

FOR THE SMALL INVESTOR

By INVESTICUS

"TWO Thousand Dollars to Invest." A letter addressed to the editor of this department bears this signature and asks for information as to the difference between a bond and a stock—from the investor's point of view. The letter, which for space reasons cannot be printed in full, tells an interesting story of how one woman—an employee of a telephone company in Canada—has been able to save two thousand dollars by sheer self-denial and determination. All of the two thousand dollars was set aside apparently out of earnings that at one time were less than ten dollars a week, but that rose, in due course, to the dizzy heights of fifteen dollars a week. Up until the present this money has been kept in the savings bank earning three per cent. At least it was safe there. But it could have been earning almost double that rate of interest with absolute safety. Apparently "Two Thousand Dollars to Invest" has waked up to this fact. She now asks the difference between a stock and a bond, and she wants to know which she should buy. On that point we are writing her privately.

There are some bonds that are infinitely worse security than some stocks. But speaking generally, and having in mind the better known classes both of stocks and bonds, the Bond is always a SAFER security than a stock. Suppose that John Jones starts a grist mill in such-and-such a village. Assume that he needs to raise capital and that you are one of the people from whom he intends to raise it. Having incorporated his company there are two ways in which he may ask you to invest in it. He may sell you stock or he may sell you bonds. (I am assuming for the purpose of this article that his company is one which has the power to issue bonds). Now if you buy stock from John Jones you are becoming a partner of his. That is to say, you buy a "share" in his business. If his business makes a profit you take your "share" of the profit. If it makes no profit, you have no redress except to sit tight and hope for better times, or perhaps bring about some change in the management or in the methods of management through the shareholders' meeting, or by bringing pressure to bear on the directors. If however, in spite of changes in the management or its methods the business continues to lose and finally collapses YOU as a shareholder are now in the same position as a bankrupt store-keeper. The creditors of the business have now a right to step in and sell all the assets. If there are enough assets to satisfy the claims of the creditors, well and good. If there are more than enough, then you and the other shareholders may have the balance distributed among you—so many cents on the dollar. But if the assets are NOT enough to satisfy the claims of the creditors, and if the limitation of liability provided by the law in the charter of the company does not happen to protect you, then you not only lose what you have invested in the company but you may even have to dig down into your purse to help satisfy the claims of the unappeased creditors.

THAT represents the extreme form of disaster that may overtake the investor in a stock company, and it is only fair to say that it happens only once in a very long time, such as when a bank fails and its shareholders are called on to put up TWICE the amount of their original

investment in the shares of the company, if necessary. But this represents the possibilities of stock investment and such extreme cases may well be borne in mind when some glib young man with a beautifully printed prospectus comes to your door to peddle stock.

But now let us assume that John Jones, who started the grist milling company, proposes to raise capital in another way. Perhaps he says to himself: "I don't want anybody to share in the possible big profits I am going to make. I will own all the shares myself (or there'll just be so many of us hold the stock between us), and we'll issue bonds." Now a Bond is in theory a mortgage, only that instead of covering all the property of the company in one mortgage it is, so to speak, subdivided into a great many little mortgages—as many as there are bonds issued. For instance, one way of doing the thing is this: John Jones may go to a trust company in his nearest city and place in their hands a real mortgage against certain of the assets of the milling company. The trust company holds that mortgage in trust and issues the bonds against it. In other words, the mortgage is security for the bonds. If the milling company fails or is getting into difficulties the owners of the bonds may call a meeting and choose a representative and this representative may take steps to secure absolute control of the milling concern and its assets. He may either sell these assets, under the mortgage held by the trust company, or he may appoint some one to operate the mills for the bondholders. The point, however, which I wish to make clear is this: that the bond holder is a creditor of the company and a preferred creditor at that. The stockholder is in the reverse position. The Bond holder is in this position, that he must have his demands satisfied even at the cost of the shareholders of the company. A share is a liability. A bond is a preferred claim on assets. A share is a share either in the prosperity or the troubles of the company. A bond is merely a claim against the company.

Of course there are all kinds of bonds. Some may have a prior claim, or may rate in a certain order of preference. All of these points should be carefully looked into by anyone who is thinking of buying a bond.

Of course there is, too, this big difference. A bond, if it is a good one, pays its interest as regularly as the clock, and the interest is always the same amount. For steadiness in amount and for regularity of income the bond is likely to be much more satisfactory than any stock. The directorate of a perfectly sound company may decide to pay no dividend on such-and-such a date, or it may reduce the rate of the dividend. This may not embarrass wealthy persons, but to the small investor it is usually of great importance.

The Moral Value of Saving

DON'T imagine for one moment that the only reason why one should save money is the fact that one may need these savings for a "rainy day." Saving money is a MORAL exercise. It requires discipline and self-denial.

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