Edward D. Jones & Co.

Member New York Stock Exchange, Inc. and Securities Investor Protection Corporation

TESTIMONY OF

JOHN W. BACHMANN, MANAGING PRINCIPAL
EDWARD D. JONES & CO.

CAPITAL MARKETS COMPETITION, STABILITY,
AND
FAIRNESS ACT OF 1990

BEFORE THE UNITED STATES SENATE
COMMITTEE ON BANKING,
HOUSING, AND URBAN AFFAIRS

JULY 11, 1990

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Testimony of

John W. Bachmann
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Before the
U.S. Senate Banking Committee
July 11, 1990

Mr. Chairman, I appreciate the opportunity to appear before this Committee to present the views of Edward D. Jones & Co., and more importantly, to communicate to you the viewpoint of our customer constituency regarding financial regulation and jurisdictional issues.

By way of background, Edward D. Jones & Co. is a stock brokerage firm and it is a member of the New York Stock Exchange. We have 1,600 branch locations from coast-to-coast, but our offices are primarily located in the mid-western states with more than half in communities of under 30,000 population. As I relay to you the convictions of our clients, you should understand that our firm does not deal with institutions nor does it cater to wealthy clients with large portfolios. On the contrary, we work strictly with individual investors, generally of moderate means. More than any other firm, we are the broker to rural America. Although our firm is on the opposite end of the spectrum of the New York firms dealing with enormous institutions with sophisticated trading techniques, we believe that nonetheless it is appropriate for us to acquaint you with the viewpoint of individual investors because, in fact, we are one of only five firms in the entire securities industry to have over one million active customer accounts. Moreover, in January of 1987 I became Chairman of the Securities Industry Association and was serving in that office when the market break of 1987 occurred. Because of the intense aftermath scrutiny, I served as Chairman a second year to provide continuity to the process of studies and hearings that followed, and have remained vitally concerned with these issues to date.

In recent years, it has become apparent that individual investors are deeply troubled with the current state of the financial market. Although we tend to visualize a marketplace today dominated by institutions, in fact individuals own directly 60% of stocks in America. They are the investors so vital to our deteriorating capital formation ability in this country. Individuals tend to truly buy for long-term investment purposes as opposed to institutions with their penchant for short term trading. We simply dare not let the current state of the markets continue to justifiably frighten these individual's savings away from American industry. Our market research together with informal feedback from these clients has made us aware that their primary fear focuses on the recent incredible volatility in financial markets. Frankly, we've detected an alarming fear never previously expressed by these individuals when discussing America's greatest blue chip corporations stemming from their trepidation about market volatility. For example, last week in response to some market research, we consistently heard a theme of being "...afraid to invest in America." The comments of a Virginia farmer were typical when he said the only stock he would invest in was livestock because at least he could eat it if the price dropped dramatically. A Wisconsin dairy farmer told us, "...The market is getting jerked around. How can somebody like me be treated fairly when the market is going from one extreme to another. If milk prices were this way, I wouldn't farm."

The volatility which is driving investors from the markets goes beyond the traditional measures of volatility, i.e. price changes from day-to-day. A new and sometimes vicious variation of volatility occasionally whipsaws our markets - intra-day volatility which witnesses the market rise or fall 100 or more points in a matter of minutes. Although the market may end unchanged by the close, the wild intra-day swings unsettle even the most seasoned investor. And frankly, it has considerably frightened the average investor. There is a direct relationship between the use of stock index futures and the intra-day volatility of the stock market. Several studies have demonstrated this relationship.

As an organization directly tuned to the opinion of such individual investors, we know that their confidence in our securities markets is extremely low. It is vital that this confidence be restored. In our opinion, we do believe there is a relationship between stock index futures (and options thereon) and this intra-day volatility. We simply cannot afford to ignore the concerns of the investing public and this nation's responsibility to insure the integrity of the securities markets. In addressing this problem, we find that having differing regulators serving generally different constituencies with varying regulatory frameworks has become obsolete due to the recent proliferation of new derivative financial instruments. There exists a regulatory gap evolving from inadequacy of coordination on the regulatory effort. I am here today to urge you to plug this gap. In essence, we seek legislation to grant a single regulator oversight authority and responsibility for all equity-related products. Similarly, we believe this sole regulator should have authority for setting forth margin policies on these equity-related products. It is our conviction that establishing the Securities and Exchange Commission as this regulator will make great strides in restoring investor confidence in our markets and, hopefully, lead to a more uniform, streamlined and improved regulatory framework for assuring the integrity of the securities markets. These recommendations are not new and have been endorsed in one form or another by the majority of industry and government groups which have devoted much time and effort to study the issue, including; the Presidential Task Force on Market Mechanisms; the U.S. Treasury, the Securities & Exchange Commission; the Federal Reserve Board, the New York Stock Exchange's Blue Ribbon Panel, the Securities Industry Association; major securities firms including those who are some of the principal participants in both the securities and futures markets as well as members of the House and Senate, some present today.

In 1988, during my tenure as Chairman of the Securities Industry Association, when meeting with various groups involved with studying the market break and attempting to mend the markets, I was struck by one overriding concept. There was unanimous agreement among these groups of regulators, exchanges and elected officials, that if one were starting today from scratch to develop a regulatory framework in this area, it would not resemble today's system. Clearly, if equity index futures had existed alongside agricultural commodity contracts in the formative years of today's regulation, we would have recognized from the outset the mistake in lumping stock market related products with agricultural instruments. Our current bifurcated system is obsolete and it is dangerous to permit it to continue. We urgently need a single regulator for all equity-related products. In our opinion, we should appoint the SEC to this role as it is looked upon as the ultimate force for public protection of the equity markets and investors since its establishment in 1934.

We have been apprised that there is a conflict between the SEC and the CFTC in what some have characterized as a jurisdictional land-grab in this area. Once again, based upon our experience in having been directly regulated by both entities, it is our opinion that the Securities and Exchange Commission is a preferable regulatory choice for this legislative thrust. Although both are competent agencies, the SEC's historical expertise in equity and equity-related products makes them the logical choice. We have heard arguments raised that in rural areas, farmers are purportedly more familiar with the work of the CFTC and that they would be the favored regulator. However, our dialogue with farmers and other individuals living in rural communities simply fails to confirm this notion. We have found no appreciable level of support among rural investors for CFTC jurisdiction or any preference for the CFTC over the SEC within this constituency. A recent conversation with a client in Kentucky is instructive when he indicated his familiarity with the CFTC through his farming livelihood, but is familiar with the SEC through his investments. In essence, we believe that the CFTC should regulate non equity related commodities, but that the SEC needs to be in charge of products related to the stock market. Such a move will not be disruptive to the CFTC because stock index futures constitute only 5% of the futures contracts under their jurisdiction.

In summary, our customers inherently understand that a sensible step in solving their deep-rooted fears over the volatility in the securities market is the designation of a single regulator. They sense that stock index futures are more clearly tied to the equity markets than traditional commodity contracts drawn upon pure agricultural products. Accordingly, they look to the entity having the greatest experience and best track record in dealing with equity-related securities as the logical choice as the regulator.

In my opinion, these changes will ultimately happen whether in current legislation or in the aftermath of another market disaster. I can only express my hope that you are prepared to make the necessary remedial changes now rather than wait for another market panic with the accompanying devastating results to prove their necessity.

I appreciate the opportunity to provide this Committee with the input of our firm and more importantly, to relay to you the predominant sentiment we hear from our individual customers including those from the rural areas we serve. Thank you for the opportunity to appear before you today and I look forward to providing you with any further information in the future you might request on these issues.

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Attachments

| IR NAME | BR & IR # | COMMENTS |
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| Ken Surber<br>Harrisonburg, VA | 267628 | Had a farmer in '87 that said the only stock he was going to invest in was livestock. At least he could eat it if the price dropped dramatically. All my farm relatives and friends in the Midwest have said many times that they would prefer the futures markets, not mess in their markets either. |
| Bob Greenly<br>Alliance, OH. | 446530 | Had a very active client who has not traded since the UAL fiasco in October. He was thinking of buying UAL, but when he saw the wide fluctuations, he said, "This is no place for small potatoes like me". You might be interested to know that his net worth is over $600,000. Many people are saving with a very low interest savings accounts, which puts a burden on social security and other programs. |
| Tom Thompson<br>Hardy, AR. | 728919 | There are several occasions that there were too many 'Gamblers now in the market which created too much volatility.' The crash of '87 only intensified the belief. Frankly my client is petrified of the NYSE gyrations. Many of my other clients are retired and simply will not subject themselves to periodical 50 point gyrations in one day. Any thing that can be done to return some stability, even if its just in their minds will be welcome. |

| IR NAME | BR & IR # | COMMENTS |
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| Bob Harter<br>Rochelle, IL. | 605345 | All my life I've bought/sold stock, but when you get moves of 30 and 500 points in one day, it's ridiculous, (It used to be 10-15 points.) There is feelings that if you buy one day, you could wipe yourself out the next. This man has always bought good, high quality blue chips, but has been scared out since '87. |
| Bill Haeffner<br>Lodi, CA. | 840522 | 1. Bud feels that the market is not safe enough to invest in now. Until the market stabilizes he will not invest into equities. He will only deposit funds in banks in insured accounts for 80% of the money he controls, the rest in tax free bonds.<br><br>2. My decision to only go with fixed CD.'s and money market accounts was based on the inherent inability of the government to regulate the stock market shown by the inability to come to some grips with undue market volatility. They were afraid to put their money at risk.<br><br>3. Had clients that used to buy utility stock, but after October '87, they have not bought one stock. Because of market volatility, they want to be able to liquidate at any sign of inflation and higher interest rates. They have lost confidence in the government's ability to run the countries economy and has irresponsible for creating this high bill to pass on to their grandkids. |

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| | | 4. It was agreed that the volatility and market being so high at the time of liquidation of 3 1/2 million worth of stocks made them feel that to take the bird in the hand now would be a better move than waiting on an insecure and scary market for 8 months. His cash has been sitting in a DPTC account and will not move it into the market because he feels that now is not the time to be investing, even since before he was nearly fully invested. |
| Charles Pockras Circleville, OH. | 431431 | Had a client that invested for 25+ years sell most of her Coca-Cola stock because of October '87 and '89. In January she did purchase a global bond fund. She perceived this to be less volatile and diversifying outside of the U.S. This is the kind of long-term conservative investor that volatility is spooking out of the U.S. market. |
| Ron Covington Blufton, IN. | 987494 | A farmer client said they would like to see the SEC regulate the commodities markets if it will reduce market volatility in the equity markets. Hugh realizes that most of the damage that the market crash of '87 caused, was the result of illegitimate investing techniques and not the result of the market simply being "too high". His inclination was to leave the market. |

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| Arnie Knecht<br>Lancaster, TX | 145908 | Comments heard frequently from farmers. "Damn, farming is enough of a crap shoot these days. I don't need to be shooting dice in the stock market." "if I want to play in a casino, I'll go to Vegas. I don't want to take that kind of risk with my money." By scaring away individual investors, the stock market is seriously threatening long-term investors by encouraging them to keep all their money in short-term instruments. |
| Van Pearcy<br>Midland, TX. | 792464 | My client is overly hesitant to invest in the market because of the huge swings. Feels the "little man", "mom & pops" have no say and no control because only large corporations, government have control. |
| Lief Nelson<br>Topeka, KS. | 981236 | Have a couple of customers who no longer trust the stock market because of volatility, mainly because of October '87 experience. |
| Bob Shillingstad<br>Richland, WA. | 840190 | My clients transferred all of their utility stocks and Washington mutual account to bonds and CD's because of volatility in the market. Bob said over and over that the market is no place for the small investor. He doesn't trust it. |

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| Randy Gershman<br>Marshfield, WI. | 539522 | Dairy farmer said, "The market is getting jerked around, how can somebody like me be treated fairly when the market is going from one extreme to another, If milk prices where this way, I wouldn't farm." |
| Peter Gauthier<br>Plaquemine, LA. | 333772 | A sugarcane farmer hasn't made an equity investment of any kind since '86 because he has no faith in the market. Mainly feels that few are controlling and manipulating stocks to the extent that the small investor has no chance to make any money. |
| Jim Hall<br>Pepper Pike, OH. | 440440 | Because of excess volatility, have no farmers. One customer quit after the '87 crash. |
| Sandy Sarillo<br>Lombard, IL. | 211539 | Since the crash of '87 stocks that involve a commodity or raw material are tough to sell. The clients don't buy because they are afraid of any stock that has to do with a commodity. I only call with "safe" stocks. |
| Mark Bachman<br>Lapeer, MI. | 481170 | 1. My client is in favor of SEC regulation of SIFT. The only money he puts into the stock market is that which he feels he can afford to lose. He doesn't want to take big chances with the market and his very limited stock holdings. |

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| | | 2. A cash crop farmer is in favor of the SEC in charge of the regulation of Stock Index Futures. He is concerned about drastic market fluctuations. He is tempted to sell his stock holdings for fear of large market swings. |
| Bill Edwards<br>Aberdeen, SD. | 573515 | Had a couple invested in Keogh plan and when they heard about October '87, they called to sell out. That was a bitter experience for them. They lost faith in the system, withdrew all their investments, and have essentially stopped investing in America. |
| Cindy Stephens<br>Sulphur Springs, TX. | 758345 | Have a client who after the October '87 disaster moved his money from Colonial Fund to a Money Market Account and will not move back into the market. During reviews with him, he comments that they cannot stand to watch their principal fluctuate so wildly. They are dairy farmers and understand risk, but market volatility has sent them to the sidelines. |
| Mike Fedler<br>Ashtabula, OH. | 443420 | 10-15% of my client base has not gone back in the market, or has thought about it because of negative response. Farmers are not the only ones that have gotten out of the market because of the volatility. |

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| Robin Hovis<br>Millersburg, OH. | 946370 | A local dairyman is very disillusioned with the market volatility. He feels like his money is made a joke of by "Wall Street Smart Alecks" who are not accountable for reckless behavior. |
| John Haley<br>St. Cloud, FL. | 360922 | Farmers are probably the most adamant in their condemnation of the volatility of the markets. Attitudes are hostile and are perceived to be manipulation of the markets by commodity interests attempting to generate personal profits. |
| Donna Bradshaw<br>Hot Springs, AR. | 719260 | One fourth of our clients are staying out of the market right now because of fear of market volatility. |
| David C. Bruns<br>Washington, IA. | 918344 | Had a client who got spooked out of the market by volatility. He said he was fed up with this roller coaster and liquidated his fund shares and put them in a money market account. |
| Wayne Petty<br>Athens, AL. | 363270 | Because of the crash in '87 a second generation farmer sold everything because it scared him out of the market. He intends to stay out for good. |

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| Jack Scott<br>Elizabethtown, KY. | 962418 | 1. The farmers in my area have great animosity toward the Chicago Board of Trade. He does favor stock index futures being governed by the SEC.<br><br>2. Stock index futures trading does not belong in the commodities sector but with SEC. |
| Peter Keay<br>Owosso, MI. | 807227 | Many clients have cashed in their stock and have never returned since to the equity markets. Some comments are: "Its not worth it to me to have my savings and investments seesaw in value so quickly, I'd rather take a lower rate and know my principal is safe." "I don't want to have to go back to work again. It's not worth it to me to potentially loose huge amounts of my savings in one day in the stock market." Volatility of program trades ultimately scared my clients into their current thinking. |

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