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REVIEW

The Economic Background to Investment

by

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[Pp. xi+661. Cambridge University Press, 1960. Price, 40s.]

The author of this book was for ten years until 1958 head of the Economic Intelligence Department of a large British insurance company and since then he has been Director of Studies in the Course in Industrial Financing at the London School of Economics and Political Science. He therefore brings to the task of writing this text-book both theoretical and practical knowledge.

The book was commissioned by the Institute and Faculty and covers a very wide area which means that, despite the lucid style in which it is written, a student will find its sheer size intimidating unless the Syllabus advises him to be selective in his reading.

It is in many respects a very good book and in some 650 pages it ranges over a very wide field. The field, however, is not so wide as the title suggests: it in fact covers the economic background to investment in Stock Exchange investment in Great Britain and has little to say on other forms of investment in Great Britain, or on investment in other countries.

Part I serves as a general economic introduction to the subject and approaches the matter in a way which a student should find helpful. I find myself surprised at the top of page 37 at being told that a rate of profit of 10% per annum is earned in the example given. I think that a student will find it an interesting and even a controversial exercise to determine what, in fact, the rate of profit is.

It is a pity that the book is marred by a number of inaccuracies, many of them trifling but some which cannot be dismissed so lightly. This, however, will at least have the merit that the student will have to read with his critical faculties alert. Part II for example deals with company finance generally and is good, but it contains its share of inaccuracies and misleading innuendos, examples of which are given in the following paragraphs.

The author fails to make clear that it is only in respect of profits tax that there is a taxation advantage to a company in putting out a debenture rather than a preference stock.

Some of his definitions are loose or incomplete; for example when he comes to define subsidiary companies he fails to state that a company is a subsidiary of another company if it is a subsidiary of a subsidiary of that company—in other words that sub-subsidiary companies are subsidiary companies.

He is particularly misleading in some of his remarks about preference shares. The paragraph which begins at the foot of page 270 is a hotchpot of misinformation. Preference shares would not be offered to ordinary shareholders "on bonus terms" if they were offered at a price below their nominal value but rather if they were offered at a price below their true market value. The expression "on bonus terms" is, of course, widely used but is an unhappy expression anyhow, since any "bonus" received by the ordinary shareholders is paid for by the same ordinary shareholders. Furthermore it is not competent for a company to issue shares below their nominal value. Later in the paragraph reference is made to the ordinary shareholders having to face the eventual repayment of the preference shares at a price above their issue price; but apart from other considerations this will only arise if either the company goes into liquidation or the directors of the company (who in this respect would be considering primarily the interests of the ordinary shareholders), consider that it is worthwhile to repay the preference shares and find that they are able to do so within the terms of the Articles of Association of the company. It is tending to become standard practice in modern Articles of Association to give the preference shareholders the right of veto over their own repayment by making such repayment conditional on the approval of preference shareholders by extraordinary resolution at a separate class meeting.

Again the concluding sentence of Chapter 13 could give the reader a quite unwarranted impression that abuses of the spirit of company law are frequent. I consider that the wording used in the introductory paragraphs of the Memorandum by the British Insurance Association to the Company Law Committee (the Jenkins Committee which is considering the question of possible revision of company law), is a far fairer statement of the situation. It says:—

> "We feel that on the whole the existing company law has worked well, and that the general standard of commercial ethics in the world of finance and investment is high. But experience has shown that, on the investment side, in some respects there is need for additional safeguards for investors."

On the other hand I agree heartily with the comment near the beginning of Chapter 17 : " Finally, as long as company accounts make no reference to turnover and order-books, give no indication of changes in conditions within a period shorter than a year, and make no apportionment of profits between the different sides of a business, the student of company affairs must at the outset recognise the paucity of the information put at his disposal."

Part III gives an introduction to public finance and Part IV outlines the banking system and monetary policy. This contains from page 385 onwards an excellent working model of the central banking system which any student of the subject, using the word student in the widest sense, should find helpful.

Part V deals with the determination of security prices and contains a great deal of general interest to the reader. Parts VI and VII are concerned with national income and international trade while finally Part VIII brings the political and economic background up-to-date. This last part contains a gem of succinct narration which reads : " In the field of economics the art of government is not so much the art of the possible as that of balancing the incompatible." The book concludes with an excellent index.

On investment and on economics the perfect book has yet to be written. One could go further and say that the perfect book would be impossible to write. While I have referred to points where this book can be criticised, there are very many more where I have left the praise unsung. Mr. Rose is to be congratulated on bringing together into a single volume material which in general can be found elsewhere but—as his useful suggestions for further reading make clear—only after extensive exploration.

J. D. B.