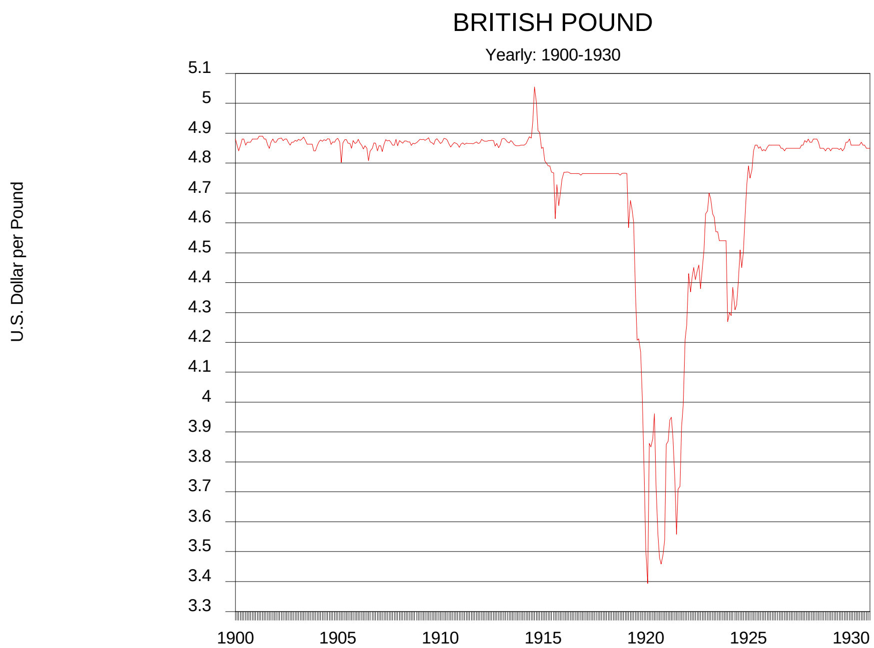
Chapter IV

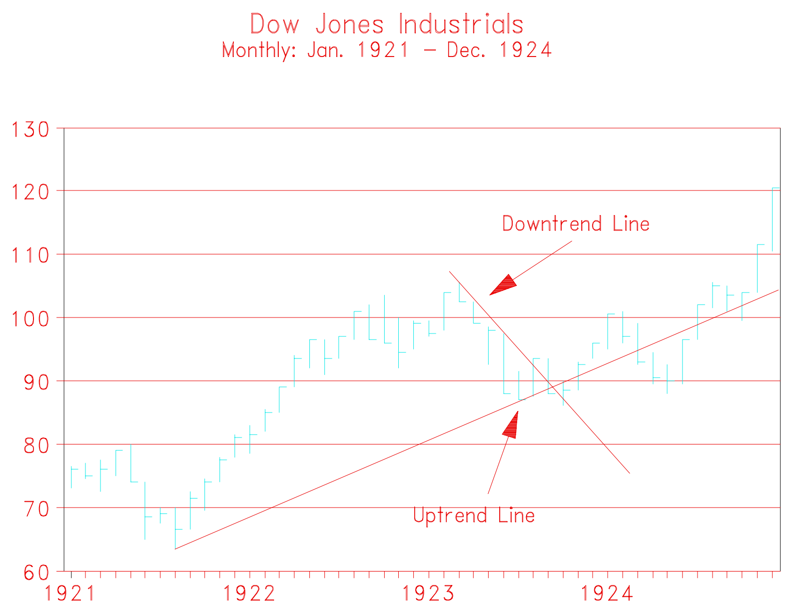
1924



The year 1924 began with the dollar continuing its rally into January. The British pound had continued to fall from its February 1923 high of $4.70 to its January 1924 low of $4.27. The French franc had fallen from its April 1923 high of 14.74 francs per dollar to 21.52 in January 1924. But the French franc continued lower against the dollar moving into February 1924, dropping to 23.58 to the dollar. This would eventually prove to be the high on the dollar until 1926.

The Swiss franc had proven to be the most stable of the European currencies. But here too, this currency dropped from its 1923 equivalent high in U.S. terms of 18.78 cents to 17.29 cents in January 1924. This would prove to be the low for the Swiss during 1924. The actual peak on the Swiss against the dollar had taken place during February 1922 at 19.6 cents and had steadily declined into the January 1924 low. From here, the Swiss would rally back to the 19.4 cent level but the 1922 high would not be penetrated during the balance of this decade.

The Dow Jones Industrials continued their rally which had begun from the October 1923 low amidst the bitter rumors which continued to fester over a proposed relationship between Livermore and the current administration. The railroads had also continued to rally into January along with the bonds. It was clearly a broad market rally and no one group could have possibly controlled enough capital to manipulate it.



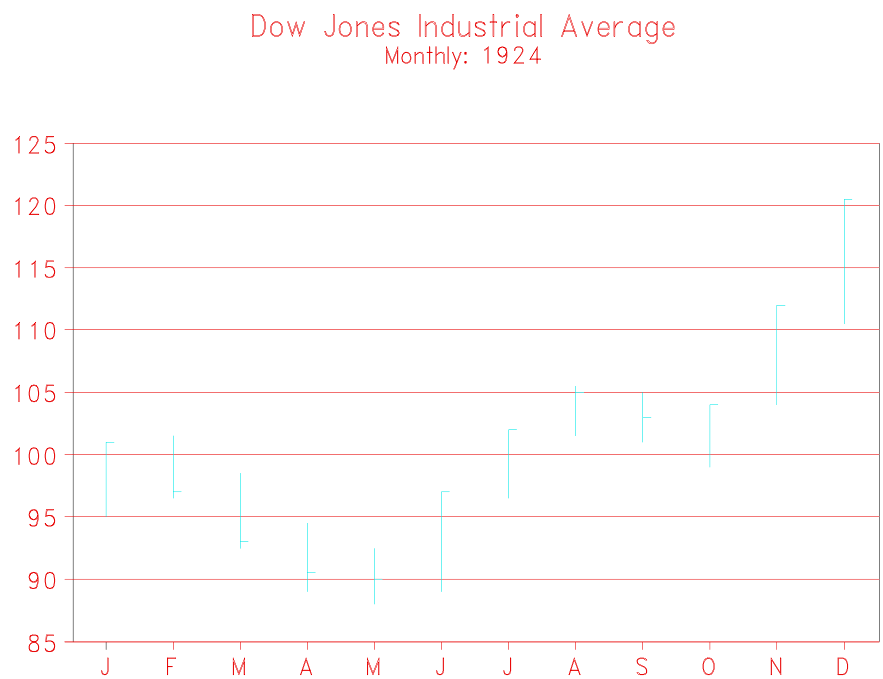
Indeed it would have been no "piker's game."

As it is today, people who are consistently wrong, or even temporarily wrong, make up rumors and stories against anyone who has been consistently right. Rumors normally run from, "Oh, he went bankrupt many years ago," implying that he will be wrong someday soon, to "I heard he was a crook so you shouldn't listen to him anyway" or "he has powerful friends and they are forcing the market to do what it would not do otherwise." These are all excuses put forth by the losers.

Jesse Livermore was one person who had been consistently correct about the market. The fact that Livermore was proved correct and that 1924 led to prosperity, "but not necessarily a boom," stands as witness to such accusations. In the years ahead, those who were the losers grew to hate Livermore, and instead of going with the trend many would fight it just to try to prove him wrong.

For those who were bearish and continued to fight the market all the way, the mere fact that U.S. Steel declared an extra dividend, based on the reality that earnings were rising, didn't matter. They remained convinced that lower interest rates indicated that a depression was due. It is amazing how differently we view the stock market today in relation to interest rates as compared to the bull market of the 1920s.

Technically, we can see that the August rally exceeded and even closed above the 1923 Downtrend Line. Although September fell back below the Downtrend Line, the market rallied back above it in October and was now ripe for an upmove. Technically there was clearly a lack of follow-through to the downside. Looking at the Uptrend Line on the yearly Chart taken from joining the 1921 and 1922 low, we can see that the 90 level was quite important. Although October 1923 exceeded the 90 level, it fell back for the monthly close. November ran up and exceeded the Uptrend Line and closed above it. Although the Industrials had not exceeded the 1919



high, they were clearly in a technical position to try one more time.

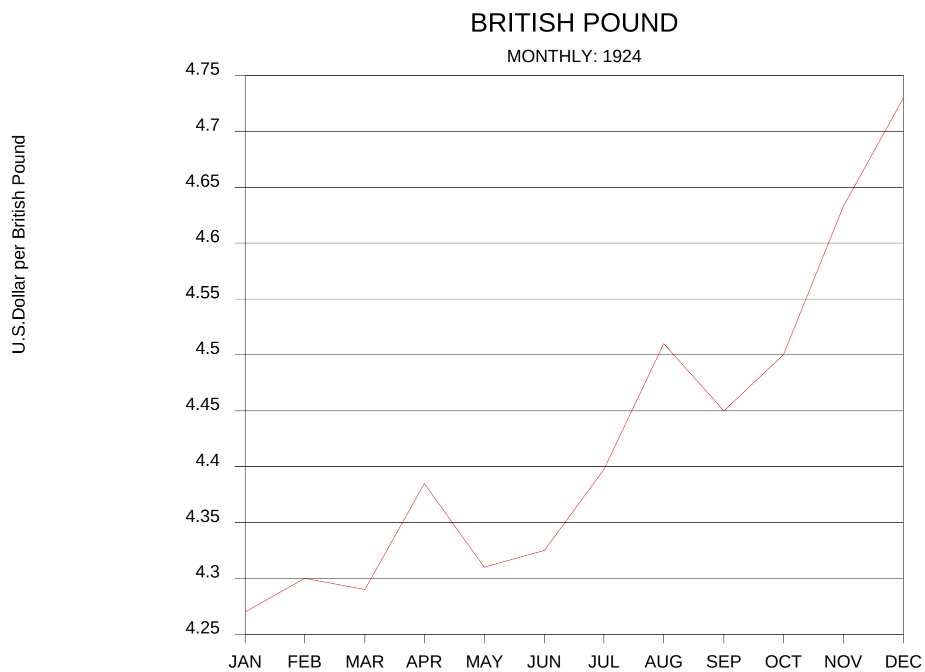
We can see from the yearly chart provided for 1924 that the market continued higher into early February and then once again corrected for a three-month reaction into May of that year. The early summer brought a substantial rally in the stock market and by August the market closed above 105 on a monthly basis. After a two-month sideways pattern going into the Presidential elections of that year, the Industrials soared as December ended and closed above 120 at record highs.

1924 brought many signs of relief, and Livermore's gut feelings proved to be correct. Germany issued the new Reichemark, which was exchanged for 1 billion old marks and was backed by 30% gold. In the United States, corporate expansion continued but, more importantly, new companies were being formed. IBM had its beginnings in 1924 along with MGM, Columbia Pictures, Dean Witter & Co., and Massachusetts Investors Trust; Kleenex was introduced and so was the first Chrysler.

There were still great arguments for both pessimism and optimism. In January 1924, the New York Times listed the issues for both sides but drew no conclusions. They were published as follows:

"The Grounds For Hopefulness
1) Our Impregnable gold, credit and banking position.
2) Large recent profits in industry.
3) Recent record freight traffic and signs of its likely continuance.
4) A conservative and economical administration in Washington.
5) Economic recovery in Europe, clearly beginning despite Germany and Russia.

The Case for the Pessimist
1) Potential of credit inflation due to our abnormal gold reserves.
2) Uncertainty as to the continuance of large industrial profits, as seen in declining commodity prices, the steel industry, etc.



3) Probability of attack, and its possibility of success, by radical Congressmen upon the Transportation Act.

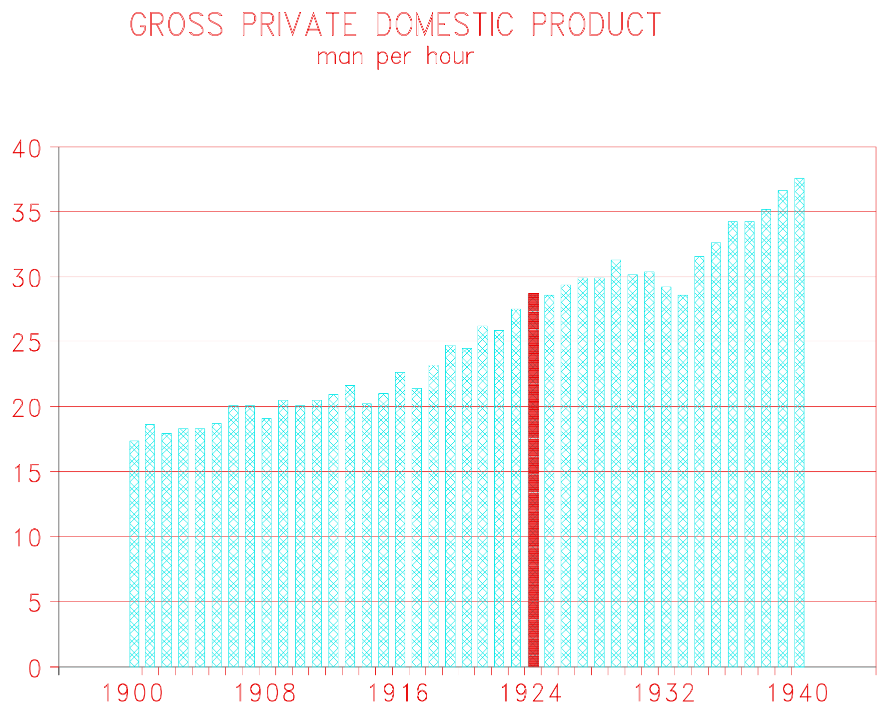
4) Unsettling influence of Presidential election, bonus agitation, possible tampering with Federal Reserve Act by farm bloc.

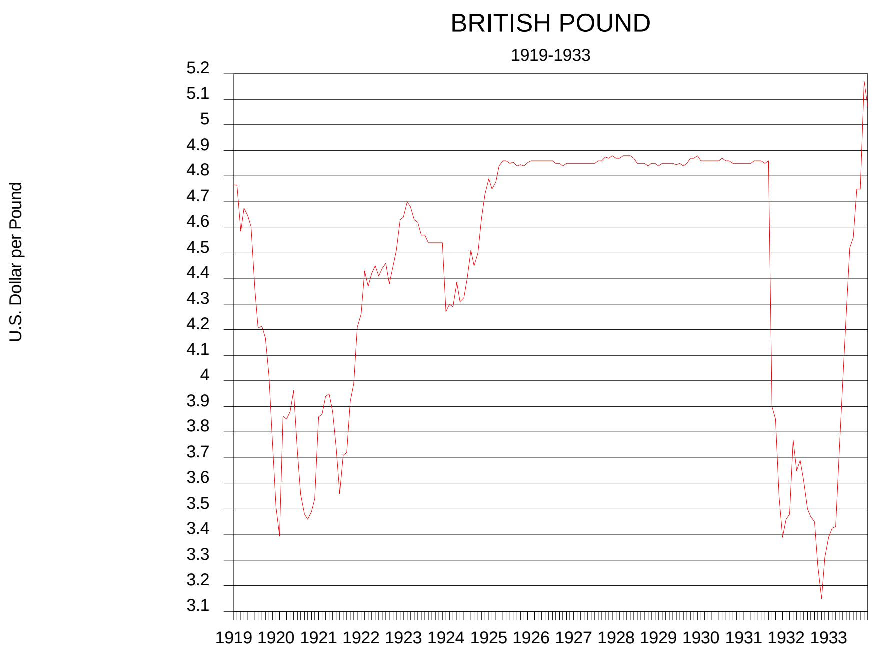
5) Germany drifting into bankruptcy, England faced with a Labor Ministry, France feeling the results of debt inflation, reparations still unsettled."

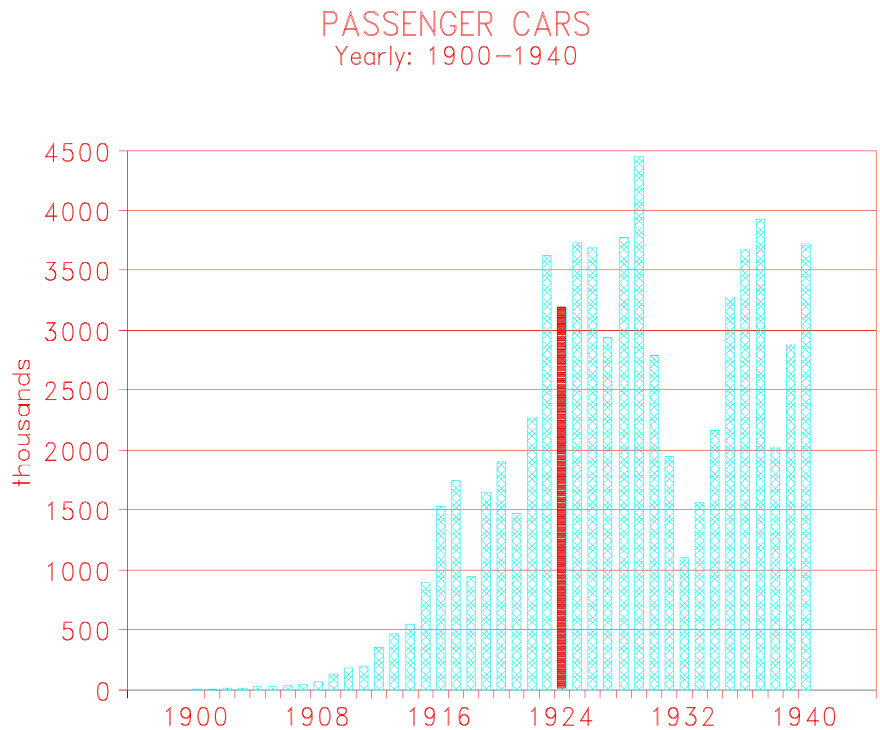
During the period of the 1920s, the so-called knowledgeable investor and analyst seemed to pounce upon every aspect of each issue and preferred to take the pessimist's view. But the bull market of this entire period was built upon the average man who came into the market and paid cash. Contrary to many false beliefs about this period, a number of the more leveraged speculators lost money on the way up as well as down.

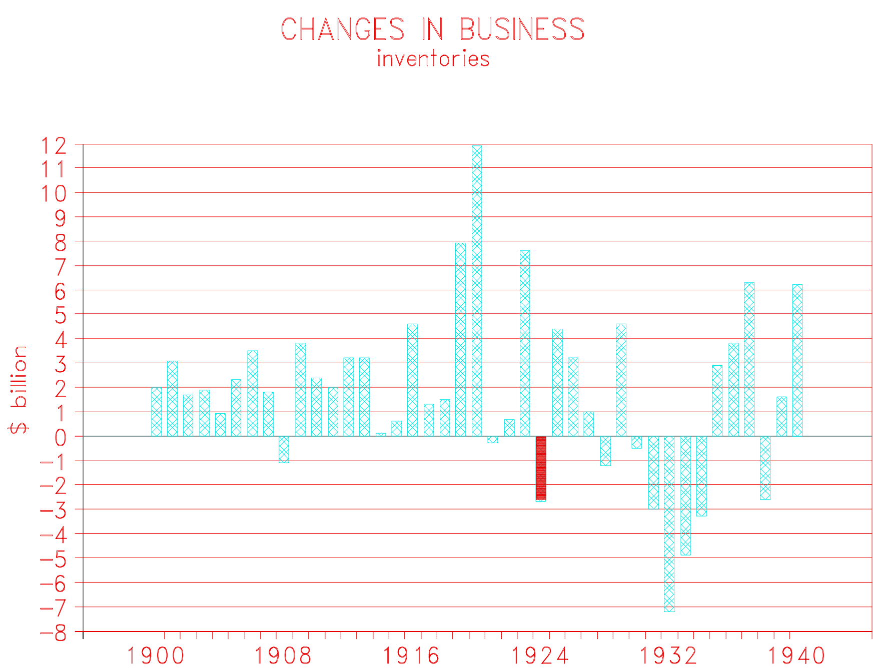
The U.S. gold reserves had reached their highest point in history with nearly half the entire world's official reserves held by the United States. Interest rates were easy, money was easy, and there was no appreciable sign of runaway inflation. Yet the soundness of the banking system was questioned; it would lead to inflation, pessimists asserted. When it came to corporate profits, the pessimist admitted that they were rising and at a record pace. But how long could this last? The U.S. would follow in Germany's footsteps, they proclaimed. This type of attitude continued for many years because these were the very traders who kept on shorting the market and who spread rumors about Livermore in an effort to discredit his accuracy and experience, both of which they lacked. Their principles had been based upon a foregone conclusion propelled by an unwarranted assumption.

Corporate profits were up on an average of 30% along with dividends as the expanding American economy prompted many members of the general public to take stock in America. The railroads, after being hard hit in 1923, rallied sharply, still leading the industrials on the way up. The prosperity and expansion continued as America became the leader in innovation.


GROSS PRIVATE DOMESTIC PRODUCT
man per hour
40
35
30
25
20
15
10
5
0
1900
1908
1916
1924
1932
1940


BRITISH POUND
1919-1933
U.S. Dollar per Pound
5.2
5.1
5
4.9
4.8
4.7
4.6
4.5
4.4
4.3
4.2
4.1
4
3.9
3.8
3.7
3.6
3.5
3.4
3.3
3.2
3.1
1919 1920 1921 1922 1923 1924 1925 1926 1927 1928 1929 1930 1931 1932 1933


PASSENGER CARS
Yearly: 1900-1940
thousands
4500
4000
3500
3000
2500
2000
1500
1000
500
0
1900
1908
1916
1924
1932
1940


CHANGES IN BUSINESS
inventories
$ billion
12
11
10
9
8
7
6
5
4
3
2
1
0
-1
-2
-3
-4
-5
-6
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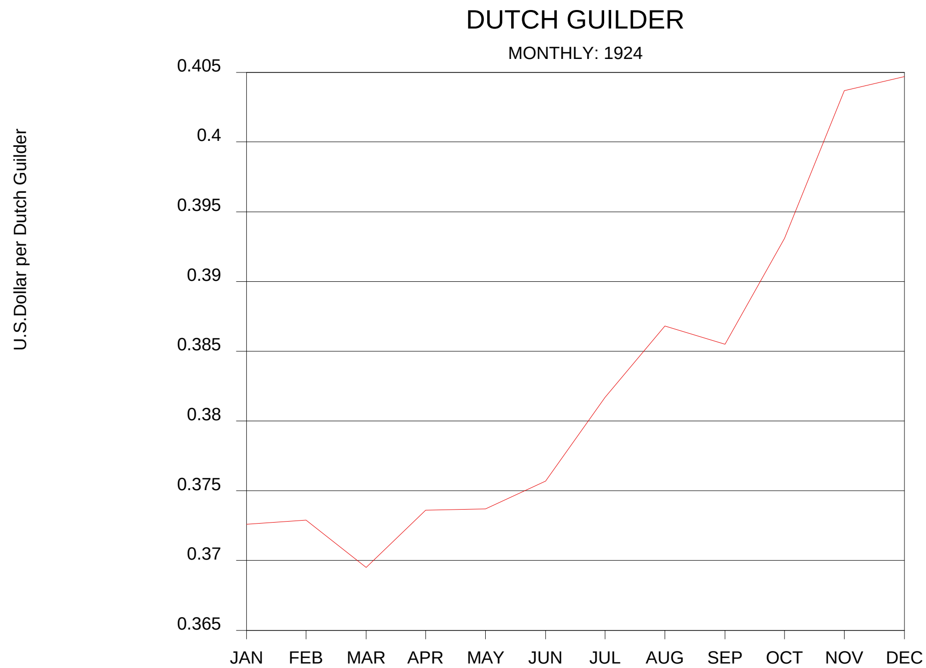
1916
1924
1932
1940



The automobile industry consistently confounded all conservative judgment. Year after year it apparently reached what the pessimists projected was its saturation point. Nonetheless, auto production forged ahead to new record highs. The cost of automobiles had actually declined by 11% from 1913 to 1923. This was largely due to the assembly line method of production.

In January 1924, U.S. Steel announced another extra dividend of 25 cents, and the very favorable fourth quarter report for 1923 displayed earnings of $49.9 million, up from $47.1 million in the third quarter. This meant that the normal dividend of 6% annually had risen to 7%. In 1922 the mills were operating at 75% capacity but as 1924 began they were at 90% capacity.

As the market rallied from the fall of 1923 into early February, Jesse Livermore began to sell out his positions in favor of the short side. In the February 25, 1924 edition of Time magazine, the business and finance section carried this article:

"Mr.Jesse Livermore, young man with light hair, big back head and solemn face, knows more about stocks and such things than all others put together. So it is said. He sells or buys tens of thousands of shares at a time and thousands follow when he says, 'Buy' or 'Sell.'

"Wall Street last week gave an exhibition of mysteries second only to the oil scandal in Washington, and in fact caused by it. The stock market had advanced steadily if irregularly for many weeks, and had become over-bought and top-heavy. At such times, any incident is enough to cause an upset.

"At this stage, enters Mr. Livermore, the noted operator. His last two main prophecies on the stock market had been sufficiently fulfilled so that he had attracted considerable speculative following. From his vantage point in Miami, he sent a statement to the press which was widely published, although the Wall Street Journal refused to include it in its columns. Mr. Livermore declared that the oil scandal had undermined confidence in the stock market, and rendered doubtful the presidential nominations.' I think it is very foolish trying to be an optimist in the stock market at the present time,' he added. The effect of his pronouncement on the stock prices was electrical. In a single day, Fisher Body tell 13 points, General Electric 8 1/2, Du Pont 7 1/2, Baldwin 6, American Can 5, National Lead 8, Houston Oil 7 1/2, U.S.Steel 3 1/8, Studebaker 3 1/4; the entire list with hardly an exception declined.

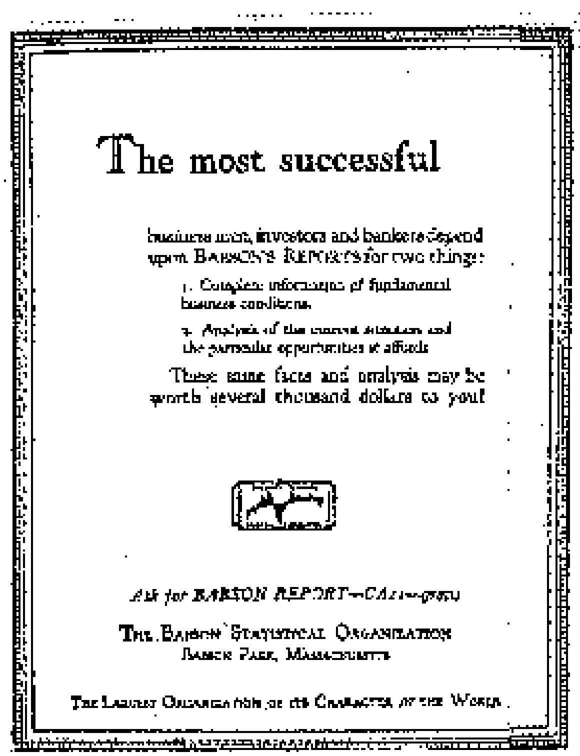
"Flattering as such results may have proved to Mr.Livermore, the real cause of the sudden decline was undoubtedly the 'technical position' of the market. After all, Mr. Livermore is a better Judge of the stock market than of national affairs. This was shown when he advocated more businessmen in our government, only to meet Senator Lenroot's retort that there had been several prominent business men rather too much mixed up in government affairs lately."

Livermore had been proven correct not only about the market but about the economy as well. Nonetheless, few people like someone who is more correct than incorrect, particularly when money is at stake. Not only did the Wall Street Journal refuse to even mention the accuracy of his predictions in light of their own views, but many grew to fester a hatred toward the man. Perhaps it was human nature to blame manipulation on Livermore rather than admit one's own error; nonetheless, this attitude could continue to the point that his own life would be threatened because of his accuracy.

Even today, the vast majority of people who trade the stock market rely totally upon fundamental analysis. The greatest of all problems lies in the fact that fundamentals change so quickly, and that the very same fundamental is often used by both the pessimist and the optimist in their arguments to support their positions.

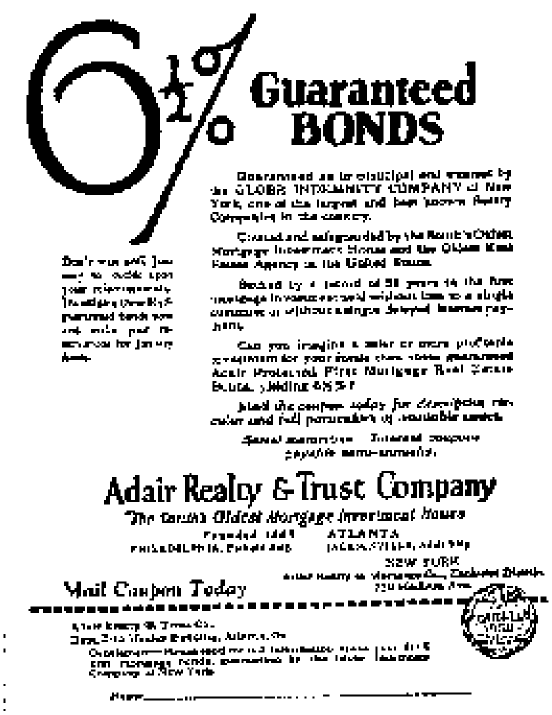
As the stock market bottomed in 1923, the height of pessimism existed. Rather than believe that the corporate strength within the economy was still moving along, indicating that the decline in the market was merely a consolidation phase, the majority chose the position that held true to their conviction that the stock market was a leading indicator, and that in itself suggested a time would come when corporate earnings would eventually drop.

With hindsight we can see clearly that that position was incorrect. There were many various fundamentals that were obviously overlooked by most analysts at that time. Foreign trade during 1923 averaged more



than $26.5 million for each working day. Exports were $13.8 million and imports averaged $12.6 million per working day. Almost two-thirds of the exports were in the manufacturing sector while the imports were primarily raw materials used in production. As 1924 began, January imports were valued at $299 million against exports which were valued at $394 million for the month.

In addition to the positive production posture of that time, the U.S. had become a creditor nation instead of a debtor nation. This did lead to serious criticism and many complaints. The complaints came largely from Argentina and Japan who claimed that the U.S. was forcing them to pay exorbitant interest rates. Of course, much was due to political reasons on the part of the party which was currently out of favor criticizing the party in favor. The truth of the matter was that foreign nations who came

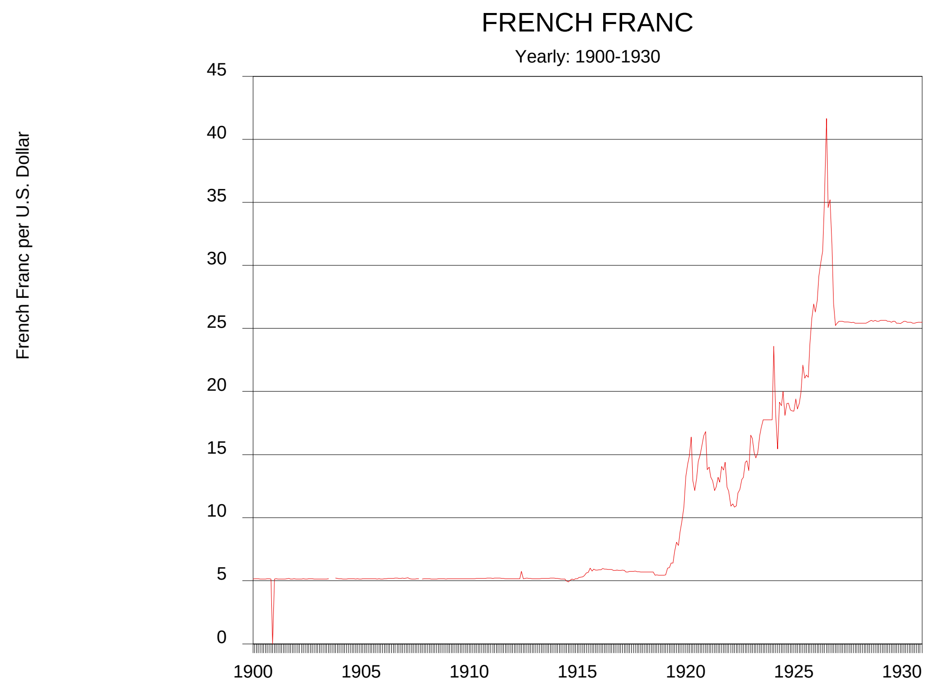


to the New York market had to compete for money against the steady demand for domestic money on the part of business and investment, which stood at several billion at that time. Therefore, to entice investors to purchase their foreign bonds, it was only natural that they would offer much higher rates of interest in order to attract_willing lenders. This was one reason why the Federal Reserve maintained the discount rate at 4.5%, which was sharply higher than call money rates.

Inflation was a concern as a result of the rising gold reserves, which stood at record levels. This was being caused by two factors. First, a strong trade surplus and second, a definitive fight in international capital to the U.S. as political and financial stability throughout Europe remained in serious question. Nonetheless, the cost of living had dropped during January by .2%. From the peak in inflation, July 1920, to January 1924 the actual cost of living had declined by 19.5% despite the rise in the gold reserves.

Time magazine reflected the sentiment in their March 10, 1924 issue by commenting on all the positive annual statements that had been pouring out for 1923 in nearly every sector. They stated: "It is, however, always important to remember that by this time annual statements for 1923 are practically ancient history. They indicate whether the given company has a strong or weak cash position, but they give little hint as to the present operations or future outlook. While sentiment is divided between optimism and pessimism, the perusal of these statements is valuable in gaining perspective; they cannot and do not furnish much of a basis for future predictions."

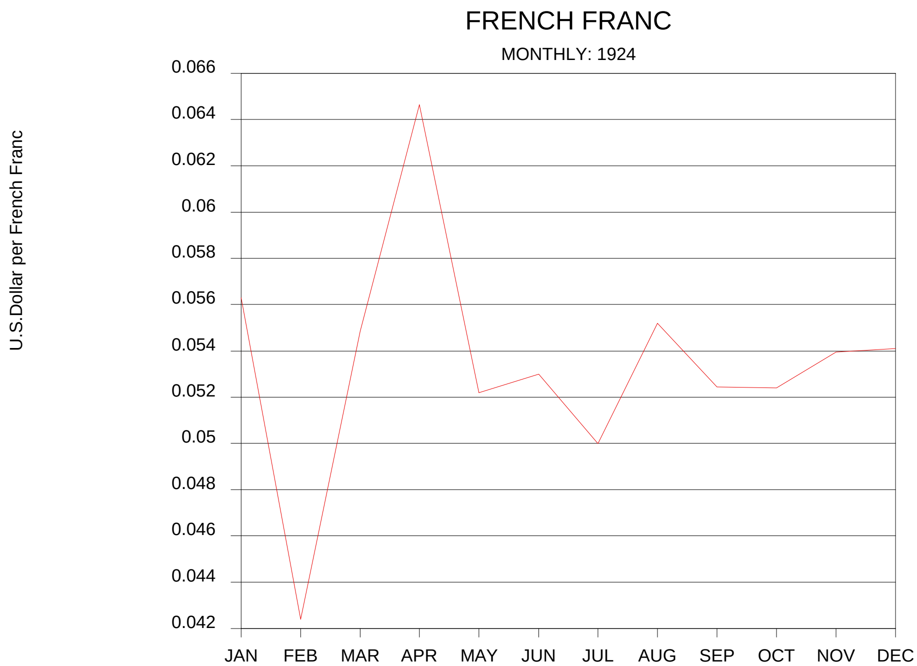
The pessimism that underscored the press commentary during March of 1924 was



quite amazing. Here the stock market had just rallied sharply, peaking during early February. Only one month of lower trending prices and everyone was right back to the good old doom and gloom scenarios, ignoring fantastic corporate earnings which should have been the basis for a solid bull market in the first place. They also ignored the fact that gold was still flowing into the States and that most of it was due to a flight of capital in favor of the U.S. economy which reigned supreme in the world at that time. The downtrend continued from February 1924 into May of that year. The foreign situation was beginning to turn during late February. Several new governments had been set up by the Treaty of Versailles and those that had been seriously battered by hyperinflation were returning to the gold standard.

France established a gold franc that was equal to 19.3 U.S. cents. However, 20 gold francs contained .1867 troy ounces of gold. Nonetheless, France did not mint any gold coins for general circulation between 1915 and 1929. Austria, with the help of Britain, discarded the krone in favor of the new schilling, which was based upon silver. The new retenmark of Germany was equal to 23.8 U.S. cents and based upon gold. Even Russia, after realizing that its rubles were worthless, issued in 1923 the new "chervonetz," which was equal to 10 gold rubles or $5.15. Hungary was forced to abandon the old krone in favor of the new "sparkrone." The European trend was not necessarily to redeem its old currencies, but instead it practically repudiated them by creating new currencies based upon gold.

The February 1923 high in the Dow had corresponded precisely with a high in the dollar on world exchange markets. As Europe regrouped, cash flow into the States began to subside and so did the buying pressure from overseas. Analysts, however, continued to view the market solely from a domestic perspective, giving no recognition to the fact that perhaps America had a monopoly upon economic stability at that time.



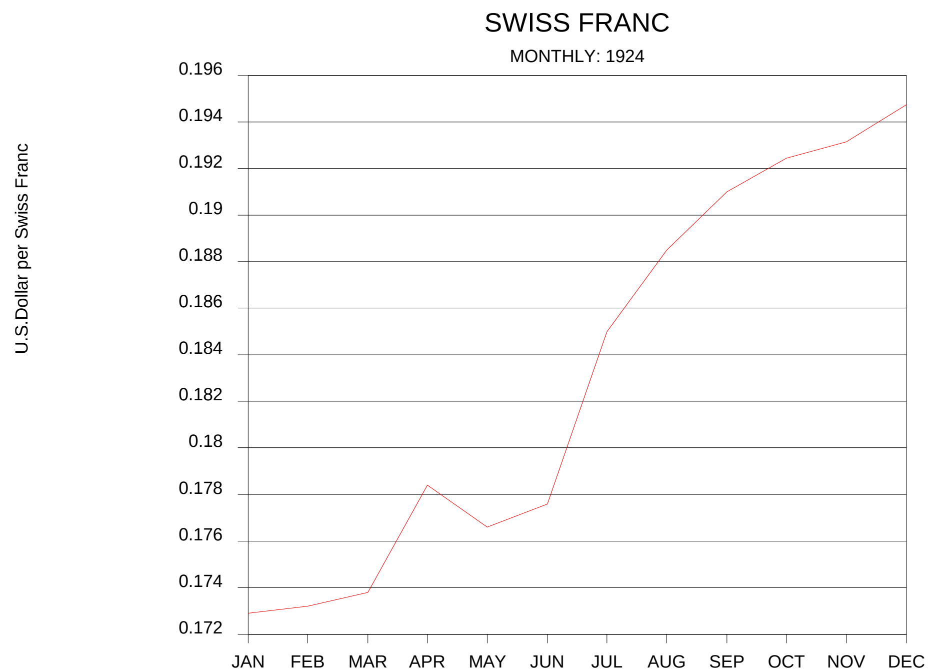
Nevertheless, as the stock market continued lower, gloom became fashionable once again. In the April 21, 1924 issue of Time magazine the opening statement under the business and finance section had this to say about the current atmosphere: "Amid the babel of conflicting opinions during the past week, on the future probabilities in business, one strong and uncompromising attitude became conspicuous. This was the bearishnsss of Wall Street."

The analysts, who preferred to choose the bearish side as usual, were pointing out that although the stock market had rallied sharply from the fall of 1923 into early 1924, many stocks remained at their lows. It was true, in fact, that many stocks did not participate in the sharp rally. Industries such as leather rubber, shipping and fertilizers had hardly moved since the February high, and neither had the automobile stocks or steel and tobacco. Others pointed out that the railroads had held up rather strongly.

The analysts were much too busy trying to find stocks that did not participate in the rally to justify why the market would continue lower, rather than explaining honestly why some sectors had risen sharply. The real reason why the rally from the 1923 low into the early 1924 high was not a broad market rally is twofold.

First, call money had remained under the discount rate and time deposits were paying 2% at best. Most foreign bond issues were forced to pay 6% to 8% in order to attract lenders. But many small investors who entered the market on full cash positions and not margin were attracted to issues which were paying an annual dividend of 5% or better. U.S. Steel is only one example. The speculators were interested primarily in price fluctuations while the capital investors were interested in return. With turmoil in Europe on the front pages during the last quarter of 1923, it was not hard to figure out, given a choice between a foreign bond paying 6% and U.S. Steel, which of the two was the safer capital investment.

The second reason why the rally into early 1924 was a selected rally lies primarily in



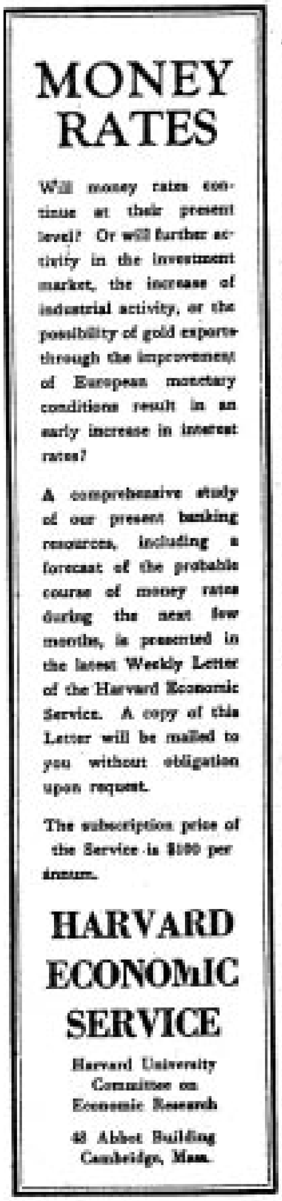
the realm of foreign exchange. Foreign investors were also attracted by the better performing companies with the best dividends. As the dollar continued its rise, the gold reserves continued to expand to record levels. The trade balance between the U.S. and Europe continued to move in favor of the U.S., reflecting a strong export economy which aided the rise in the gold reserves. However, the gold reserves grew even sharper than the exports which reflected that a net capital flow to the U.S. on a cash basis was also taking place. This was not in payment for goods but capital fleeing into the dollar.

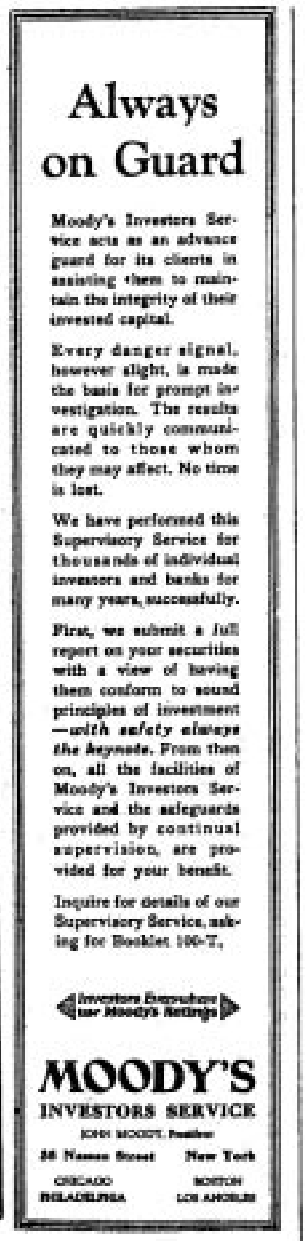
Therefore, it clearly seems plausible that the only people who didn't know why the market had risen during that period when the dollar rallied sharply were the professionals.

The small U.S. investor's motives were dividends and concern over foreign bonds. The international investor focused on the safety of the dollar and the profits brought through foreign exchange. Both forces combined to make the rally from the 1923 low a rally which was selective largely focusing upon the blue chips. In many respects this was the very same type of rally which was witnessed from the September 1985 low when the Dow Jones Industrials lead the broad market to new highs all the way.

The real estate boom, which was largely taking place in the East, was becoming a little uncertain at this point in time. Commentary again found Realtors expressing their fears that the boom was now at an end. Commodity prices continued to fall from December 1923. Yet some commodities such as livestock, oils and building materials, were advancing. Nonetheless, steel production was establishing all-time new records. Output for March had reached 4.1 million tons compared to 3.7 million tons during the previous month, 3.6 million tons in January 1924, and 4 million tons during March 1923.

The fears that were circulating were largely based upon anticipation rather than on hard-core facts. Most became skeptical





about the future of business conditions every time the stock market began a down tick. But the building boom was still intact even during March. Building expenditures during March 1924 were $318 million compared with $248 million in February, $189 million in January and $292 million during March 1923.

The Federal Trade Commission was also active during those days. They sent forth a directive to Eastman Kodak and associated firms that stated in no uncertain terms that they must cease from restraining competition in the manufacture and sale of motion picture film. It specifically singled out and barred Kodak from acquiring control of three additional laboratories. The Commission reported that Kodak had essentially a monopoly on the manufacture of positive film and a complete monopoly on negative film.

The sentiment hadn't changed, and as April continued to click on by, the April 28 commentary in Time Magazine was still quite gloomy: "Nothing is quite so easy to do, or so unfair in the doing, as throwing mud at former prophecies that haven't panned out. Hindsight, now as previously, is much simpler than foresight. All the same, there was heard last week considerable criticism of the bankers and industrial leaders who last fall predicted great prosperity this spring. The spring has come, but profits in most lines of industry are getting leaner each week; in some industries they have disappeared."

April began to see somewhat of a decline in production and this prompted everyone to proclaim that the stock market peak in February had foretold of this disaster. The declines were actually hardly worth noting, yet the press focused upon the disasters which were still centered within the leather, textile and fertilizer sectors. Time reported: "It is the basic 'assumption' now for a quiet summer and only a bit of a rally in the fall provided Coolidge is reelected."

It was during May 1924 that John Maynard Keynes' book hit the streets selling for $2.50. Perhaps no one realized at that time just how much difference that $2.50 would make in the future events of Western civilization. His book was revolved by Time on May 12, 1924 under the title of "Monetary Reform." Time commented on the book as follows:

"Mr. Keynes, famed British economist, has never before emphasized so clearly the fact that he is a fiscal Bolshevik.

"Monetary Reform analyses the function of money, shows how it affects the investing and business classes, the earner, production. It discusses inflation and its relation to taxation and capital levy. It delves into the whole theory of money and the foreign exchanges. It suggests alternative aims in monetary policy and then advocates inflation, neatly garbed.

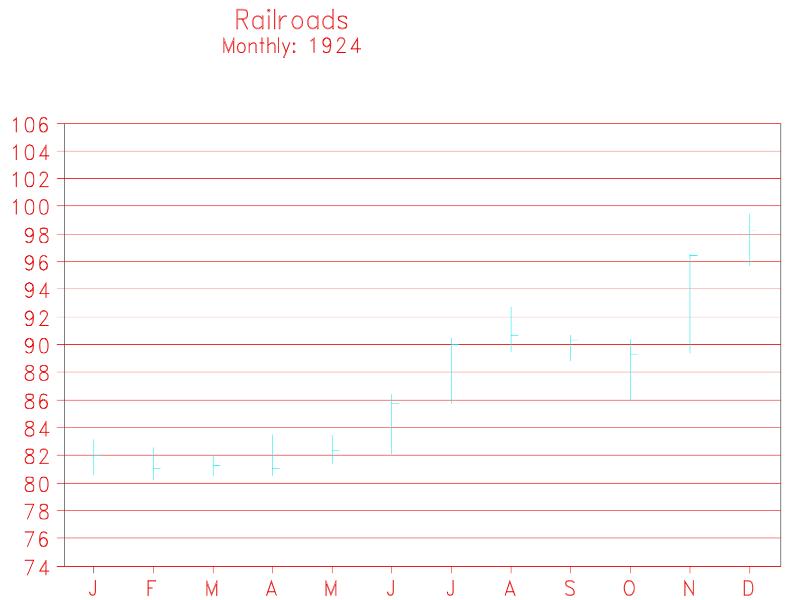
"Mr. Keynes wants a devaluation of currency, which means stabilization of money at present values. He wants internal purchasing power fixed on a commodity-value basis related to unemployment, state of trade, etc., while the external purchasing power shall be controlled by gold whenever necessary.

"Those readers who have followed Mr. Keynes' recent course will not be surprised at this attack on the present fiscal policies of most countries. Mr. Keynes would have the world embark upon great experiments. He apparently imagines that the clarity of his expression stimulates not the imagination but the common-sense of men. His contentions are a subversion of established fiscal policies in use for more than 100 years, a period in which, as Mr. Keynes agrees, the gold standard of currency became the unquestioned foundation of 'the stability and safety of a money contract.' It is inconceivable that rapid progressivism should be regarded favorably in the conservative world of money.

"The author is fortunately being ignored, because every country in the world is seeking to claim parity with the dollar and to fix its internal values to the gold value of its currency or in other words, to deflate. Furthermore, if the signs of the times be read aright, the Federal Reserve Bank has already adopted a policy of discounting European notes in large amounts, which is a policy more calculated to assist the recovery of European currencies than any yet operated."

Time's unfavorable commentary upon the publication of the Keynesian theory, which is so widely employed today, provides a good insight into the general attitudes which prevailed. Those who have attributed the great bull market of the 1920s to irresponsible speculation that swept the nation should go back and read a bit further beyond 1929. If anything, the one consistent undertone that prevailed was one of disbelief and conservatism. On the slightest down tick, pessimism soared. Perhaps rightfully so, considering the number of panics that had taken place during the previous 20 year period.

Nonetheless, as the market continued lower into May, industrial production did have a fairly sharp correction in a very abrupt fashion. Steel production, which had been at 90% capacity, fell to 60% capacity in May. Yet there were some strange signs which counteracted against the declining stock market and sharp correction in the industrial production. Money was very abundant and very cheap. As the stock market bottomed, commentary in the press by early June compared the stock market to a motionless sphinx which had entered a



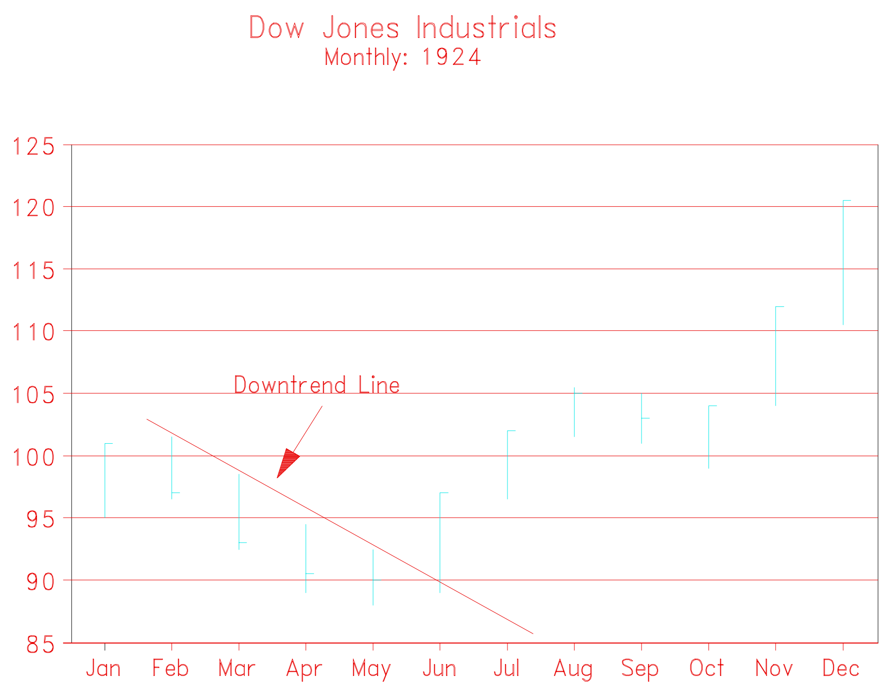
Sargasso sea where ships became entangled in a bed of seaweed.

The economy had indeed come to a pause in its robust fervor for expansion. In part, this was created by the sharp rise in the dollar. Exports to Europe had slackened during the first quarter in response to the high in the dollar and the adjustment period following the collapse of Germany.

One aspect of the foreign war debt owed to the United States had begun to rear its horns and it eventually became a leading element thrusting the U.S. into a debtor nation position decades into the future. The total war debt owed to the U.S. from World War I was roughly $11 billion. While Europe haggled with reparations demanding $33 billion in payment from Germany, the British and the French launched propaganda toward the U.S. and indeed within its own borders to forgive its war debts. By this time, the U.S. had already granted concessions to the European governments forgiving a portion of their debt. The British were given a concession of 30%, the French 40%, the Italians 70% and the Belgians approximately 60%.

One aspect of the war debts had a large part in creating the Great Depression (which eventually led to Keynes' "Bolshevik" policies being embraced out of sheer desperation), and this lay solely in the interest impact to the United States. By 1929, only $250 million in payments would be made by Europe on its war debt to the United States. That same corresponding period cost the U.S. government $450 million in interest to float that loan through its own bonds.

This effect would be a subtle yet distinct factor which would remain hidden in the economic statistics for many years. The reluctance of Europe to pay its debt then and after World War II added a fair portion to the U.S. national debt, which to this day is still being carried at interest costs in the hundreds of billions in 1985. Eventually in 1933, France repudiated its debt on the premise that it could not afford to pay its $60 million annually. The truth of the mat-



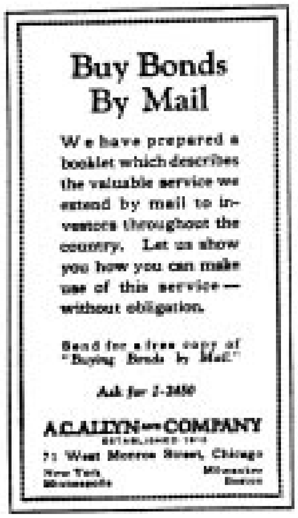
ter is that France at that very moment had $500 million on deposit in New York City from a surplus on international exchange.

The foreign trade picture began to turn equally as fast as the dollar's retreat from its January-February 1924 high. The British pound rose from its January low of $4.27 to $4.38 by March. By July this trend continued as the dollar retreated and the pound rose to $4.57. By year end, the pound closed 1924 at $4.73 near the pre-war par level. 1924 began a sharp upturn in U.S. exports to Europe and the trade surplus grew sharply, rising 44% above the 1923 surplus. This trend began to shape the future in April although the market would continue lower into May.

Technically, the market had corrected into a May low. The 1924 Downtrend Line (connecting the February and March highs) had contained the rallies during April and May. During early June, the market had begun to rally and once the 1924 Downtrend Line was exceeded. The market fell back and tested it once on a weekly basis and never looked back again. By August the market rallied to slightly above the 105 level, trying for the second time to penetrate the 1923 high and the major high of 1919. As I have discussed at our technical seminars over the years, the more a market tests the same area, the more likely it will be for penetration and eventual follow-through.

On June 9, the press admitted that perhaps the business conditions were not going to collapse entirely. Most commented upon the fact that money was easy and that the outlook indicated that it would continue to remain so.

The banking business began at this time to take on a new style or image. Prior to mid-1924, banks regarded advertising as undignified. Yet all sorts of advertisements began to appear in the papers. Steady and aggressive campaigns were launched as **a** scramble to become a billion dollar bank became the main battle cry. Up to this time, only the American Bank had surpassed that lofty goal. This change in the banking attitude also played an important



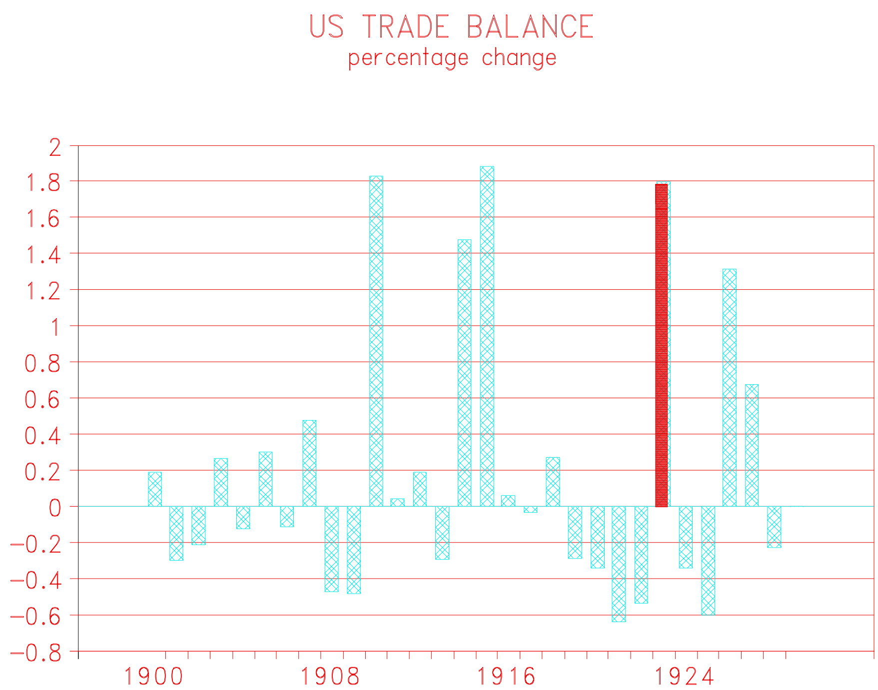
role in the mental attitude that would help create the biggest bull market in history. Numerous major corporations had been formed and the public was bombarded by new and exciting events. Banks were aggressively competing for business, which tended to increase the perception of just how sound the underlying structure actually was at that time.

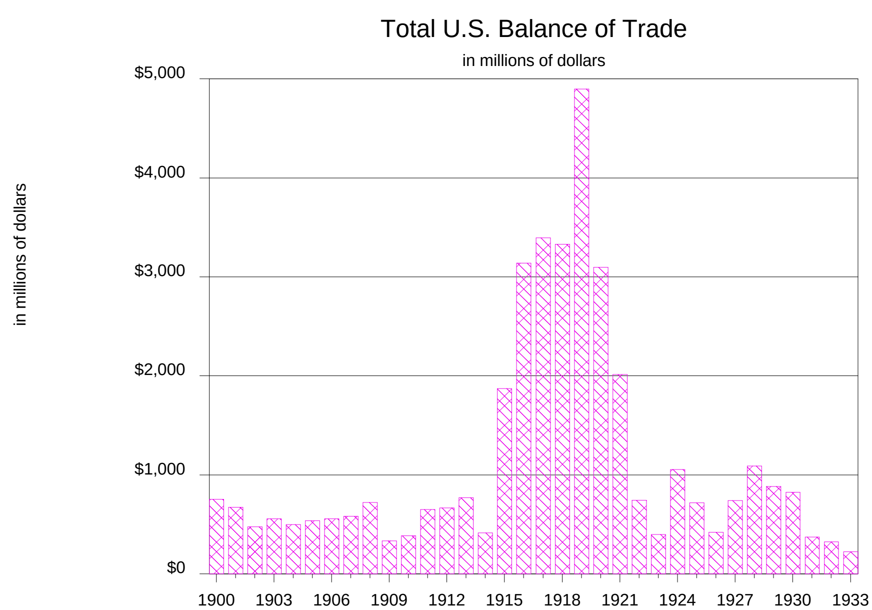
Interest rates were falling drastically. By mid-June, call money rates fell below 3%, setting a new record low; by June 20, call money fell to 2%, which was a six year low. The Federal Reserve followed suit and the discount rate was lowered from 4.5% to 3.5%. The stock market began to rally. Today such a rally would at once be attributed to a decline in rates thereby affording more capital for speculation. But once again it coincided with a rise in capital flow in favor of the U.S. created largely by the dramatically rising trade surplus. The discount rate cut came after the market had already bottomed and the gold reserves were growing abnormally once again.

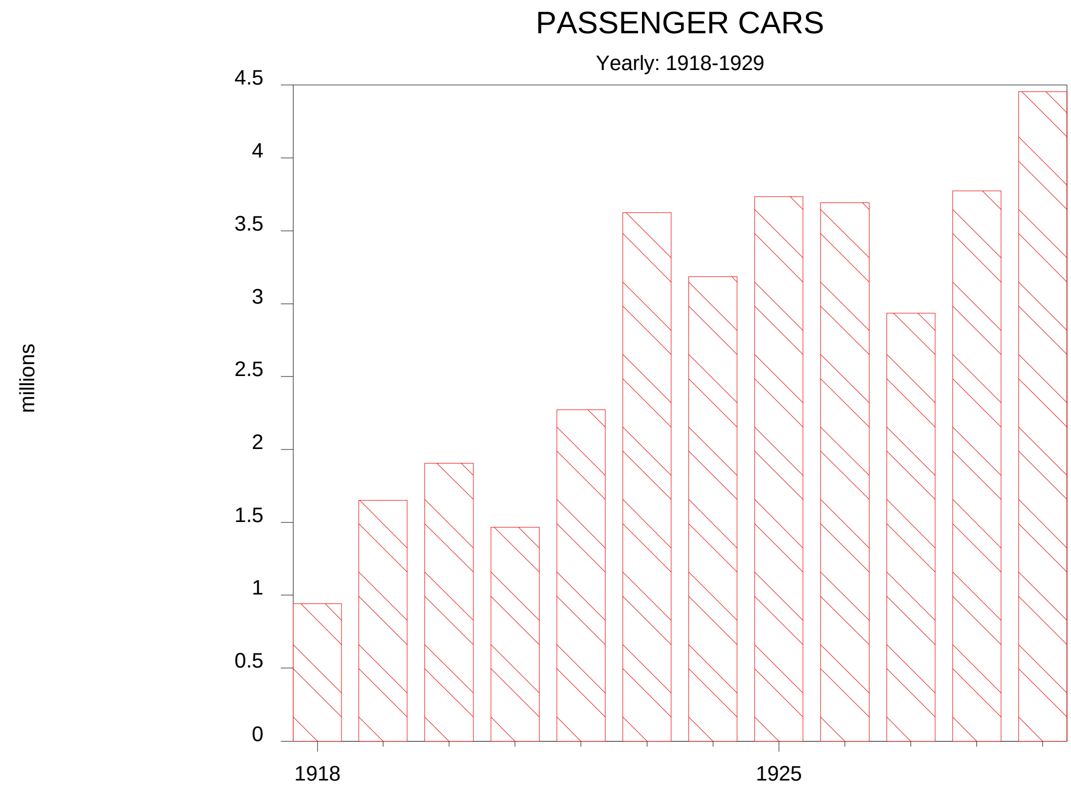
Everyone was waiting for Livermore, who back in February proclaimed his bearishness and was once again right on target. The press called upon him to see if he would give the market his blessing but he remained unchanged. However, he gave his reasons which were widely published. He basically stated that he felt that it takes a lot more than simply cheap money to make a bull market and he pointed out quite correctly that all the recent rallies in the stock market had taken place during rising periods when interest rates were substantially higher or during sustained periods of higher rates. Most of the press ended their articles much more favorably than in the past. For example, one article ended by adding: "The importance attached to Mr. Livermore's opinion in Wall Street and elsewhere is due to the large number of times he has been correct."

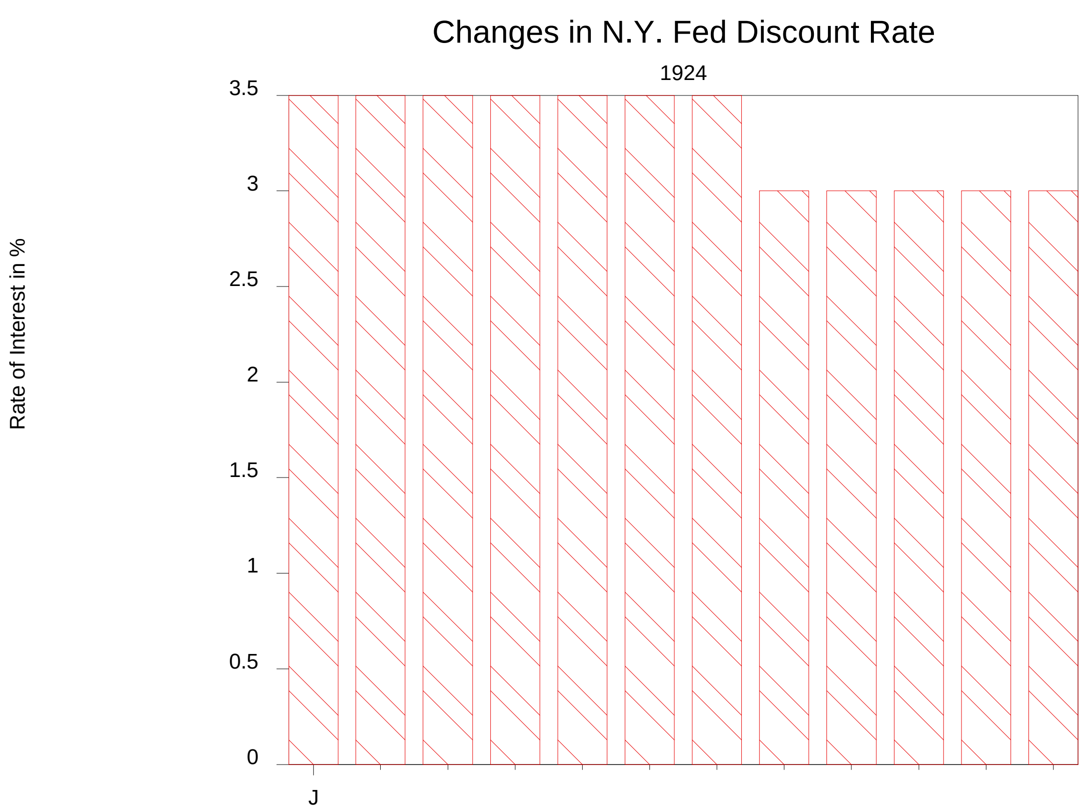
During this period there was actually an oil crisis taking place simultaneously with the stock market low. In 1923, there was an unexpectedly large oil production. Most companies had stockpiled crude because prices had dropped sharply when auto production fell to some degree. However, in those days, oil consumption depended greatly upon the weather, not for heating oil considerations, but for gasoline consumption. The winter of 1924 was exceptionally cold and the spring was wet. The automobile was largely a novelty and used primarily for excursions and this put a damper on the American motoring public's activities which included joy rides into the country for relaxation. If weather was bad, gasoline consumption fell.

But during the spring of 1924, the oil companies raised the price of crude, bringing out the wildcatters once again. This sparked further production and gasoline stockpiles rose tremendously, setting a re-


US TRADE BALANCE
percentage change
2
1.8
1.6
1.4
1.2
1
0.8
0.6
0.4
0.2
0
−0.2
−0.4
−0.6
−0.8
1900
1908
1916
1924


Total U.S. Balance of Trade
in millions of dollars
in millions of dollars
$5,000
$4,000
$3,000
$2,000
$1,000
$0
1900
1903
1906
1909
1912
1915
1918
1921
1924
1927
1930
1933


PASSENGER CARS
Yearly: 1918-1929
millions
4.5
4
3.5
3
2.5
2
1.5
1
0.5
0
1918
1925


Changes in N.Y. Fed Discount Rate
1924
Rate of Interest in %
3.5
3
2.5
2
1.5
1
0.5
0
J

cord high at the end of April of 1.6 billion gallons. Gasoline prices started to drop and undercutting took place in the Midwest as well as on the East Coast. The oil stocks became hard hit going into early June.

Up to 1924, the interest rates in the United States had, by and large, been higher. But after the Fed lowered the discount rate to 3.5% in June 1924, the U.S. emerged as the lowest interest rate market. This was interpreted much differently at that time than we would interpret such an event today. Time magazine put it very well on June 30 in their comments as follows:

"Usually London, as the former financial center of the world, has been able to maintain the lowest money rates, while New York rates have ruled far above."

In those days, the higher the rate of interest a nation paid, the less of a credit rating it maintained within the international community. Money was pouring into the United States as nervous Europeans looked upon America as the land with streets paved in gold. Industry was expanding, innovation was abundant, and from their eyes the U.S. was the place to be. As foreign capital flooded into the United States, the interest rates continued to drop to the point where call money rates reached 2%.

In 1924, foreign capital was pouring into the U.S. while the discount rate had been declining steadily since 1920. Around the world the official discount rates stood at the end of June 1924 as follows:

Austria.................. 12.0%
Belgium....................5.5%
Bulgaria....................7.0%
Czechoslovakia........6.0%
Denmark..................7.0%
England....................4.0%
France.......................6.0%
Germany.................10.0%
Greece......................7.5%
Hungary..................18.5%
India..........................7.0%
Italy...........................5.5%
Japan........................ 8.0%
Holland................... 5.0%
Norway..................... 7.0%
Poland.................... 12.0%
Portugal....................9.0%
Rumania...................6.0%
South Africa............ 6.0%
Spain.........................5.0%
Sweden.....................5.5%
Switzerland..............4.0%
United States..........3.5%

The stock market began to rise sharply by the end of June and during July the upward trend continued. By and large, everyone remained confused and began to suggest that the rally was due to the decline in interest rates. But the true cause was the influx of a 44% rise in the U.S. trade surplus.

In the July 7, 1924 edition of Time magazine, this attitude was expressed: "Wall Street, however, after several months of an uninteresting experience with meaninglessly see-sawing prices, is now getting the old-fashioned thrill that only a sudden decline in interest rates can give. Bonds and stocks with fixed or certain dividends are making new highs daily. Yet, on the basis that it takes something more than cheap money to produce rising markets and prosperity, investors are still gun-shy of industrial stocks for the most part. The Great God Livermore has yet to declare himself convinced that the turn in the Industrials has come. But it is too much to believe that the speculative leader is unaware of the soaring investment markets, or that he has not profited somewhat thereby."

What was taking place was still the two fold play. First, foreign investment seeking dollar safety entered the market looking for higher dividend paying stocks. Many industrials were still paying a 4% to 7% dividend and with call money at 2%, they were looking at a hard-core fixed profit. This dividend play in the face of cheap money also attracted the small investor ahead of the so-called knowledgeable investor. What only hindsight would reveal was the hidden truth that the schlep on the street sometimes knows more than the man in the back seat of the limousine.

Although money was cheap, it hadn't yet broken all-time record lows which had been established at 1.55 back in 1894. Yet the 2% level matched the low which had been established prior to World War I during June 1914. Speculation then began to circulate that the Fed was going to cut the discount rate again to 3% and the buying fever continued, reaching a high during mid-August of 1924 before any setback would come.

Nonetheless, just in the midst of the early weeks of August before the high came into play, U.S. Steel once again announced a surprise extra dividend, but this time an extra 1/2 point or 50 cents. Although the earnings of U.S. Steel did decline from $50 million during the first quarter of 1924, the second quarter was still $41.3 million. This meant that U.S. Steel earnings for the first half of 1924 were $8.47 per share which was still another record.

Most analysts today perceive lower rates of interest as bullish and higher as bearish. Some would point to this June discount rate cut and assert that it was the fundamental reason why the market rallied. But this would be proven incorrect in the months and years that followed. The importance of this discount rate cut is that it was bullish only because the call money rate and long-term rates were below the dividend yields. Therefore, just as we saw money market funds burst with cash and attract money from the stock market in the early 1980s, in 1924 the stock market was paying more than an interest-bearing account and as such rallied as capital flow turned positive. Capital, even domestically, will flow to the highest bidder and in 1924 it was the stock market.

Then it came. On Thursday, August 7, the Fed cut the discount rate to 3% as money simply poured into the U.S. economy in the face of a continued expansion in the U.S. trade surplus. The rising stock market and the impressive earnings on the part of America's largest corporations lured many foreign investors. But just as the news broke following the earnings and the discount rate cut, the market peaked. After closing August above 105, the market pulled back to eventually dip below 100 moving into October, just prior to the Presidential elections.

The world had come under serious debt pressure due to World War I. The actual amount of gold in the world was far less than the outstanding debt which was owed to the United States and by mid-1924 the U.S. held more than half of the entire official world supply.

South African gold production was reaching a record level of 829,437 ounces in July of 1924 alone. Due to various laws in nations such as Britain, which prohibited the exportation of gold, and due to the premium placed upon gold itself among the debt ridden world, most of the South African new gold production was pouring into the United States. As this continued, money in the U.S. remained easy and relatively cheap. This created much confusion within the analytical sector which served for many as a misinterpreter of the economy. Everyone was used to lower rates during recessions but not during expansion.

Traditionally, it was held that declining interest rates reflected a lower demand for money and subsequently it was regarded as a sign of recession. But at the same time, interest rates which became too high were seen as inflationary, robbing industry of profits. Therefore, it was consistent under the current interpretation of interest rates within that atmosphere for Livermore to point out that the stock market had risen previously on higher rates and not with lower rates. Subsequently, even the famous Jesse Livermore became confused by the declining rate during the summer of 1924 and he indeed missed the rally along with most other professionals.

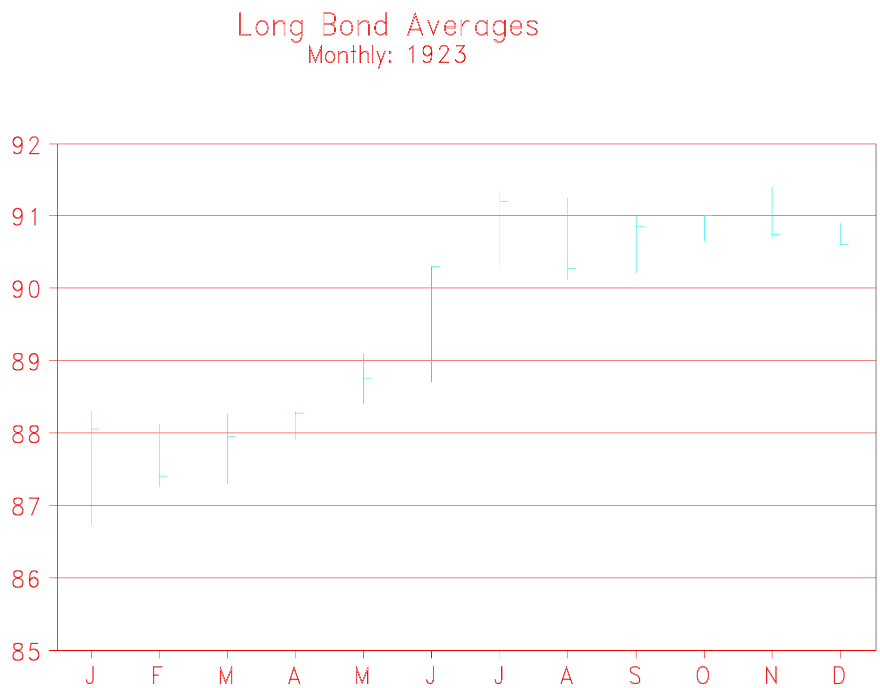
As the market came into its bottom prior to the Presidential elections, money remained easy but call money rates began to rise for the first time that year. Call money suddenly rose from 2% to 2.5%. Gold imports began to ease off sharply as India began to attract the precious metals. Yet foreign loans were increasingly being floated in New York as the world came knocking on the U.S. door for money. This was one primary factor for the rise in the call money rate during October 1924.

The winter and spring had already been fairly cold and damp. When it came to the wheat harvest in the fall the rains continued in Europe and became very destructive, forcing wheat up to $1.50 on the futures in Chicago.

After the August high, the market traded down through a consolidation phase for two months coinciding precisely with the last drop in the discount rate. But the consolidation had reached bottom, barely penetrating below the 100 level during October. In the final throws of October, the market rallied back and closed at 104. Suddenly, from the opening bell in November, traders scrambled nearly buckling under the pressure of huge volume which had not been seen since the pre-1920 years.

Then the stock market took off in one of the most straight up moves it had ever made. Immediately the press jumped on the move, interviewing everyone trying to find out what was really going on. The consensus narrowed the reasons down to three: 1) The election of President Coolidge; 2) Coolidge's lack of action against the railroads to restrain laws which would break them up; 3) Britain had come close to socialism yet in the nick of time veered away and elected a Conservative government. These were the main occurrences reported as the influencing force which encouraged the masses to buy. Although these were logical reasons to the experienced trader in an attempt to interpret the actions of the unsophisticated investor, again they missed the important aspects which made sense to the little guy. If U.S. Steel is paying 7% and the bank 3%, you had to be crazy not to buy U.S. Steel. This led the common masses into the stock market as never before in the face of declining income on time deposits at the banks.

Brokerage houses were reporting that private individuals who hadn't invested in the market since the war had suddenly decided that business conditions were sound. The rally was led by the rails with new highs for the year being scored across the board. Volume soared to near record levels trading 2 million shares a day.



It was in November that call money rates fell back to 2% again but this time some foreign capital was leaving New York in favor of Europe. The "Expert's Plan" had been adopted and everyone turned their eyes toward Europe assuming that a robust recovery was at last at hand. In anticipation of that, N.Y. banks began to lend overseas to various industries. The London stock market began to rally and sterling at last began to firm, approaching the pre-war level coming close to par. By November all the press had turned from doom and gloom and pronounced that the signs now pointed the way to prosperity moving into the spring of 1925.

Many infrequently traded stocks suddenly appeared on the ticker tape. During the week of November 10, 689 different stocks traded and in the ten post- election days 18,717,732 shares had changed hands, which was a record since 1901. The total appreciation in the value of the entire exchange was nearly $3 billion with an average advance of 5 points.

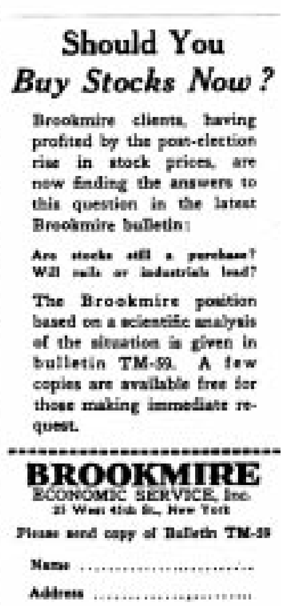
The ticker was twenty minutes behind and the press announced that it was the "public's market." By early December the market still soared; advances were simply all over the place. Time magazine had this to comment:

"The stock market has continued to prove the most active spot in business. Volume has been continuing at about an average of 2 million shares a day, with rising prices in both rails and industrials. Liberty bonds, on the other hand, have been stationary or weak- another normal sign of a good sized 'bull market.'"

Again, the commentary at that time was strikingly different from what we would expect today. Here, Time magazine clearly states that declining bonds and rising stocks were the true sign of a good bull market. As long as interest rates are relatively higher than dividends, the bias will be toward bonds. But if rates are under dividends, the bias swings toward the stock market. The strong rally into the end of 1924 was reflective of capital leaving the bond market and flooding into the equity markets. This is an important insight which has been seriously lost in recent years.

Another important insight into this market has been misinterpreted by many who have written only about the Crash of 1929. The picture that has been painted is one in which the masses were recklessly over-margined, borrowing everything they could to buy stocks. We will take a look at that period when it comes into play later during 1928. However, the initial raging bull market which took off from the October low in 1924 was strikingly different from what most of us would have expected.

Time magazine reported: "One remarkable feature of the recent market activity has been the stationary status of broker's loans. Usually, as stock prices rise, Investors sell out to speculators who buy 'on margin,' thus occasioning a rise in the amount of money borrowed by stockbrokers at the banks. No official figures on broker's loans are kept, but fairly reliable estimates indicate that recently no advance has occurred in their amounts."



The stock market was rising not on margined speculation but on solid investment. As reported by Time magazine in December: "Public investment in real estate has been on a decline." Cash was flowing from both the bond and real estate markets directly into the stock market for full cash purchases. This signaled not speculation, but massive investment due to rising confidence in the private industrial sector of the United States. The U.S. trade surplus with Europe would stand at a 44% gain over 1923 by year end.

On December 15, 1924, Time Magazine reported as follows:

"On the Stock Exchange, heavy volumes in trading continue, along with a continued although somewhat irregular advance in prices. As yet, no signs of security inflation have appeared except in a minor way. Broker's loans are stationary and purchasing is still largely for cash. Declarations of new dividends, especially among the weaker railroads, already go to show that the autumn's 'bull market' has not been a merely speculative movement, but caused by fundamental economic reasons.

"The real puzzle is with industrial securities. They have appreciated along with the rails, but more uncertainly and subject to larger reactions. Moreover, securities of different industries have behaved quite differently. Industrial news continues to become more encouraging."

Indeed, the commentary during December 1924 sounded universally bewildered by the substantial appreciation in the industrials. Normally, the railroads had been viewed as the bulwark within the overall market. Railroads had been the rage of the 1907 period but by the 1920s they had gained a more conservative perspective. The industrials had now become the speculative issues. For example, during 1921 the railroads bottomed during June at the mid-65 level. The industrials continued lower into August reaching 64 on the Index. The railroads rallied reaching 94 during September 1922, whereas the industrials continued to lag, eventually reaching 103 by December. The railroads therefore bottomed in advance and peaked in advance of the industrials. Even during 1923, when the industrials reached their lowest point during October, the rails had already bottomed during June and were in a moderate uptrend into year end. During early 1924, the industrials fell from their February high into the May low correcting by merely 14% while the rails traded sideways between 83 and 80, which was less than a 4% correction from a January high.

Between June and December 1924, the rail rallied from 82 to 99 while the industrials rallied from 89 to 121. The rails lost their leadership and from this moment on, the Dow Jones Industrial Index would begin to assert a more prominent role. The "puzzle" with which the analytical world was faced was a loss of their leading indicator.

Eventually, this change in leadership between the rails and the industrials was another milestone unto itself. It reflected the fundamental change in the perception of the American economy. At last America had entered the true industrial age where innovation, ingenuity and determination would change the course of history. In the years to come, the industrials left the realm of speculative issues and entered into the world of investments. Even in the years ahead the slow death of the rails was not easily foreseeable. Yet in 1932, the rails had fallen 95% while the industrials had declined by 88%. Perhaps not that much of a difference, but a subtle enough one that pointed to the slow death through the decades to come. The rails eventually evolved into today's Transportation Index.

The big news hit in December. Gold started to flow out of the U.S. and back to Europe. The British pound, which had reached $4.70 in February 1923, fell in January 1924 to $4.27. The pound had continued to rally and although still below par, which was $4.76 at that time, it had reached $4.73 in December of 1924. The European recovery was steaming along spurred onward by the loans extended to it by the New York banks. Suddenly, the outflow of gold from N.Y. caused many to buy even more stocks, proclaiming that fears of a gold inflationary period were over.

Indeed, the gold exports were something to write about. In one day J.P. Morgan & Co. sent $5 million in gold coin to the German Reichsbank. Although this was viewed as a means to stem potential inflation, the truth of the matter, when looked at closely, revealed that even though this single shipment was greater than all the gold payments from the U.S. to Germany in a ten year period, it was still merely a payment due them on account of their borrowings of $110 million. The gold exports received headlines and were proclaimed as a sign that a gold inflationary wave was out of the question, but they were, in fact, merely gold loans to Europe.

Strangely enough, these very words of the pessimists were turned against them. Those who had continued to point to rising gold reserves and declining rates as a warning of future depression gave rise to this burst of investment as gold began to flow out of the States. It did not matter that it was largely due to loans. No one seems to have analyzed such cash flows in a detailed posture in those days. The analysis was 100% domestically oriented. Yet, the other signs that the pessimist used in his arguments were drawn from the depressed state of the world at large. Now with the so-called "Exports Plan" to rebuild Europe, even this fundamental turned against the pessimist.

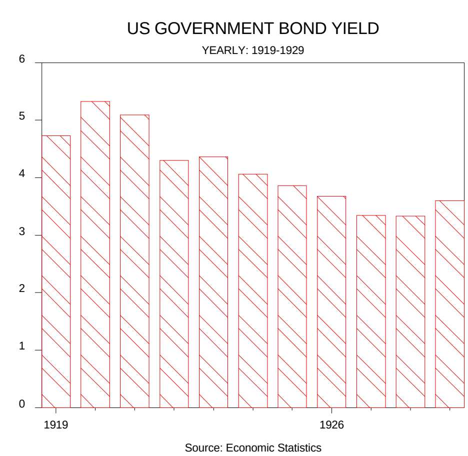
Nonetheless, the fact that on a domestic level people were pouring their cash into the stock market and not into real estate or bonds was not truly reflective of the bond offerings themselves. The following is a list of the bond offerings sold in the U.S. between 1921 and 1924:

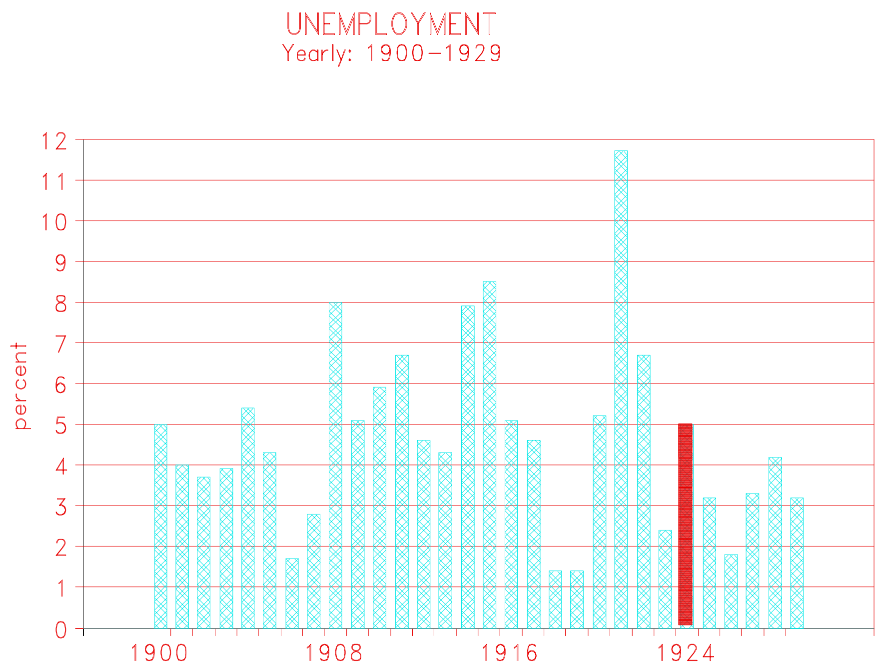
1921........ $2,145,406,132
1922........ $1,675,131,561
1923........ $1,608,595,788
1924........ $2,127,823,688

Although cash was generally leaving the bond market, 1924 was still a record year for bond issues, nearly reaching the 1921 level. But there was a noted and distinct difference in 1924 compared to the previous years. The total sales of bonds this year included state and municipals which had not been the case before. Prior years were largely federal and corporate but in 1924 the states began to borrow much more heavily as well. Foreign capital had still been absorbing much of the bond issues during this period, but with the recovery boom in Europe, this began to slacken as well. The biggest buyers of the bonds domestically were the banks and not the public.

As 1924 drew to an end, call money rates jumped from 2% to 4% in one month. Granted, this may appear to be a sudden and sharp rise, but the stock market continued higher and closed the year on the high above 120 on the Dow Jones Industrials. The disruption of the financial markets was caused by a tremendous amount of payments which came due from many places at once. The British had to make a $68.5 million interest payment and a $23 million principal payment on their war debt to the U.S. The final income tax payment for 1923 was due in December at that time and the U.S. government 4% bonds were sold to subscribers.

Even though the call money rate doubled in one month, at such times in the past it was not unheard of to see the rate swing nearly three to four times during such periods. Therefore, the mere fact that the rate had only doubled was a bullish sign for the market and illustrated that the great American Financial System was sound and capable of handling huge transactions of record proportions. Therefore, in the face of doubling the brokers loan rates in a single month, the market pushed ever higher because sales are still largely for cash. Second, higher rates reflected higher demand and, as previously stated, the analysis of that time was based on the awareness that depression and declining rates had always gone hand in hand.

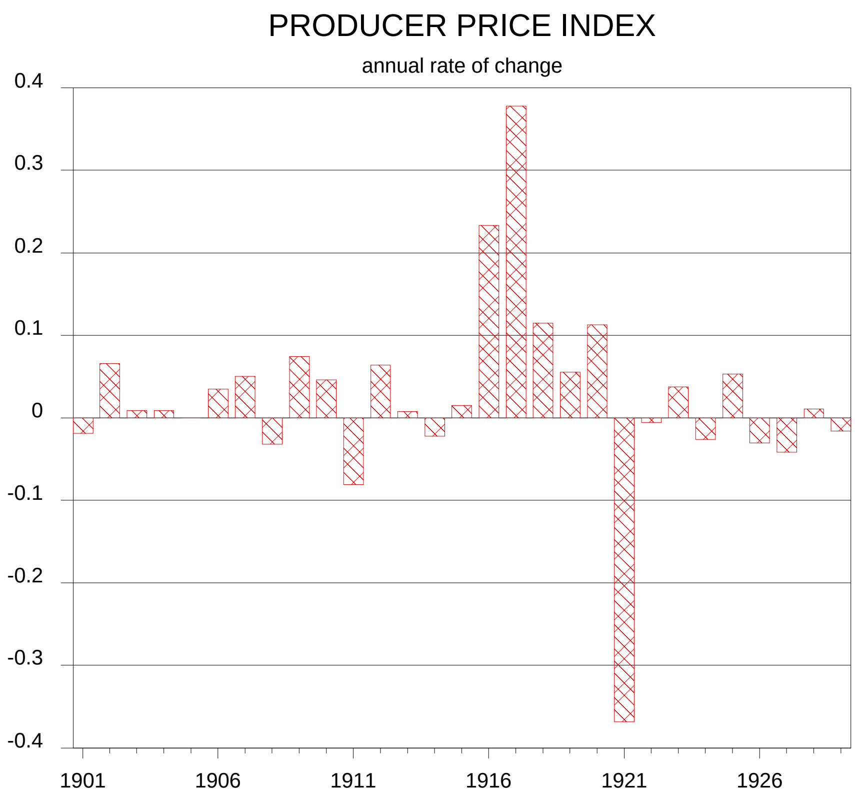


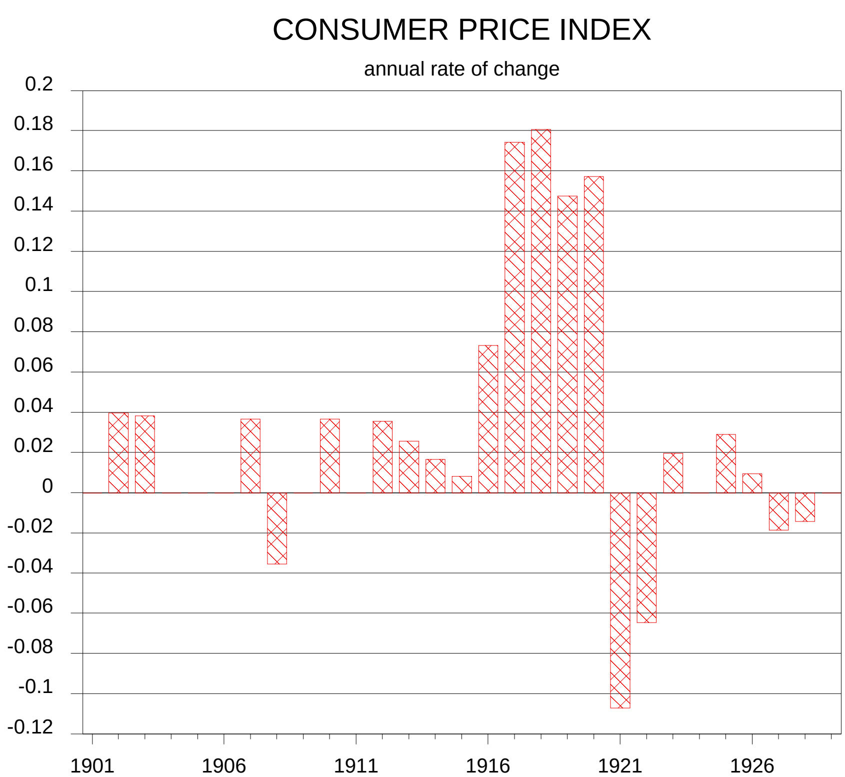


In retrospect, the bond market was neither the mirror image nor the companion of the stock market during the early 1920s. The bonds had collapsed during the depression of 1920 and bottomed as rates began to decline in 1921. But contrary to what most people would assume, again based upon the mere fact that the U.S. had never defaulted on a Federal Bond issue, the bonds were killed at the end of 1921. With huge defaults and excessive European debt coupled with large outstanding corporate issues, bonds remained plentiful.

But as the world sorted out its economic woes, U.S. federal and corporate bonds rallied sharply from 75 on the Dow Jones Index up to slightly above 92 during September 1922. From that point onward, despite declining rates, the bonds fell back, dipping below 86 by March 1923. For thirteen months the bonds traded sideways while the stocks rallied. A trading range between 88 and 86 had become well established. Finally in May 1924 the bonds rallied as call money rates began to approach 2% which proved to be a six year low. The first discount rate cut by the Fed in June caused the bonds to explode, reaching back above the 90 level. In July, the trend continued as the bonds reached above 91. But in August a clear and decisive divergence revealed something that would set the tone for the next five years. When the August 7, 1924 discount rate cut to 3% took place, the bonds were unable to rally and instead fell one full point without even exceeding the July high. While the bonds became paralyzed for the balance of the year, the stock market soared from a low in October of 99 to nearly 121 by year end. The vote was in. Capital, both large and small, was rushing into the stock market when it was clear that dividends were far greater than bond yields.

Taxation rose during 1924 as well. Forty-six states imposed what was called the "Inheritance Taxes." This would be followed by Federal government taxes the next year, in addition to state taxes. This was one of the first underlying factors which would bring inflation back as government on both federal and local levels grabbed for more


PRODUCER PRICE INDEX
annual rate of change
0.4
0.3
0.2
0.1
0
-0.1
-0.2
-0.3
-0.4
1901
1906
1911
1916
1921
1926


CONSUMER PRICE INDEX
annual rate of change
0.2
0.18
0.16
0.14
0.12
0.1
0.08
0.06
0.04
0.02
0
-0.02
-0.04
-0.06
-0.08
-0.1
-0.12
1901
1906
1911
1916
1921
1926

money and eventually forced upon industry a higher cost in labor.

The claims made earlier against Jesse Livermore by the pessimists stated that he had manipulated not merely the summer rally, but the exorbitant rally in the price of wheat just to get Coolidge elected. Those charges were obviously proved false by the stock market's broad rally at year end. But in addition, wheat, which had touched $1.50 earlier, had now passed the $1.75 level moving into year end, and the prospects for another cold winter had the bulls calling for $2 in 1925.

The year 1924 proved to be the beginning of a broad bull market sparked by investors and not by over margined speculators. Business conditions were sound and corporate earnings as well as dividend yields stood at record levels.

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