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Report #3
Trips to:
First National City Bank of New York
  Bond Administration Department
  Bond Cage Department
The New York Stock Exchange
The Toronto Stock Exchange

Duration: May 17 - July 3, 1959

FIRST NATIONAL CITY BANK OF NEW YORK

Bond Administration Department

A bank's assets include three broad categories: cash, loans and investments, and the latter is the primary concern of the Bond Administration Department. After cash reserve requirements have been met, all funds not loaned are placed at the disposal of the Bond Administration for investment in securities at the best possible interest return consistent with safety and liquidity.

The Bond Administration Department also underwrites and deals in municipal securities, trades Federal funds, assists clients with their investments, and advises corporations on their financing problems. Related to its several responsibilities, the Department is divided into three sections: Governments, Municipals, and the Corporate Finance Advisory Service.

Permissible investments for a commercial bank must qualify from the standpoint of marketability and investment quality. Regulations specifically prohibit the purchase of common or preferred stocks. Bonds or any other evidences of debt must be free of any element of speculation. The bank's portfolio is therefore chiefly invested in U. S. Treasury securities for maximum security and marketability and in high grade state and municipal bonds which provide the best net investment earnings because of exemption from Federal tax. Holding in-corporate bonds are limited in amount since the net return after taxes are relatively less attractive.

The portfolio of any commercial bank may be thought of as a reservoir to which funds flow and from which they are withdrawn, depending upon the conditions of the economy and the resultant rise and fall in demand for loans.

By the very nature of the investment function, the bond portfolio frequently must operate at a disadvantage because usually funds are not available for investment when credit is tight and bond price attractive -- the money then being committed to the loan portfolio. Conversely funds are usually in good supply when bond prices become cheap. To anticipate changes in the availability of funds and the action of the market, Bond Administration must be constantly alert to changes in economic conditions, the direction of Federal Reserve credit policy and the treasury's probably financing program, as well as shifts in the supply and demand for savings in all major investment fields. The nation's fiscal policy, specifically whether the Federal budget entails a surplus or deficit, has a direct impact on the supply of government securities, but the bearing on the various sectors of the market will vary depending on the Treasury's choice of maturity for new issues. The demand for borrowed funds in the form of bank loans and new bond flotations by business corporations, the volume of mortgage financing of homes and office buildings, and state and municipal financing of schools, highways, and other public works require careful estimates. Consideration of these factors requires close liaison with the Economics Department and the senior lending officers of the bank.

Probably the first consideration governing the investment of funds is the needs to establish sufficient holdings of short-term treasuries, where price fluctuations are minor, to serve as a liquidity reserve against rising loan demands and deposit withdrawals. The remainder, available for more permanent investment, may be then committed to government maturities due beyond the short-term range, or to municipal securities, and to a lesser extent, corporate bonds. While it is often impractical to alter commitments radically when once made, there is nevertheless a constant effort to shift the character and maturity range of the Bank's investments in order to maximize profit opportunities in a rising market or to reduce exposure to depreciation in a falling market.

Let us examine the three sections of the Bond Administration Department:

I. Government Section

The Government Section is in charge of handling government securities. Its primary functions are:

1. To manage the Bank's $1.5 billion Treasury obligation portfolio and to execute all the market trading.

2. To trade millions daily in the Federal fund market with correspondent bank --an important means of maintaining the required level in the bank's legal reserve position or assuming full employment of temporary excess funds.

3. To advise customers and execute orders from the smallest denominations up, at net prices in the over-counter market, without commission or other charges.

(1) The Government Section has as its primary responsibility the active management of the Bank's Treasury obligations portfolio and the execution of all market trading.

Every week, the Money Committee of the Bank composed of its senior officers has to make decisions concerning the amount and type of investment in marketable Treasury obligations. The marketable public issues include treasury bonds, treasury notes, treasury certificates of indebtedness and bills, postal savings baonds, and Panama bonds.

a. Bonds - Treasury bonds represent long-term obligations and have maturities of five years and above. The variation in coupon rate reflects the treasury practice of selecting a rate at the time of issue which, in accordance with the maturity, permits offering the bonds at par.

b. Notes - Treasury notes, which mature in one to five years, represent medium-term obligations. Unlike treasury bonds, the notes sold to the public or banks are not callable before maturity. They are traded exclusively over the counter where the principal buyers are commercial banks.

c. Certificates and bills - Treasury certificates of indebtedness and treasury bills are short-term obligations which mature in one year or less. The certificate of indebtedness, which had been the principal means of short-term treasury financing, was completely replaced in 1934 by the treasury bill which had been first introduced in 1929.

Treasury bills are sold at auction on a discount basis at prices set by the market. Since the bills usually mature in 91 days, there is a 13-week cycle of issues. New issues of treasury bills are obtained only by tender to the teasury through the Federal Reserve banks. Public announcement of offerings of treasury bills are usually made on Thursday, tenders are received up to 2:00 p.m. (Eastern time) on the following Monday, and the bills are usually dated and issued on Thursday of that week.

The bills are bought chiefly by commercial banks for secondary reserve purposes, by corporations for working capital or income tax payment purposes.

According to the Bank's need in cash and the condition of the money market, the Money Committee of the City Bank decides the amount and types of treasury obligations to be invested in, and the Government Section is charged with the execution of the Committee's policy. To do so, buying or selling treasury obligations -- the Section contacts with many dealers in order to get the best price.

The Government Section also specializes in the buying and selling of Federal Agency issues such as territorial bonds, Commodity Credit Corporation securities, Federal Deposit Insurance Corporation securities, Federal Housing Administration securities, Federal Land Bank securities, etc

(2) The second important function of the Government Section is to trade daily in the Federal funds market with correspondent banks and others. To illustrate: suppose the City Bank today has an excess reserve of ten million. Then the Government Section tries to get in touch with other banks in the New York area or banks throughout the United States, in order to lend its excess reserve to these banksthat temporarily are short of reserve. On the other hand, when the City Bank is short of reserves for a few days, it will ask for temporary loans from other banks which have excess reserve.

Thus banks that are temporarily short of reserves can make up their deficiencies without increasing the over-all level of reserve which happens when banks borrow direct from the Federal Reserve's discount window. Moreover, trading in Federal funds makes it possible for the banking system to use its reserve more efficiently and makes sudden changes in the money supply less likely. This trading is beneficial to the borrowing banks too because the interest rate applied to their loan is smaller than the Federal Reserve's discount rate for the same transaction.

In performing this trading, the Government Section maintains a record of all its sales or purchases during the day.

II. Municipal Section

The Municipal Section watches over the City Bank's $500 million portfolio of state and municipal securities, and also plays a major role in the underwriting and distribution of state and municipal bonds originating throughout the United States. As manager, it participates in syndicates which have underwritten about one-quarter of all the long-term general obligations annually issued by the states and their subdivisions. The department carries an inventory of bonds for sale to investors.

It is interesting to study municipal bonds, and the procedure of underwriting and reoffering them.

1. Municipal Bonds

Broadly speaking, Municipal bonds are issued by any of the 49 states, cities, towns, counties, villages, school districts, and other political subdivisions. In short, by any domestic taxing authority below the level of the Federal Government. A Municipal Bond is, in effect, a long-term loan made by the bondholder to the issuer, for the purpose of providing public improvements, such as roads, schools, waterworks, public buildings, sewers, and other essential services.

2. Types of Municipal Bonds

There are four main types of Municipal bonds:

A. General Obligation Bonds -- These bonds are secured by full faith credit and are payable from the full taxing power of the municipality.

B. Limited Tax Bonds -- Sometimes an authority borrows funds and does not pledge all its taxing power. They are payable, for example, from a share of the state's gasoline taxes and/or motor vehicle tax.

C. Revenue Bonds -- These are secured by the revenues of a particular department of the municipality or of a special authority created to operate a project which is hoped will be self-supporting. The authority to be set up may have a multitude of purposes: water, sewers, gas, and electrical facilities, port facilities, ferry systems, bridges, and toll roads.

D. Housing Authority Bonds -- These bonds are issued by the Federal Government agency called the Public Housing Authority to finance the construction of low-rent houses all over the United States. Rents charged in these projects may not be sufficient to pay off the bonds; so the P.H.A. each year makes up any deficit with funds granted by Congress.

3. Form of Municipal Bonds

There are two forms of municipal bonds, coupon and registered. The coupon is transferrable by delivery to bearer, whereas a registered bond is registered on the books of the municipality and title can only be transferred by endorsement. Therefore, one of the advantages of a registered bond is that in case it is stolen or lost, there is a certain protection for the registered owner. On the other hand, the advantage of the coupon bond is that it is more marketable and is easier to use for collateral.

4. Quality Ratings for Municipal Bonds

As municipal bonds are of different types, they have different qualities. The quality ratings are given to municipal bond issues by two recognized independent advisory services which specialize in collecting and publishing financial information. These two services, Moody's and Standard Poor's, do not deal in securities at all. Their ratings, from the top quality down, are as follows:

Moody's)	Aaa	Aa	A	Baa	Ba	B	Caa	Ca	C
Standard & Poor's)	A1+	A1	A	B1+	B1	B	C1+	C1	C

Most investors in municipal bonds favor those issues which are rated Baa or B1+ or better.

5. Exemption of Municipal Bonds from Federal Income Taxes

The interest on municipal bonds is fully exempt from federal income taxes, both normal and sutax. Municipal bonds enjoy freedom from federal taxation under the doctrine of reciprocal immunity whereby the federal government may not tax the governmental functions of the states, nor the states the functions of the Federal Government.

The two exemptions of the Municipal securities are not written into the bonds, it is inherent in the United States Constitution as interpreted by the Supreme Court under the doctrine of reciprocal immunity.

Since they are tax free, municipal bonds are very attractive for individuals in high tax brackets. If an investor is in the 87 percent bracket (unmarried, and annual earnings from $90,000 to $100,000), a tax-free yield of four percent is equivalent to a taxable yield of 30.11 percent. Even if an investor is only in the 53 percent bracket (earnings from $18,000 to $20,000), the tax-exempt six percent is equivalent to an 8.51 percent taxable yield. It is hard to find such a return on capital elsewhere.

6. Fluctuations in Municipal Bond Prices

If an individual sells a municipal bond during its life (i.e., before maturity), he may do so at a profit or a loss, depending on the money market at the time he sells. For example, suppose that several yearsago a bond was issued with a three percent interest rate. In the meantime, the money has become harder to borrow, and therefore interest rates have increased so that they now average four percent. It stands to reason that an investor who can buy a new municipal bond that will pay him four percent is not going to buy an older bond that will only pay him three percent. To make the older three percent bond attractive to buyers in a four percent market, the bondholder has to cut its price. In other words, the older bond is offered for sale at a discount, i.e., at a price lower than its par or face value of $1,000.

On the other hand, if money has become easier during the period the individual holds the bond, he might make a profit by selling it at a premium. But if he keeps his bond until its maturity date, he can expect to collect its full face value, regardless of interest fluctuations.

7. Marketability of Municipal Bonds

There are two markets for municipal bonds: the primary market and the secondarn market. The parimary market is the market for new bonds just sold by the community and offered for the first time to the general public, by an investment banking firm or a syndicate of investment bankers. The secondary market is the market in which older issues are bought and sold before their maturity date.

Neither market is a market place in the sense of the New York Stock Exchange, for example. Almost all municipal bonds are traded in the over-the-counter market, which is a countrywide network of dealers in touch with each other by telephone or teletype. In the over-the-counter market, prices are arrived at by informal negotiation among dealers instead of an an exchange floor by the auction system.

8. Distribution of Municipal Bonds

The distribution and sale of municipal bonds to purchasers is done by municipal bond dealers or banks with bond departments. They act as underwriters or principals, purchasing bonds for their own account, and then reselling them at a higher price if possible.

One of their most important functions is to bring together the municipality that wishes to sell the bonds and the investor who has money to lend.

The difference between dealers and dealer banks is that the dealers can handle all types of municipals, whereas dealer banks can only handle general obligation bonds.

The second important class of house which handle municipals are the municipal bond brokers. They act principally as the contact between dealers and act as agents rather than as a principal.

9. Procedure of Municipalities in the Issuance and Sale of Bonds

The authority for the issuance of municipal bonds stems from the constitution of the state or a vote of its electorate. A very important feature of an issue is the maturity. The rule of sound municipal financing is that no bond should run beyond the life of the improvement.

With respect to the interest rate, the bidders may name it.

The bidders usually prefer to keep the premium down to the lowest possible figure.

It is permitted to split interest rates, i.e., to submit two or more different rates on the same issue. The reason for this is that a bid for all four percent bonds might produce a large premium, whereas a combination of four percent, $3\frac{1}{2}$ percent and 3 1/5 percent rates would produce a bid of approximately par and permit a reoffering at a small premium.

After the details of the issue have been determined, the next step for a municipality is to advertise its bonds for sale. The request for bids may be made in a local newspaper or in some trade paper, such as the Daily Bond Buyer.

It is also customary to prepare official notices of bond sales giving the description of the bonds, the amount of the issue, the maturity date(s), the interest rate, whether or not more than one interest rate can be bid, and if so, whether there is any limit to the size of the rate. There is also a financial statement released by the municipality in question. These notices are usually sent to all the bond dealers and banks that might be interested in bidding on the bonds.

10. Procedure of Bond Dealers and Banks in Purchasing Municipals

If a dealer is interested in issues from certain sections of the United States, he has to decide whether the size of the financing is such that he requires partners or whether he is going to bid alone. In the first case, he will look for partners to form an account, and the members of the account (dealers and/or banks) have to appoint a manager in charge of bidding, reoffering of the bonds and settling the account.

The account is usually set up to run for thirty days during which time the offering prices cannot be changed without the consent of the majority of the members. If, at the end of thirty days, the issue has not all been sold, the account can be renewed and extended for another period of thirty days by mutual agreement, or if the majority of partners do not wish to extend the account, the remaining bonds are divided up among the members in accordance with their prorata share.

11. Procedure After Account is Formed

After the account has been set up, a form letter is sent out to the municipal officials requesting an official notice of sale which contains an official bidding form. Then the syndicate proceeds to (1) the analyses of the municipals, (2) the decision of the scale of the price, (3) the bidding procedure, (4) and the reoffering.

(1) Analysis of Municipal Bonds

There are four general considerations in determining the credit standing of municipals, especially general obligations:

a. The economic background.
b. The administrative and legal factors
c. The debt structure
d. The current operating procedure and record.

a. The Economic Background

Under this heading are considered such terms as the growth of industry and population, the occupation of the people who inhabit the community, the source from which they obtain income to pay local taxes, etc. The air here is to gauge the community's ability to pay its obligations.

A good credit risk will have, among other things, adequate transportation facilities giving its access to raw materials needed by its industries and to markets for its finished products. It will have also a diversification of industry within itself or its surrounding areas.

Diversification does not necessarily mean that a community must have a large number of industrial plants manufacturing a broad range of products. Diversification may also mean various activities sudh as banking and finance, commerce, wholesale and retail distribution, recreational facilities, etc.

A high-grade credit risk will also have a record of steady rather than spasmadic growth. The general level of wealth of its inhabitants is experssed in home ownership, salaries, income tax payments, high percentage of skilled workers, etc.

b. Administrative and Legal Factors

This heading relates to the type of government, the legal restrictions upon the issuance of bonds and the levying of taxes, the political history of the community and the elusive but vital factor of willingness to pay its debt.

c. Indebtedness

A high-grade credit naturally will have a moderate debt. Ordinarily the analyst relates a community's debt to that of other similar communitie He also attempts to determine how heavy the debt is in relation to the issuer's wealth by determining the ratio between the net tax-supported overall debt and the assessed valuation. The assessed valuation is the aggregate of the assessments of the various pieces of property in the community for determination of the levying of the annual tax. The net tax-supported debt of the city represents the gross debt of the issuer less the water debt and other debts deriving from the municipally owned utilities, and the sinking funds which have been accumulated for the payment of debts.

To the debt of the city must be added a proportion of the debt incurred by overlapping governmental units because such debt is an obligation of the inhabitants of the city. If, for example, a city includes one-half of the assessed valuation of the county in which it is situated, the property owners within the city are liable for one-half of the county debt.

The rule of thumb is that if a community's overall debt does not exceed ten percent of the assessed valuation, the debt is assumed to be of reasonable size.

Other items to be considered are the rates of retirement of the outstanding debt and whether the retirement schedule might be considered likely to pose a problem in the community's annual budgets.

d. Current Operating Record

In municipal finance the analyst is confronted with the fact that there is no uniformity in municipal accounting either in procedures or in terminology.

The factors of weakness that occur in operating accounts are such items as widely fluctuating tax collections, the accumulation of operating deficits and their carryover from one year to the next or their funding into long-term bonds.

(2) Meeting of the Account Member to Decide on the Scale of Price

A few days before the sale, it is necessary to decide on the offering prices at which the bonds will be offered to the public. The account manager calls a meeting, usually the day before the sale, and each member attends with his idea as to the prices at which the bond should sell. These may be very close together on may cover a very wide range, in which a considerable discussion is necessary. If the scale which is finally agreed to is higher than some of the members are willing to go, they have the right to drop out of the account and thier share is usually divided among the other members.

Mathematical Procedures

After the scale has been decided upon, it is necessary to convert the scale into dollar prices, to determine the average selling price of the issue and to arrive thereby at a bid price.

The table below permits to compute the average selling price of an offering scale and bid price:

Dated: May 1, 1959 Due May 1, 1960-70

Amount	Due	Yield	Price	
$ 50,000	1960	.60%	101.10	
50,000	1961	.50	101.99	
50,000	1962	.60	102.67	305.76 x 50 = 15,288.00
60,000	1963	.65	103.35	
60,000	1964	.70	103.92	
60,000	1965	.75	104.39	
60,000	1966	.80	104.76	416.42 x 60 = 24,985.20
75,000	1967	.85	105.02	
75,000	1968	.90	105.18	
75,000	1969	.95	105.23	315.43 x 75 = 23,657.25
100,000	1970	.95	105.73	105.73 x 100 = 10,573.00
				74,503.45

74,503.45 divided by 715 = 104.20 Average selling price
minus .92 Spread
103.28 Bid

The table consists of an offering scale for a hypothetical issue of $715,000, one and one-half percent bonds dated May 1, 1959 and due serially May 1, 1960 to 1970. In this case the dollar price for each maturity has been computed, and the average selling price has been computed therefrom.

(3) Bidding Procedure

After the price has been set, the next step is to submit the bid to the municipality. This may be done in any one of several ways. Sometimes the bid is mailed. However, it is infrequently done now, because most dealers do not like to have a bid standing overnight. Usually on important sales, the bidder will either send one of his own men as a representative to attend the sale or will arrange to have a local dealer or a local banker submit the bid for him. In both cases, the bidder gives the banker or his representative the bid over the telephone. This is filled in on the bidding blank and then submitted to the municipality at the last moment.

The municipality usually requires from each bidder a good-faith check ranging in amount from one to five percent of the par value of the bond being sold.

Speaking generally, the bid showing the lowest net interest cost to the issuer usually is accepted. When the sale is over, the unsuccessful bidder's good faith checks are returned to them and the successful bidder's check is retained by the municipality until the contract is completed.

Legal Opinions

It is customary in bidding municipal bonds for dealers to require from the municipality the form of opinion delivered by a bond attorney. This form states that the bonds are legally and regularly issued. This practice grew out of the wide-spread defaults which occurred in the late nineteenth century.

Method of Payment

When the bonds are ready for delivery, the dealer bank puts up the money for the group.

Bonds are sold plus accrued interest, either from the date of the issue which is usually the case of a new issue, or from the last interest paying date if one has passed. The reason for the payment of accrued interest is obvious. The purchaser is only entitled to interest from the time he makes payment and the previous owner is entitled to it up to the time he receives payment.

Occasionally bonds are sold flat, which means that there is no accrued interest paid.

(4) Reoffering

For the bidder who purchases the bonds, the next step is to reoffer them. The bonds are offered at basis prices with few exceptions. Sometimes the longer maturities may be offered at a dollar price. From the offering prices there is allowed to other dealers what is known as the dealer's concession. In other words, if the syndicate is offering a new issue of municipals and some dealer who is not in the syndicate wants to buy them, he will take them at the offering price less the concession, and then sell them to his customer at the offering price, his profit being the amount of the concession.

In addition to the concession, the members of the syndicate take the bonds at the offering prices less what is called the take-down. This is generally more than the dealer's concession.

The net profit over the take-down goes into the account and is divided among the members at the terminationof the account.

III. Corporate Finance Advisoty Sergice

This group is available to assist the Bank's loaning offbcers and their customers with problems in the general area of corporate finance that does not fall into the customary pattern of bank lending. In many ways, the group's activities are similar to the investment banking field (but on a consulting basis) and are helpful to customers who do not have a strong banking connection.

Most of the problems referred to the group fall into the following general categories:

a. Analysis of a customer's capital requirements, and recommendations as to the form of any financing that may be involved. The latter includes such problems as debt or equity, public or private financing, and often the quëstions raised relate to terms loans which may involve the bank participation.

b. Problems involving refinancing, corporate reorganization, mergers and acquisitions being about another activity of the group, that of its "Business Clearing House." In accordance with the bank polity, the Business Clearning House has operated on a referral basis, with no attempt to seek out companies on one side or the other.

c. Valuation studies, to determine the economic value of a business enterprise, or of securities of a corporation.

d. Studies relating to less well-known or new financing mediums such as sale-leaseback, equipment leasing, natural resources production payments.

e. Analysis of particular companies or industries, usually to determine any change in their long-term credit standing.

Bond Cage Department

The Bond Cage is the operating arm of the Bond Administration. Its duties are as follows;

1. Processing purchases and sales of securities made by the Bank for Investment Account, Dealer Account, Syndicate Account and occasionally for account of customers.

2. Receiving and delivering securities.

3. Effecting and receiving payments for securities

4. Bending securities

5. Pledging securities

6. Processing subscription to U. S. Government offerings, including weekly issues of treasury bills, for the bank's and customers' accounts.

7. Maintaining records and making reports of those various operations

The Bond Cage is divided into four sections: Delivery, Syndicate, Special Services and Accounting.

I. Delivery Section

Contract -- All transactions are authorized by a pre-numbered purchase or sale contract and approved by two seniors officers. The Bond Administration provides the Bond Cage with a contract for each purchase or sale transaction. This contract gives the name of the party with whom the trade is made, date of trade, amount and description of securities, price or yield, method of payment, delivering instructions.....

Operating tickets -- Number-controlled operating tickets are typed from the data contained in the contract. They form the basis for confirmation, security movements, receipt and payments, and accounting records.

Confirmation -- The City Bank confirms all trades except those with dealers in New York City and discloses whether it is acting as principal or agent. Generally, the bank receives confirmation from all those with whom it has made trade, including dealers in New York City. These confirmations are checked against the proper operating tickets.

Deliveries -- Incoming deliveries are received over the counter, through the Stock Clearing Corporation, and from the Incoming Registered Mail Dept. They are counted and examined for contract and ticket conformity. After entry in the vault blotter, the securities are forwarded to the Bond Vault.

Outgoing deliveries, previously requisitioned from the Bond Vault, are similarly counted and examined, before delivery by armed messengers, armored trucks, or Outgoing Registered Mail Department. Out-of-town deliveries in excess of $500,000 are reported to the Insurance Department before shipment.

Unless otherwise specified, United States government obligations are deliverable on the next business day after the date of trade. All other securities are deliverable on the fourth business day after the date of trade.

Payments -- Payment for incoming deliveries is made by cashiers' checks, departmental credit, credit to an account or credit to Stock Clearing Corporation.

Report -- A report of the bank's U. S. Government holdings is made daily to the Bond Administration. This report, broken down by maturity classification, includes par value, amortized cost, market value, and appreciation or depreciation.

The Bond Cage maintains a complete file on all issues held.

II. Syndicate Section

This section processes and handles all issues of State and Municipal general obligation bonds purchased by a group of bond dealers, of which the Bank is the manager.

Formation -- The formation of each account, the allocation of member's participation, submission of the bid and authority to the Bond Cage to make the good faith deposit are initiated by the Bond Administration. There are two types of accounts: The Bond Syndicate Account is formed to bid on and market an original issue of bonds. A joint account is formed to handle a secondary offering of bonds. All transactions are authorized by the Bond Administration, either by contract or memoranda.

Take Down -- If the group's bid is successful, the members of the account contact the Bond Administration and specify the amount and maturity of the bonds they desire. The Bond Administration confirms by letter all take down, and forwards a copy to the Cage together with a contract covering the total amount. The take down are given to the Cage in three divisions: members, group sales, and designated sales (for dealers).

Delivery by Issuer -- In the offering of sale, the issuer specifies the place of delivery. Delivery in New York is usually made at the Signature Company. If out-of-town, the Cage makes arrangements with a local bank to act in the bank's behalf. Each new issue must be examined in detail as to signature, coupons and seal. The Cage should require a signature and no-litigation certificate, treasurer's receipt and a signed approving legal opinion. When examination of the bonds and relative papersis completed and found in order, payment is then made to the issuer. The ticketing and security handling follow the pattern of the Delivery Section.

Delivery to Members -- After payment has been made to the issuer, a detailed confirmation is forwarded to each member of their take-down by maturity, delivery date, and amount of payment due from them. Similar confirmations are forwarded to all the group and designated sales. The bonds are then blocked out, numbered and packaged. On delivery date, each member must arrange to pick up his bond against payment. The ticketing and security handling are the same as in the Delivery Section.

Settlement of Account -- After all the bonds have been sold and delivered, designated sale concession distributed, and all expenses in connection with the account have been settled, the account is then closed. A statement is prepared detailing the distribution to each member of the profit, or the amount due to the manager if the account ended in a loss. The Bond Administration distributed the checks or bills as the case may be.

III. Special Services

Lending Securities -- The City Bank lends securities from its portfolio, mostly United States government issues, to approved dealers and dealer banks for the purpose of enabling them to fulfill delivery commitments. These loans are for short periods, not in excess of three weeks, and are secured by cash. Loans are made on a par basis while margins are calculated on market value.

The bank's commission charge is one half per cent per annum. Each loan is generated by a letter agreement outlining the loan terms, including the right of recall without prior notice.

The ticketing and security handling follow the same pattern as in the Delivery Section.

A daily report of outstanding loans, by dealers, and issues, is made to the Bond Administration and the district.

Pledging Securities -- Dollar deposits of the U.S. Government and its agencies, and certain deposits of States and Municipalities and other governmental bodies, are required by statute to be secured. Securities are also required for trust deposits with the city bank.

The bank is also required to pledge collateral to secure borrowings from the Federal Reserve Bank, and for loans of federal funds made to the bank by correspondent banks with temporary excess reserves.

For all of the Bank's pledge, it uses U. S. Government securities, most of which are in coupon form.

Pledged securities are deposited with the escrow agent specified in the pledge agreement. These escrow agents include the Federal Reserve Bank, the City Bank Corporate Trust Department.....

Since deposits fluctuate, it is necessary to follow them closely at all times to see that they are adequately secured. When an account is closed or balances decline, steps are taken to close out or reduce the bank's pledge.

The ticketing and handling of securities follow the pattern of the Delivery Section.

Cash and Exchange Subscriptions

From time to time, the Treasury Department invites subscription for various issues of U. S. obligations. The issues and terms of the offering including the good faith deposit required, are fully detailed in a consolidated circular of the Treasury Department and its fiscal agent, the Federal Reserve Bank. These offerings can be either on a "cash basis" or an "exchange basis."

Commercial banks may submit subscriptions to cash offerings for their own account. These subscriptions are usually restricted to a percentage of their combined capital, surplus and undivided profits and no good faith deposit is required. Subscriptions for the account of customers must be accompanied by a specified good faith deposit, not subject to withdrawal until after allotment. The securities allotted are delivered to the City Bank or the Federal Reserve Bank. Qualified depositors are permitted to make payment by credit to Treasury Tax and loan account. Reimbursement by customers is obtained in the same manner as Treasury bills.

The amount of the Bank's subscription or customer's subscription is authorized by memoranda from the Bond Administration.

All subscriptions for the customers are confirmed by the Bank. Later the customers are notified of their allotmentsand the amount of payment due.

The ticketing and security delivery follow the same procedure as in the Delivery Section.

Exchange subscriptions are somewhat similar except that no payment is involved. The securities for exchange are surrendered with the subscription to the new issue(s).

Treasury Bills -- Weekly, the treasury department invites tenders, on a discount basis, for their 90/92 day treasury bills. These tenders can be either on a competitive or non-competitive basis, the latter being restricted to an amount not to exceed $200,000. No good faith deposit is required. Subscription for the bank's account and for account of customers are usually entered on Monday and the next business day the Bank is notified by the Federal Reserve Bank of the amount and basis of award. Non-competitive tenders are accepted in full at the average price of accepted competitive bids. Customers are notified of the allotment and of the amount of payment due. The bills are delivered to the Bank at the Federal Reserve Bank, usually on Thursday against payment by charge to the Bank's Lawful Reserve Account. Reimbursement is obtained by the Bank for customers' allotments, and by charge to its Bond Account for its own allotment.

All subscriptions are channeled to the Bond Cage by the Bond Administration, and the competitive bid price is specified by letter, unless a customer fixes his own price.

The ticketing and security delivery follow the procedure of the Delivery Section.

IV. Accounting Section

This section keeps records of all the transactions performed by the Bond Cage Department. Here are the most usual accounting entries:

Customer's Purchase from Dealer through the Bank

Debit		Credit	
Customer's Account	$10,000	Cashier's Check or XYZ Dealer's Account	$10,000

Customer's Purchase from Portfolio

Debit		Credit	
Customer's Account	$10,000	Bond Account	$ 9,900
		Interest Account	50
		Bond Profits	50

THE NEW YORK STOCK EXCHANGE

The New York Stock Exchange is a market place for securities.

It is not like the conventional auction where only buyers compete and there is one seller. On the Exchange there is a two-way auction market: bidders compete with each other to purchase at the lowest possible price the shares they want to own. Simultaneously, those seeking to sell compete with each other to get the highest price for the shares they are offering. The buyer bidding the highest price and the seller offering the lowest price agree on a figure which is acceptable to each and the transaction is made.

The Exchange is a market place where prices reflect the basic law of supply and demand. It is a market place where shares in American industry can be readily bought and sold, no matter how far the buyer and seller live. The mechanics of transmitting their order to the Exchange and the machinery for executing the order are the same in either case. The seller does not have to search for a buyer and does not have to advertise.

Let us examine the organization and functioning of the New York Stock Exchange.

I. Organization of the New York Stock Exchange

The New York Stock Exchange is a voluntary association of 1,366 brokers and dealers in securities.

A. Members of the New York Stock Exchange

There are four categories of members:

1. Commission House Brokers are Exchange members affiliated with member organizations doing a securities business with the public. They execute customer's orders to buy and sell on the Exchange and receive the commissions on those transactions.

2. $2 Brokers execute orders for other members who may be absent from the floor or who may be very busy.

3. Odd-Lot Dealers serve investors who purchase or sell a few shares at a time, rather than in the conventional 100-share unit, known as round lot. The odd-lot member acts as a dealer, not as a broker, i.e., he buys and sells stocks for his own account.

4. Specialists, so called because they specialize in dealing in a few particular stocks.

The main function of a specialist is to maintain a fair and orderly market of the stocks in which he specializes. The specialist must often risk his own capital by buying at a higher price or offering at a lower price than the public may be to pay or accept at that moment. For instance, the last sale in XYZ stock was at $35 a share; the lowest offer to sell is $35 a share and the best bid to buy is at $34. Depending on conditions in the market, the specialist might bid $34½ in order to narrow the temporary spread between supply and demand. In a rising market the specialist frequently sells stocks from his own account at a lower price than that at which the public will sell. In so doing, he stabilizes the price fluctuating.

The Exchange set specific requirements for specialists regarding market experience, their dealer functions, and the amount of capital they must have.

As a specialist, his business is concentrated on a particular group of stocks at one trading post. Thus he can also act for other brokers who cannot remain at one post until prices specified by their customers are reached. He mjst subordinate his personal interest in the market to the public. The specialist, cannot buy or sell at any price for his own account until he has executed all public orders held by him at that price.

B. Board of Governors

The rules and regulations governing the conduct of members are set by the Board of Governors, which is elected by the members. The Board exercises policy making and disciplinary powers. Departments include the following:

1. Department of Stock List which examines corporations' listing applications preliminary to final Board consideration.

2. Department of Member Firms which administers rules and policies concerning members' conduct and financial stability.

3. Department of Public Relations and Market Development which explains the Stock Exchange's functions to the public and assists member organizations in their relations with investors.

4. Department of Research and Statistics

5. Department of Floor Procedure which administers rules regulating trade on the Exchange.

In addition there are:

- The Office of the Secretary which processes applications for membership.
- The Stock Clearning Corporation which expedites the receipt and delivery of securities following transactions on the trading floor.
- The Quotation Company which operates the stock and bond ticker systems.
- The Building Company which operates the Exchange's real property.

The Exchange is an unusual form of enterprise. It has nearly 1,300 employees. It does not try to make a profit (because it does not own any stock) and does not sell any, and it is not a charitable organization. It is a voluntary association of brokers.

C. Local and Foreign Offices

Linked with the Exchange is practically every city in the United States. If a community cannot afford an office of a Stock Exchange, member firms have access to the facilities of the Exchange through the local bank.

There are also member firms offices in Argentina, Germany, Hawaii, Panama, Puerto Rico, Canada, Cuba, England, France, Holland, Monaco, Switzerland, and Venezuela.

D. The Securities and Exchange Commission

The SEC have the duty of administering the 1934 Act which makes compulsory:

- Adequate disclosure of information about a listed security.
- Registration with the SEC of all securities listed on national securities exchanges.

There are about 1,200 listed stockes traded at the New York Stock Exchange. The Act also bans all manipulative operations such as pools, misleading statements, raising or depressing the price for the purpose of inducing the purchase or sale of securities by others.

In addition, the SEC requires officers, directors and principal stockholders of companies with securities listed on an exchange to report any transaction by them in the stock of their company. These reports are made public by the SEC.

E. The Federal Reserve Board

The Federal Reserve Board regulates the use of credit in the securities market. It regulates the flow of credit in the banking system. Brokers may borrow only from a source approved by the Federal Reserve Board which also determines how much credit a broker may extend to a customer to purchase listed securities.

Anyone purchasing a listed stock can pay the full amount involved, thereby buying outright; or he can make partial payment and borrow the balance from his broker, thus buying on margin. At present, the margin rate set by the Federal Reserve Board is 90 percent

II. Description of the New York Stock Exchange

The New York Stock Exchange is located in a big building at the corner of Wall and Broad streets in Manhattan. The trading room has a high ceiling and a trading floor about half the size of a football field.

All around the edge of the trading floor are telephone booths where clerks representing various brokers work. There are telephones connecting them with their home office. These phones are the basic instruments of the securities business, for it is through them that all the public orders to sell or buy stocks come to the floor of the Exchange.

Spaced at regular intervals on the trading floor are eighteen trading posts. Each trading post or station is a horse-shoe-shaped counter, inside of which there is room for a dozen clerks and for several employees of the Exchange.

All buying and selling is done around the outside of the trading post. About 75 different stocks are bought and sold at each post. Little placards on the counter show the names of the stocks at a particular position, and below each placard is a price indicator showing the last price at which a transaction in that stock took place and whether this price represented an increase or decrease from the last transaction - a plus sign if it represented an increase, a minus sign for a decrease.

III. Functioning of the New York Stock Exchange

First, it must be borne in mind that the Stock Exchange itself neither buys, sells, nor sets prices of stocks. The Exchange provides the market place for individual buyers and sellers.

Regulations for trading on the floor of the Exchange stress the importance of the open market, ie. secret deals are impossible.

All transactions reflect the basic law of supply and demand, i.e., the highest bid and the lowest offer have precedence. Bids and offers must be called aloud. Transactions are promptly reported over the Stock Exchange's nationwide system. No trades are allowed on the Exchange floor before or after trading hours.

To show how the Stock Exchange works, let us take an example. Suppose that Dr. John Jones of Maine has sold his summer cottage. After consultation with a Stock Exchange member firm, he decides to buy common shares in U.S. Steel Corporation. He asks the member firm's representative to find out for him what Steel shares are selling for on the Exchange.

Over a wire to his New York office the representative asks for a "quote" on U.S. Steel. A clerk in the firm's New York office dials the quotation department at the Exchange to obtain the current quotation on U.S. Steel. Current quotations on all listed securities are received by the quotation department over direct wires from each trading post on the floor.

The clerk in the New York office immediately relays the information to Maine that U. S. Steel common is quoted "65 to a quarter." This means that, at the moment, the highest bid to buy steel common stock is $65 a share and the lowest offer to sell is $65.25 a share.

Order Enters the Market

Dr. Jones tells the representative to go ahead. The latter writes out an order to buy 100 shares of U. S. Steel "at the market" and has it wired to his New York office where it is phoned to his firm's partner on the floor of the Exchange. "At the market" means at the best price possible at that time. The floor partner hurries over to the trading post where U.S. Steel shares are traded.

About the same time, a San Francisco tailor, Robert Smith, decides to sell his 100 shares of U.S. Steel to get funds to enlarge hisstore. He calls his broker, gets a "quote," tells his broker to sell. That order is also relayed to the floor by a direct wire. Smith's broker hurries to the steel post. Just as he entersthe steel "crowd," he hears Jones's broker calling out,"How's Steel?" The specialist answers, "65 to a quarter."

Every broker is charged with the responsibility of getting the best possible price for hiscustomer. He must exercise his experience, knowledge and brokerage skill.

Jones' broker says to himself, "I can't buy my 100 at 65. Someone has already bid at 65 and no one sells at that price. I'd better bid 65 1/8." (1/8 of a point is the minimum fluctuation in the price of most stocks.)

Smith's broker thinks, "Looks like I can't sell my 100 at 65¼, someone has already tried to get that price. I'd better try to get 65 1/8."

So, when Smith's broker hears Jones' broker bid 65 1/8, instantly he shouts, "sold, 100 at 65 1/8." They have agreed on a price and the transaction takes place.

The two brokers complete their verbal agreement by noting each other's firm name and reporting the transaction back to their phone clerks so that their customers can be notified.

In the meantime, an Exchange employee has sent a record of the transaction to the ticker department for transmission over the ticker network. The report appears like this: X 65 1/8 - X being the ticker symbol of U. S. Steel.

If 200 shares instead of 100 shares has changed hands, the transaction would be noted this way:

X 2 S   65 1/8

If 1000 shares have been involved, it would appear on the tape:

X 1000 S   65 1/8

The number of shares in a round lot transaction is specified only when more than 100 shares are traded. To keep traders abreast of the market action, the Exchange reports to flash printing, and at half minute intervals it flashes the latest prices of 30 key stocks representing a variety of industries on the tape.

Thus within a few minutes Dr. Jones has arranged to exchange the proceeds from the sale of his summer cottage for 100 shares in the world's largest steel company. Smith has sold his shares in that company for money to expand his own business.

Other Types of Orders

1. A Limit Order specifies a price to buy or to sell a stock.

2. GTC Order - If the customer wants his order to hold good indefinitely, he gives his broker a good-till-cancelled order.

3. Stop Orders or Stop-Loss Order are designed to limit losses and protect profits. To illustrate: if a person bought stock at $35 a share, he could enter an order to sell at "30 stop." In the event the stock declines to $30, his order automatically becomes a market order and is executed at the best price possible.

   Or, if stock bought at $35 a share should rise at $55, for example, the customer could give a stop order to sell at $50.

Less than 100 Shares

The 100-share unit is known as a round lot. From 1 share to 99 shares are an odd lot which are bought and sold by the odd-lot broker.

The fee paid to the odd-lot broker is higher than that of paid to the round-lot broker.

Short Selling

Short selling in the securities market is the selling shares that a person does not own and he has to borrow the same number of shares in order to make delivery to the purchaser. When he buys the stock later to return to the lender, he hopes to do so at a lower price, thus making a profit. Short selling may not be used as a device to depress security prices artificially and there are rigid rules to enfore this prohibition. No short sale of a stock is permitted except on a rising price. For instance, there might be six transactions in a given stock at a price of \$45 a share, but no stock could be sold at \$45 unless the price before the six transactions at \$45 has been \$44 7/8 or less. Essentially, short selling is a normal business transaction, just as a farmer sells his crop before harvest time.

The Dow Jones Industrial Average

Basically, stock prices obey the law of supply and demand. When most people want to buy, the general market will rise. When most people want to sell, the market will decline. Individual stocks, of course, may move independently, reflecting development peculiar to a company or an industry. When it is reported that the market advanced or declined, it usually means that one of the market averages has gone up or down. Most of the popular averages are based on a limited number of issues, for instance, the well-known Don Jones Industrial Average based on only 30 stocks. (There are about 1,200 listed stocks at the NSE.) Actually, average may be misleading.

The Dow Jones Industrial Average is compiled by adding the prices of 30 stocks. This total is divided by a divisor which is intended to compensate for past stock splits and stock dividends. In other word, the total is not divided by 30. An average might decline, say, 6 points with no individual issue in the average declining more than \$2 a share. The main value of an average is gauging the course of the market over a period of time rather than as a measure of daily fluctuations.

Matched and Lost

One of the rules governing trading on the floor is that where there is more than one bid at the same price, and it is not possible to determine the order in which such bids were made, the brokers "match" coins to determine who shall participate in the transaction. For example, three brokers all bid for stock at \$50 a share at the same time, two of them bidding for 200 shares each and the third bidding for only 100 shares. Then another broker with a sell order decides to sell 200 shares at \$50. The two brokers bidding for 200 shares each would "match" to see which one makes the purchase. The third broker bidding at \$50 would not be entitled to "match" because his bid is not so large as the amount offered.

If the customer for whom the losing broker was acting asked enquiry, he would receive the message "matched and lost" from the floor.

Most "match" situations occur as a result of a basic auction market rule which provides that every sale "clears the floor" and starts a new auction. For example, a broker enters a crowd with the market 49 7/8 - 50¼ and bids 50 for 100 shares. A few minutes later another member enters the crowd and bids 50 for 100 shares. Another broker comes in five minutes later and makes an identical bid. Any willing seller at 50 would sell to the broker making the first bid at 50. However, if another member enters the crowd and bids 50 1/8 for 100 shares, he can buythis stock at that price. This transaction at 50 1/8 clears the floor and places the three brokers bidding at 50 on parity so that they will have to "match" against one another in the event that 100 shares of stock come into the market to sell at 50.

Monthly Investment Plan

Until 1954, the smallest amount of stock that anyone could buy was one share. In that year, however, member firms of the New York Stock Exchange created the Monthly Investment Plan (M.I.P.), under which it is possible to buy a fractional share of stock. It was designed to permit people to invest a sum of money every month or every quarter and to acquire full or fractional shares of any stocks listed on the New York Stock Exchange.

By this method of systemat investing, a person would not have to wait till he had acquired several hundred dollars, emough to buy five or ten shares of some stock. The M.I.P. plan is geared to the tempo of life today, since most American families are used to settlaing their bills on a monthly budget basis.

Under this plan, the buyer signs a contract with a regular broker, a member firm of the Exchange, thereby he agrees to accumulate shares of a particular stock listed on the Exchange and to invest a regular sum of money every month or every quarter toward the purchase of that stock. M.I.P. contracts may be cancelled by the buyer at any time, and the buyer can skip payments without any penalty.

Commission Rates

Here is the basic schedule of rates made effective June 1959:

On a purchase or sale amounting to $100.00 or less, as mutually agreed, usually six percent.

On a purchase of sale between $100.01 and $399.99: 2 percent plus $3.

On a purchase or sale between $400.00 and $2,399.99: one percent plus $7.

On a purchase or sale between $2,400.00 and $4,999.99: One-half percent plus $19

On a purchase or sale between $5,000 or more: 1/10 percent plus $39.

These rates apply on the purchase or sale of 100 shares of a given stock.

Stock Clearing Corporation

All settlements between member firms are arranged through the Stock Clearing Corporation, so that a minimum of cash and securities are exchanged. Thus, a firm may have sold 1,100 shares of General Electric for its customers on a given day and bought only 1,000. To settle its accounts, in that stock on that day, the firm would have to send only 100 shares to the clearing corporation. The delivery of the other 1,000 shares from its customers who sold that stock to the buyers is purely an internal bookkeeping procedure. Dollar balances, the net amounts owed and the net amounts due, are handled in the same way.

The New York Stock Exchange is a wonderful institution where people can acquire democratic ownership. Many people think the Exchange as a casino for the rich. In fact, the Exchange is accessible to every person even to those with low incomes as the M.I.P. indicated. At the main entrance of the New York Stock Exchange the following legend reads, "Here is where people buy and sell ownerships in America's leading corporations."

The New York Stock Exchange is a place through which most of the industrial enterprises can obtain new equity capital by selling their new issues. If there were no Stock Exchange, capital would soon become sluggish and the financing of new ventures, no matter how promising, would be heavily curtailed. Today, when we flip the switch which turns on the electric light in the United States, we are commanding machinery which cost millions of dollars, and this machinery is financed and owned by thousands of shareowners.

The stocks provide an efficient hedge against inflation for those who invest in them. Past experience has always indicated that the stock market is going up, over a long period of time, of course. Prices of food and clothing and almost everything in the country - including stocks - have steadily gone up and the purchasing power of the dollar has gone down.

THE TORONTO STOCK EXCHANGE
(My field trip in Toronto, Canada from July 6-9, 1959)

The Toronto Stock Exchange boasts the best mechanical facilities of any Exchange in the world, facilities that enable it to enable a volume exceeding 12,000,000 shares a day without undue strain.

In the main, stocks are traded on the Toronto Stock Exchange very much as they are in the New York Stock Exchange and American Stock Exchange, but there are several significant differences.

1. Floor trading is not restricted exclusively to members brokers. Thus, on the Toronto Stock Exchange, every member is permitted to appoint as many as five "attorneys" to execute orders for him. Such attorneys must be approved by the Exchange as qualified for their jobs.

2. There is no formal system of specialists who make markets in various stocks by buying or selling them for their own account such as there is on the New York Stock Exchange.

3. There are also significant differences in the units of trading. Thus, on the Toronto Exchange, oil and mining stocks selling at less than $1 a share are called "penny stocks" -- and are traded in units of 500 shares, and if the price is $1 or more, the trading unit is 100 shares. On industrial stocks, different units of trading are employed. On such stocks selling at less than $25 a share, the unit is 100 shares; between $25 and $100, it is 10 shares. All of these different units are known as broad lots rather than round lots.

4. Odd lots can also be bought or sold on Canadian Exchanges, but they are not handled by special odd-lot brokers as they are on the New York Stock Exchange, and the price of an odd lot is not automatically determined by the price that prevails on the next broad-lot trade. Each odd-lot order is subject to separate bargaining between two or more brokers on the floor.

5. Canada does not have a national agency like the American Security and Exchange Commission to police and regulate the securities business, but every province has its own securities commission.

Many of the common stocks listed on the Toronto Exchange are on a dividend paying basis, the average return on them is generally a little lower than it is for those listed on the New York Stock Exchange. But the typical buyer of Canadian stocks is not so interested in dividends. He buys common stocks because he wants to share in the dynamic growth of the country and its industry, and he expects his shares to pay him a handsome profit over the years ahead as a result of an increase in price.

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