nemesis of the world of finance.

Security Analysis
First Edition, 1934

We have no scoring system for security analysts, and hence no batting averages. Perhaps that is just as well. Yet it would be anomalous indeed if we were to devote our lives to making concrete recommendations to clients without being able to prove, either to them or to ourselves, whether we were right in any given case. The worth of a good analyst undoubtedly shows itself decisively over the years in the sum total results of his recommendations.

The Analysts Journal
First Quarter, 1946

If we could assume that the price of each of the leading issues already reflects the expectable developments of the next year or two, then a random selection should work out as well as one confined to those with the best near-term outlook.

Security Analysis
Third Edition, 1951

The investor with a portfolio of sound stocks should expect their prices to fluctuate and should neither be concerned by sizable declines nor become excited by sizable advances. He should always remember that market quotations are there for his convenience, either to be taken advantage of or to be ignored.

Sound generalizations can be more dangerous than unsound ones because they lure more people into unwarranted actions.

The Intelligent Investor
Third Edition, 1959

The post-World War II world has been characterized as 'brave' and 'new.' Brave it is, indeed, but we are not positive that it is equally new. We can be skeptical about a complete break with the past.

Security Analysis
Fourth Edition, 1962

Common stocks have one important investment characteristic and one important speculative characteristic. Their investment value and average market price tend to increase irregularly but persistently over the decades, as their net worth builds up through the reinvestment of undistributed earnings . . . . However, most of the time common stocks are subject to irrational and excessive price fluctuations in both directions, as the consequence of the ingrained tendency of most people to speculate or gamble—i.e., to give way to hope, fear and greed.

Financial Analysts Journal
September/October, 1976

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