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The practice of playing the stock market for relatively short-term gains has now reached such a high level that it tends to give a bad name to capitalism, thus threatening the cornucopia of goods and freedoms which only capitalism can provide. The country would be improved by revision of its income tax law to reduce such activity, instead of treating it as a treasured national resource.

Short-term stockholdings are the norm for take-over arbitrageurs and now-numerous "professional-bad-guy" investors (often called "raiders" by their detractors) who buy stock in quantities sufficient to create or enhance take-over threats and compound their stakes and encourage imitation as they are, more often than not, bought out at a profit either by the threatened corporation or in some forced sell-out of the corporation's entire business. But the largest share of short-term stockholding now occurs in simple super-activity by securities' portfolio managers as each seeks to be better than the others in predicting short-run changes in security prices. As large fees, commissions and other paper-shuffling profits are earned in the course of increased short-term activity, the result is augmentation of a prosperous class of "new capitalists," not at all in the mold of Andrew Carnegie, who tend to do for the reputation of capitalism what the court of Louis XVI did for the reputation of monarchy.

Too much easy money is now being made by too many pie-divider types as distinguished from pie-producer types. This is bound to raise anticapitalistic sentiments as it is increasingly recognized, for instance, (1) that the work of one good dentist does more for general felicity than that of thousands of investment counselors whose clients in aggregate are poorer for their efforts as they try to out-perform one another in hyperactive management of pension fund common stock portfolios, and (2) that most of these investment counselors (and stockbrokers and others who service them) are honorable, energetic, often brilliant people who would be more useful in other employment if not drawn by financial incentives to their present pursuits.

The problem occurs in part because the stock market provides much more than the minimum liquidity necessary to create reasonable cash-in capacity for suppliers of long-term capital to corporations. The extra liquidity entices into play a huge supplemental group — speculators (including pension funds and other institutions with staid names) seeking relatively short-term gains.

Our liquid stock market, sheltered by gentle tax laws, has acquired a Jekyll-and-Hyde character and serves not only as an orderly place for transaction of essential economic business but also as a near-ideal gambling casino. In recent years the casino part, with its great wealth and prominence, fascinating denizens and occasional bonanzas, has drawn in ever-increasing cascades of short-term speculation. Current 100-Million-share days bring to mind the words of Keynes as he looked back at 1929:

> *"Speculators may do no harm as bubbles on a steady stream of enterprise. But the position is serious when enterprise becomes the bubble on the whirlpool of speculation. When the capital development of a country becomes a by-product of the activities of a casino, the job is likely to be ill-done."*

What, if anything, should be done about these developments? How much legalized gambling should our laws encourage, incident to the process of investing in stocks? These are very difficult questions.

One way to address questions of such difficulty is by the "thought experiment" so beloved by Albert Einstein. Suppose the laws were revised to discourage anything but long-term holding of common stock. Assume, as an example, that the income tax rate on any sort of marketable-common-stock-related gain was 70% for *all* non-underwriting holders, including pension funds and charities, with *no* offsets permitted for losses, unless the holding period was at least five years. Would the country be improved?

Although tinkering would be desirable to prevent fringe inequities, it turns out that such tax law revision would be a good thing.

The revision supposed would drastically reduce stock option trading and make the market for common stocks *less* liquid, but liquidity would remain much better than that available for owners of farms or industrial real estate and would be good enough. Commissions on common stock transactions would be higher, but not greatly higher, and would not impede serious long-term investment.

Investment in common stocks would become a little more like real estate investment, or the investment made when Henry Ford received his grubstake. Investment in newly-issued

common stock and common-stock-related securities like convertible debentures would continue, although the first public issues of formerly private companies would create a less liquid after-market, tending to force prices toward levels which would attract serious buyers planning to hold for a long time. Most expansion of business plant would be financed, as it always has been, by retained corporate earnings and borrowings.

The potentiality for crazy, greedy, speculative stock market orgies would probably be reduced. Such orgies are harmful to a country, have recently occurred in Israel, Kuwait and Hong Kong, and can conceivably occur here, as in 1929 or worse.

The "professional-bad-guy" game, on balance not a good thing, would probably be dampened down to some extent from its present frenzy, and what was left would provide more tax revenue.

Long-term thinking would be more dominant, not only in the stock investment process, but also in the corporate management process, as the whirlpool of speculation, decried by Keynes, was reduced. It is contrary to the national interest to have corporate managers as pre-occupied as they now are with short-term records and temporary stock market effects. So pre-occupied, managers cause corporate action too similar to that of politicians voting to effect outcomes in the next election rather than the next generation.

After anti-common-stock-speculation revision of the income tax law, some portion of the nation's best brain power would be diverted from stock speculation into activities such as creation of more efficient retailing or diesel engines. Accumulators of capital would tend to be a little more in the mold of Edwin Land, David Packard and Jack Nicklaus, whose contributions prevent resentment of their good fortune. Aristotle rightly concluded that power should go to people perceived as deserving power, and improvement in the reputation for quality of society's big winners would be desirable.

There is little to lose by shifting tax burdens to favor by a greater extent long-term instead of short-term investment. The present gross excess of short-term investment, if squeezed out, would not be missed by the overwhelming majority of citizens. Pension and endowment funds could easily adapt to purchasing stocks with the same time horizons now used when purchasing real estate and, in aggregate, would be richer for the change. Stockbrokers

can reasonably be required to join independent truck drivers, unionized air line stewardesses, etc., in adjusting to reduced incomes caused by changes made in the laws to improve the economic system. Moreover, even if a little pro-social activity were eliminated along with more massive anti-social activity, that is no real objection. The problem is like that of the cancer surgeon who wisely uses his knife despite the inevitable destruction of a little good tissue with the bad.

With gambling proclivity entrenched in the culture, it would be unwise to try to eliminate all gambling. But it does not follow that gambling-type activity should be subject to subnormal instead of above-normal income tax rates and be intermixed influentially with the capital development of the country. While gains made in long-term common stock investment should be tax-favored as an inducement to saving and eventual transfer of power, gains made in relatively short-term stock investment, in essence mere gambling-type activity, should either be taxed normally, or better yet, be taxed at above-normal rates.

The rewards and penalties of the Internal Revenue Code channel the energies of the citizenry and have a high moral content as they encourage one kind of activity over another. Recently, Congress, at the request of commodity traders and other special interests, has legislated in a manner exactly opposite from right by imposing on a dollar earned in holding a stock index futures contract for ten minutes a tax rate *lower* than is paid on a dollar earned in farming, teaching or night work as a janitor. To the extent the income tax law differs from norms of social value judgment, it becomes less respected, a serious thing when tax collection depends largely on voluntary compliance. The recent legislation impairs what we need, esteem for the tax law, to enhance what we would be better off without, more trading in stock index futures.

The utility of "thought experiment," for lesser mortals as well as Einstein, lies in its capacity to force acceptance of truths which are counter-intuitive. Counter-intuitive as it may be for traditionalists and "free-enterprise" types, the country would work better if the income tax law were revised to deter the short-term speculation and *reduce* liquidity in the stock market. The truly productive part of "free-enterprise" and the security of its future would thereby be both (1) enhanced by increased emphasis on long-term effects of investment accompanied by diversion of talent from speculation to more

useful work and (2) less likely to be damaged by unsound future legislation attributable to public resentment of after-effects of stock market orgies and wasteful proliferation of "new capitalists" who produce too little for what they get.

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