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including Dow Theory principles
by a Wall St. mastermind

THE
B **A**
OF **C**

STOCK

SPECULATION

By S. A. NELSON. Introduced by RICHARD RUSSELL

S. A. NELSON

**THE A
B C
OF STOCK
SPECULATION**

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PREFACE

Following the publication of *The A B C of Wall Street* there were many requests for a book dealing with the principles governing stock speculation. If there is one man better qualified than another to produce such a book that man is Mr. Charles H. Dow. Several attempts were made to have him write the desired volume but they were unavailing. From time to time in his Wall Street career, extending over a quarter of a century, Mr. Dow has carefully evolved his theories of successful stock speculation. They are to be found in Chapters IV to XX, inclusive, and can be commended to any one interested in stock speculation as remarkable for their grasp of a subject about which so little has been written and so much misinformation is gratuitously offered the public. In the preparation of this little volume thanks are also due to the *Wall Street Journal*, the *Evening Post*, the *Dow, Jones & Co.'s News Agency*, Mr. Alexander Dana Noyes, Mr. Daniel Kellogg, Mr. E. W. Harden, and a number of brokers and speculators. The reader of course understands that there is no royal road to success in speculation. It would be fallacy to undertake to show how money can be made. No infallible plan has yet been discovered. Experience and observation when intelligent, however, are valuable, and we are of the opinion that the average speculator will find a study of the following pages to be useful and profitable.

INTRODUCTION

Many years ago a well-to-do uncle of mine died. He left me a modest sum of money. The stock market being "fashionable" at that time, I promptly trotted down to a brokerage office and picked an alert looking broker. The broker told me that "the market was headed up", that the country's future was assured, and that I should put my money into "good common stocks". This I did. Fortunately, I put only one half of my money into common stocks, unfortunately, the market collapsed within about a month's time. I was poorer but not wiser.

However, this experience did start me thinking. The New York Public Library is always an excellent place to engage in thinking, and I used to spend all my spare time in those hallowed halls. In short, I read everything and anything I could find pertaining to the stock market.

I must admit that perhaps 90% of what I read seemed to shed little or no light on why I so quickly lost money in the stock market. I kept reading. It further dawned on me that 90% of what I was reading was pretty much worthless from the standpoint of understanding the stock market. And finally, finally, I came upon a battered loose-leaf volume entitled "Dow Theory Comment". I read this volume from cover to cover. It contained (with the exception of a few missing pages) all the market letters written by one of the great market students, Robert Rhea. Here was a man who electrified Wall Street with his famous service during the 1930's. Here was a man who (right

in his service) "called" the 1932 bottom, the 1937 top and subsequent bear market, and the 1938 rise. What was more, he made it all sound logical. He gave reasons; he, in brief, talked sense.

Scattered through Rhea's writing were constant references to Charles H. Dow, the founder of Dow, Jones & Co., first Editor (and, of course, owner) of the Wall Street Journal. Dow's understudy at the Journal was William P. Hamilton, another brilliant market student. Hamilton carried on after Dow's death, both with Dow's market ideas and with Dow's editorship of the Journal. What Robert Rhea had done was to take Dow's original ideas about the market, together with Hamilton's further additions to Dow's ideas, and build the whole into what we today call Dow's Theory.

If Rhea could put all this together, I thought, then I want to read what Hamilton wrote and what Dow wrote. What Hamilton wrote was not difficult to find. It is all contained in a book entitled "The Stock Market Barometer". Later, I republished this book myself in the interest of market students.

But what Dow wrote -- that was a tough one. Dow wrote for his Wall Street Journal. All his market observations, observations so penetrating and universal that they form the basis of modern technical analysis, were written in the form of editorials for the Journal around the turn of the century. At that time a man named S. A. Nelson was publishing a library of books about Wall Street. Nelson was a great admirer of Dow's and to his everlasting credit, Nelson recognized the historic value of Dow's work. Nelson begged Dow to write a special book on his unique theories of the stock market. But Dow was a reticent man. Fin-

ally, Nelson did get permission to include a number of Dow's Wall Street Journal editorials in a book which Nelson entitled, "The A B C of Stock Speculation".

Chapters IV through XX of this book consist of actual Wall Street Journal editorials by Dow. Note that at the bottom of the first page of these chapters is a little footnote by Nelson saying: "Dow's Theory". Nelson wanted readers to know that these chapters comprised what he, Nelson, considered to be Dow's Theory. The name stuck. The ideas which were originated by Dow, augmented and amplified by Hamilton and Rhea, became known as Dow's Theory. Dow died in 1902. He died before his "Theory" became famous, and before his ideas became widely accepted.

But those ideas are to the stock market, what Freud's ideas are to psychiatry. They form the basis for a whole way of thinking, and they have been built upon, expanded and augmented over the years.

Study this little book, "The A.B.C. of Stock Speculation". You will probably be amazed at how modern most of Dow's observations seem and sound. And be glad you own this book. Had I been fortunate enough to own it many years ago, I probably would have saved most of my first and only inheritance.

Richard Russell
San Diego, California

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THE A B C OF STOCK SPECULATION

CHAPTER I.

ORIGIN OF STOCK BROKERS, STOCK EXCHANGES AND STOCK SPECULATION.

Etymological authorities are not in entire accord respecting the origin of the word "Broker." Jacob's Law Dictionary says: "The etymology of the term Broker has been variously given. By some it has been derived from the Saxon *broc*, misfortune, as denoting a broken trader; the occupation being formerly confined, it is said, to unfortunate persons of that description (Tomlins). According to others it was formed from the French *broieur*, a grinder or breaker into small pieces; a Broker being one who *beats* or draws a bargain into particulars (Termes de la Ley, Cowell). The law Latin from *obrocator*, however, seems to point distinctly to the Saxon *abroecan* (to break), as the true root, which in the old word *abbrochment* (q. v.) or *abroachment*, had the sense of breaking up goods or selling at retail. A Broker, therefore, would seem to have been originally a *retailer*, and hence we find the old word *auctionarius* (q. v.) used in both these senses (Barrill's Law Dict., tit. "Broker"). Wharton gives, as the derivation of the word the French *broceur*, and the Latin *tritor*, a person who breaks into small pieces (Whar. Law Dict.,

tit. "Broker"). Webster gives as its derivation, the old English *brocour*, Norman French *broggour*, French *brocanteur*. Under the word "broke," to deal in second hand goods, to be a Broker, Webster says it is probably derived from the word *brock*. Worcester derives it from the Anglo-Saxon *brucan*, to discharge an office; *brocian*, to oppress; and the French *broyer*, to grind. See "Broke" and "Broker." The word "Broker" seems first to occur in literature in Pier's Ploughman, "Among burgeises have I be Dwellyng at London. And gart Backbiting be a brocour. To blame men's ware." It clearly means here a *fault finder*, as in Provencal *brac* is refuse. The Broker was originally one who inspected goods and rejected what was below the standard (Wedgwood). Crabb's Dig. of Stat., tit. "Brokers," 261, says, "There were a class of persons known to the Romans who were deemed public officers, and who united the functions of bankers, exchangers, Brokers, commissioners and notaries all in one under the description of *proze netae*."

As early as 1285, in England, the term Broker occurs in an Act of Parliament. It enacts that "there shall be no Broker in the city (London), except those who are admitted and sworn before the warden, mayor or aldermen."

John R. Dos Passos, an authority on stock exchange law, says: "The next statute passed in the reign of James the First, more than 300 years later (1604) regulates the calling of Brokers with greater detail than the first act and clearly shows, by the use of the words 'merchandise and wares' that down to this period the Broker in money, stock, and funds had no legal existence. . . . It was

not until the latter part of the seventeenth century, when the East India Company came prominently before the public, that trading or speculating in stock became an established business in England; and the term 'Broker,' which had then a well-understood meaning was promptly transferred to those persons who were employed to buy or sell stocks or shares, and who thenceforth became known as 'stock-brokers.' "

In 1697 owing to the "unjust practices and designs" of Brokers and Stock-jobbers in selling tallies, bank stock, bank bills, shares and interest in joint stock, a stringent act was passed permitting only sworn appointees to act as Brokers. In the reigns of William III., Anne and George, statutes were passed regulating the practice and trade of Brokers.

An early legal writer describing Stockbrokers, said: "Stockbrokers are persons who confine their transactions to the buying and selling of property in the public funds and other securities for money, and they are employed by the proprietors or holders of the said securities. Of late years, owing to the prodigious increase of the funded debt of the nation, commonly called the stock, they are become a very numerous and considerable body, and have built by subscription, a room near the Bank, wherein they meet to transact business with their principals, and with each other; and to prepare and settle their proceedings before they go to the transfer-offices at the Bank, the South Sea and India houses, thereby preventing a great deal of confusion at the public offices, where the concourse of people is so great during the hours of transferring stock that if

the business was not prepared beforehand it would be impossible to transact it within the given time."

The advantage of having a Broker as an intermediary was recognized by merchants many centuries ago. A sixteenth century writer on the law says: "It is an old proverb, and very true, that between *what you will buy?* and *what you will sell?* there is twenty in the hundred differing in the price, which is the cause that all the nations do more effect to sell their commodities with reputation by means of Brokers than we do; for that which seems to be gotten thereby is more than double lost another way. Besides, that by that course many differences are prevented which arise between man and man in their bargains or verbal contracts; for the testimony of a sworn Broker and his book together is sufficient to end the same."

Dealings in Stock certificates constitute the main business of Stock-brokers, but the origin of stock certificates has not been satisfactorily traced beyond the middle of the seventeenth century. Property in this form was not known to the ancient law. While mercantile or commercial corporations existed among the Romans, history gives us no information regarding their character or methods of conduct.

Ang. & Ames on Corporations (10th ed.) Ch. 18, Sec. 26, says: "A *Collegium Mercatorum* existed at Rome 493 B. C., but the modern bourse from the Latin *bursa*, a purse, originated about the fifteenth century. Bourges and Amsterdam contend for the honor of having erected the first bourse."

"The Roman law," says John R. Dos Passos, "required

three persons to organize a corporation; and as each body had at least that number of members, if not more, it would seem but natural that a certificate, or some other substantial muniment of title, should have been issued by the corporation to its respective members, in which the proportion of interest of each in the capital or corporate property of the association appeared. But whether a certificate was, in fact, issued, and, if so, was regarded as property capable of sale or other negotiation, and of vesting in the representatives of the owner, on his decease, or whether the corporations were all of the nature of guilds conferring upon the members mere *personal* rights—all of these questions seem now to be incapable of solution; and the Roman law, which sheds such floods of light upon commercial subjects apparently leaves the above matters in total darkness.”

In England, in 1770, Lord Mansfield in a case wherein it was contended that stock certificates were *money* decided against that view, saying: “This is a *new* species of property *arisen within the compass of a few years*. It is not money.”

The Stock Exchange or Bourse in its present use is a modern creation. Brokers and dealers in stocks and merchandise dealt together in an exchange in Cornhill, London, in 1670, or thereabouts. In 1698, the Stock-brokers of London obtained quarters for their exclusive use.

The first Stock Exchange formed in the United States was that of Philadelphia, where a Board of Stock-brokers formally organized and adopted a constitution in the early part of the eighteenth century.

The New York Stock Exchange, framed on the plan of the one in Philadelphia, was organized in 1817, but curiously enough this institution is in possession of a document bearing date May 17, 1792, signed by a number of Brokers, in which it is stated: "We, the subscribers, Brokers for the purchase and sale of public business, agree to do business at not less than one-fourth of one per cent."

Medberry, in his "Men and Mysteries of Wall Street," describes early stock speculation in this country as follows: . . . "When Washington was President, and Continental money was worth a trifle more as currency than as waste paper, some twenty New York dealers in public stock met together in a Broker's office and signed their names in the bold, strong hand of their generation, to an agreement of the nature of a protective league. The date of this paper is May 17, 1792. The volume of business of all these primitive New York Brokers could not have been much above that of even the poorest first-class Wall Street house in our time (1870). The Revolutionary shipplasters, as the irreverent already styled them, were spread over the land in such plenty that there were \$100 to each inhabitant. Something was to be made, therefore, from the fluctuations to which they were liable. Indeed, one of the greatest Broker firms of subsequent years derived its capital from the lucky speculations of its senior member in this currency.

"The war of 1812 gave the first genuine impulse to stock speculation. The Government issued sixteen millions in Treasury notes, and put loans amounting to one hundred and nine millions on the market. There were endless

fluctuations and the lazy-going capitalists of the time managed to gain or lose handsome fortunes. Bank stock was also a favorite investment. An illustration of one of the sources of money-making to Brokers at this period is found in the fact that United States 6s of 1814 were at 50 in specie and 70 in New York bank currency.

"In 1816 one could count up two hundred banks with a capital of \$82,000,000. . . . One day in 1817, the New York stock dealers met in the room of an associate and voted to send a 'delegate' over on the stage line to investigate the system adopted in the rival city (Philadelphia). The Philadelphia visit was successful; and the draft of a constitution and by-laws, framed from that of the Philadelphia Board, received the final approbation of a sufficient number of Brokers to enable the New York Stock Exchange to become a definite fact. Three years after, on the 21st of February, 1820, this preliminary code of rules received a thorough revision and the organization was strengthened by the accession of some of the heaviest capitalists in the city. Indeed, with 1820, the real history of the Exchange may properly be said to commence."

In Europe stock speculation historically was marked with white stones by the "Tulip Craze," the South Sea Bubble, the John Law inflation in France, and later by the wild speculation in Kaffirs.

In this country for more than half a century stock speculation had its basis in the securities of the steam railroad. It has ebbed and flowed with the promotion, construction, decline, and reorganization of that industry.

In the last decade speculation has been fostered by the

“industrial proposition,” which has resulted in offering to the public shares of industrial corporations. Not an industry has been passed by. Like the railroad the industrial corporation is destined to have its periods of promotion, construction, decline and reorganization. It will not be difficult for the reader to determine which period he has under immediate consideration.