"RELATIONSHIPS, RELATIONSHIPS, RELATIONSHIPS": THE MUTUAL FUND INDUSTRY'S MANTRA FOR SUCCESS FROM THE 1940S THROUGH THE 1960S

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Throughout the 1940s, 1950s, and 1960s, the mutual fund industry grew tremendously. While a strong stock market and Americans' improved confidence in corporate securities facilitated this expansion, the fund industry itself played a crucial role. Fund leaders diligently worked to create strong relationships with the investment dealer community, the main distributor of fund shares. Individually and collectively, mutual fund companies cultivated these relationships by providing dealers with the sales and service support they needed in order to sell shares to millions of Americans.

In the 1940s, the securities industry in the United States still faced substantial difficulties. While the Great Crash had deteriorated many people's confidence in common stocks, government war bonds during World War II also served to divert many investors' attention away from the stock market. Perhaps not surprisingly, on an annual basis for most of the 1940s, individuals withdrew more money from the stock market than they added. According to the Federal Reserve Board's Flow of Funds data, in the period from 1939 to 1947, individuals removed a net total of $4.9 billion from corporate securities.[1] Within this challenged securities world, however, the mutual fund industry[2] fared relatively well. Sales of funds actually grew modestly during this period of weak consumer interest in individual corporate securities. In 1941, the first year the industry began compiling investment company data, mutual funds experienced from share sales net increases in capital of $8.2 million. Between 1941 and 1947, the fund industry experienced gross sales of $1.3 billion and net sales of just over $800 million.[3]

In the 1950s and 1960s, popular interest in both mutual funds and individual securities increased. American consumers began spending their high

levels of savings that they had accumulated during World War II, which in turn bolstered corporate earnings and stock prices. Consumer disposable income continued to increase during the postwar years, while the economy remained healthy and devoid of the rampant inflation many had feared. A bull market, a strong economy, and returning public confidence in securities converged with factors inside the mutual fund industry to increase the pace of expansion that had begun in 1940.

This rapid development generated exceptional growth in fund asset levels and the number of shareholders. Journalists noted the industry's "phenomenal growth" and its position as "the fastest growing, most competitive . . . phenomenon of the U.S. financial world."[4] Between 1940 and 1972, the last year of almost uninterrupted growth, the number of open-end mutual funds (also known as investment companies) increased from 68 to 269. In 1940, fewer than 300,000 accounts existed. By the end of 1971, there were almost 11 million accounts. Though these numbers do not take into consideration multiple accounts held by one person, they still demonstrate substantial growth. Aggregate fund asset levels during the same time period grew from $448 million to almost $60 billion.[5]

Understanding how the industry expanded in the 1940s while much of the investment world struggled, and how it ultimately achieved such tremendous growth by the early 1970s, requires analyzing the mutual fund industry's relationship with the investment dealer community. Despite recent historical studies about the industry's growth, scholars have overlooked the essential role that this relationship played. From the advent of American open-end investment companies in 1924, founders of two out of the three original funds grew their companies by actively selling shares to the public. At the outset, fund leaders generally distributed their shares at retail, meaning through sales representatives associated with the fund. Gradually, however, leaders embraced the wholesale system of distribution, whereby the fund contracted with dealers independent of the fund, who in turn sold the shares to the public. By the late 1930s, more funds preferred this system over retail sales.

The independent dealers worked for New York Stock Exchange member firms and nonmember broker-dealer firms. While open-end investment companies continued to use various distribution channels, by the early 1960s, three-quarters of all mutual funds[6] distributed their shares to the public through independent dealers.[7] Exploring this connection between dealers and funds is essential to understanding the fund industry's growth, and doing so demonstrates that leaders' abilities to build strong relationships with the dealer community were crucial for success. "Invaluable," was how George Putnam, son of Putnam Investments' founder, described these relationships.[8]

Heretofore, when scholars have discussed reasons behind the fund industry's success, they have concentrated on factors instigated by people and events outside the industry — specifically, government regulation and salespeople's marketing techniques. Natalie R. Grow, in her 1977 dissertation,

"The 'Boston-Type Open-End Fund' — Development of a National Financial Institution: 1924-1940," concludes that the Investment Company Act of 1940 was "the cornerstone of the mutual fund industry, marking the beginning of its real growth."[9] The cooperation between leaders of various open-end investment companies that preceded the Act united formerly disparate members of the investment company community who continued to work together for the industry's general well-being and expansion. Matthew P. Fink, in his 2008 book, *The Rise of Mutual Funds: An Insider's View*, agrees with Grow and adds that the Act's rules and guidelines helped instill public confidence that the open-end fund industry had shed some of its dubious practices.[10]

Fink also argues that the Revenue Act of 1936 was the "most important event in mutual fund history," in part because it preserved tax favorable status for open-end investment companies. As Fink explains, prior to the Revenue Act, "The federal income tax law provided a 100 hundred percent exclusion for dividends received by one corporation from another corporation. Therefore, investment companies did not pay any tax on dividends they received from corporations in which they invested." Fink further notes, "Investment companies passed these corporate dividends on to their shareholders, who paid tax as they would on any dividends they received."[11] In 1935, President Roosevelt proposed ending this tax benefit for corporations, which would have severely affected mutual funds. Indeed, fund leaders feared that ending this tax benefit would put them out of business.[12] Smart thinking and tenacious interaction with Capitol Hill earned the open-end fund community an exception to this rule, which became part of the Revenue Act of 1936.[13]

A fund only received this exception, however, provided that it met certain tests. These tests were created to help ensure that the fund operated as an investment company seeking profits for shareholders, rather than as a corporation seeking profits for the directors. The tests also were designed to promote the interests of the shareholder, as a small investor, against unsound money management and the gambling type of behavior that had contributed to the 1929 Crash. One test required diversification, stipulating that fund managers invest no more than 5 percent of the assets in one corporation. Another test inhibited managers from engaging in speculative activity by preventing them from deriving more than 30 percent of the fund's gross income from the sale of securities held for less than three months.[14] Fink asserts that these two tests promoted sound financial management, protecting the mutual funds and shareholders from debilitating losses during difficult markets. In addition, the tax provision gave open-end mutual funds a competitive advantage over closed-end funds because the latter group was not afforded the same preferential treatment until the Revenue Act of 1942.[15]

Though this tax treatment was important to mutual funds, there is no way to know if the mutual fund community would have collapsed had mutual funds not continued to receive tax favorable treatment. Also not certain, but probably safe to say, as Fink does, the tests mandating diversification and

discouraging speculation at least helped prevent disastrous money management, such as had occurred in the 1920s, the 1960s, and in the past decade.[16] While the Revenue Act was significant, given its timing, it may be more accurate to note that it simply supported further industry expansion rather than instigating or shaping the trend. Open-end funds already had begun to expand more than half a decade before the Act was formed or even conceived.[17] Meanwhile, closed-end funds had declined steadily in popularity since 1929 and showed little signs of recovery.[18] Finally, the Act maintained the status quo tax treatment of funds, and therefore, in this sense, it was a neutral force in the fund industry's evolution.

Fink also emphasizes the primacy of the stock market in the industry's rebound, and he credits the markets with enticing individuals into funds. While a reignited market certainly helped, evidence strongly suggests that something more than stock market returns brought people into funds. As previously discussed, during the 1940s, consumers tended to shift away from individual corporate securities, withdrawing more money from the sector than they added. But, as highlighted here, during this same period, people began embracing mutual funds. Though this disparity in consumer behavior flipped for a period of time in the late 1940s and early 1950s, it did not represent a retreat from funds. Between 1947 and 1953, consumers placed $4.2 billion of their savings into individual corporate securities, as opposed to $2.2 billion into mutual funds; after this period, however, households again preferred mutual funds through at least 1972.[19]

Given people's general gravitation toward funds, some factor, or factors, in addition to markets, must have attracted individuals to this vehicle. Janice Traflet, in her 2009 article, "Never Bought, Always Sold: Salesmanship, the Small Investor, and the Early Postwar Surge in Mutual Fund Participation," explores the role of "salesmanship" in the rise of funds' popularity. By exploring various sales tactics used by fund salespeople, she supports the notion that active selling was required for industry growth.[20] Historians have yet to consider, however, what fund companies themselves did to promote their own expansion. Through financial compensation, and sales and service support, they cultivated relationships with the investment dealer community. The former factor — financial compensation — still needs a thorough analysis in order to determine the extent of its contribution to the industry's growth. Evidence strongly suggests, though, that it helped encourage dealers to sell funds over individual securities. During the 1950s and 1960s, mutual funds periodically increased their sales load, most of which went to the dealer as commission, in order to garner sales and remain competitive with other mutual fund complexes. Most funds and many dealers also participated in the longtime business practice of reciprocity, whereby funds placed brokerage business with investment dealers who sold the fund's shares.[21]

How fund companies, both separately and collectively, used sales and service support to create relationships with investment dealers is central to this analysis. Of the three original open-end investment companies, State

Street Investment Corp., founded in 1924, was the exception to the focus upon distribution. State Street's founding partners thought of themselves as money managers rather than salesmen, and thus they focused solely upon the investment management aspect of their new business. For the first three years, trustees sold the fund only to family members, waiting until 1927 to ask others for money. Not until 1932 did the trustees "hire a guy to peddle" shares of their investment company.[22]

On the other hand, from its creation (also in 1924), the trustees of Massachusetts Investment Trust (MIT) prioritized attracting the public to their fund. Trustee Edward G. Leffler was a talented securities salesman with Learoyd, Foster & Co. in Boston, which was owned by the other two MIT trustees, Charles H. Learoyd and Hatherly Foster, Jr. The three men utilized this firm's brokers to sell MIT shares to the public.[23] Leffler's goal was to distribute MIT nationwide, but almost immediately he became discouraged with the other two men's slowness to embrace his vision. Leffler therefore found two other entrepreneurs who shared his vision of widespread distribution — John T. Nightingale, an insurance salesman, and William A. Parker, a stock and bond salesman. Together they created Leffler & Co. on December 13, 1924. The company contracted with MIT to sell its shares to the public, but this arrangement, too, soon disappointed the men. They felt that MIT lacked a commitment to sales, and they disliked MIT's investment policy; the fund owned 120 stocks, which the men felt was too diversified.[24]

On November 23, 1925, Leffler, Nightingale, and Parker, along with George Putnam, organized the country's third open-end investment company, Incorporated Investors, in order to implement their own investment policy and sales convictions.[25] The men changed the name of their retail distribution company to Parker, Putnam & Nightingale, Inc.[26] Because sales to the public were initially weak, Parker and Leffler approached contacts at other brokerage firms hoping to convince them to sell shares of Incorporated Investors. The men had such success with this new approach that by the end of 1926, they abandoned the idea of distributing through retail and committed themselves to wholesaling through already established brokerage houses. The men traveled throughout the country, later hiring others called "wholesalers" to do so, and established selling contracts between Parker, Putnam & Nightingale, Inc. and brokerage firms. The contracts stipulated that, in return for sales of the Incorporated shares, the brokerage firm would receive a predetermined portion of the sales load paid by the shareholder, and the remainder would go to Parker, Putnam, & Nightingale, Inc. MIT soon copied this wholesale method of distribution, though it and most other investment companies during the 1920s still distributed at retail.[27]

By the 1940s, the wholesale distribution system had become the norm, and it continued to be so through the 1960s. Yet this was not the only sales model employed by mutual funds. Two of the largest fund complexes[28] in the 1950s and 1960s, – Hamilton Management Corporation and Investors Diversified Services, Inc. — employed their own salespeople. These individuals only sold

their respective firm's funds, and they were the only sales representatives who did. A minority of funds distributed their shares directly to the public without a sales force of any kind.[29]

After World War II, investment companies were still a relatively new concept for dealers as well as the public. Because dealers were unaccustomed to selling funds, the sale of the product over an individual security required a concerted effort. Some dealers feared that offering clients mutual funds undermined their credibility as investment professionals because it turned the stock selection and management over to someone else. Others felt that the upfront sales load was an unnecessary expense. In order to overcome the community's hesitancy, fund leaders had to provide service and help with sales.

To do this, representatives of fund companies traveled around the country visiting with dealers. Prior to the 1940s, as in the case of Incorporated Investors, these traveling representatives were typically the fund's own directors or trustees and sometimes a small group of wholesalers. In 1936, Massachusetts Distributors, a firm that had been created to distribute shares of MIT, employed six wholesalers across the country, and Parker Corporation (as Parker, Putnam, & Nightingale had been renamed) employed three.[30]

After the Second World War, the use of wholesalers became the norm in order to keep up with increasing competition among investment companies due to the many new entrants and accelerated public interest in mutual funds. Unfortunately, information is unavailable regarding the number of wholesalers for the years between the mid-1930s and the 1960s, but it is clear that MIT's distributor[31] had increased its wholesale force to twenty-one by the mid-1960s, and Parker Corporation's force had grown to twelve.[32] The total number of wholesale representatives employed by twenty of the major funds that distributed through independent dealers ranged from 219 to 242 in the first half of the 1960s.[33] Within their sales territories, which were often extensive areas of the country, these wholesalers visited with dealers in their offices, providing them with basic administrative and marketing support, such as keeping their offices stocked with prospectuses and other marketing pieces, and updating them on a fund's holdings and dividend payments.[34]

The wholesaler's major responsibility was to form relationships with dealers. The story of how American Funds (one of the most widely sold funds by dealers today) and Edward D. Jones & Co. became partners illustrates the importance of the wholesaler's ability to relate to the dealer community. Edward D. Jones & Co, a stock brokerage firm founded in 1922 in St. Louis, Missouri, took pride in providing financial advice to small town communities. In order to service its target clientele more effectively, the firm began in 1955 to establish one person offices in small towns across the Midwest.[35] Until the late 1960s, the firm's brokers sold very few mutual funds because the founder and managing partner, Edward D. Jones, favored individual stocks and directed his brokers accordingly. Mr. Jones passed away in the late 1960s, and his son, Ted Jones, succeeded him at the helm. Graham Holloway, the leading wholesaler

for American Funds, a complex based in Los Angeles, California, saw an opportunity in this leadership change. In 1968, Holloway approached Ted Jones about introducing his brokers to the idea of actively selling American Funds. Ted Jones' initial reaction was, "Don't want you selling any big city ideas to our small town brokers!" Holloway responded, "How about if I could help them sell small town ideas that are right for them and right for their customers?"[36]

The "small-town idea" that was most important to Ted Jones was the "buy and hold" concept of managing money rather than frequent turnover. Although a fund's money managers bought and sold as frequently as necessary to fulfill the fund's stated objective, the mutual fund as a savings vehicle minimized the broker's need to trade. With Jones' permission, Holloway and his fellow wholesalers visited with Edward D. Jones brokers around the region, teaching them about mutual funds, how they minimized the need to trade clients' accounts and fulfilled clients' long-term financial goals. With the work of American's wholesalers, Edward D. Jones & Co. quickly became one of American Funds' largest distributors.[37]

Successful wholesalers effectively showed dealers why mutual funds were attractive to the growing middle-income segment of the population, many of whom lacked market experience.[38] As wholesalers explained, funds were cheaper and easier to own than a similarly diversified portfolio of individual stocks. Wholesalers also aided dealers by helping them with the sales process, providing sales tools and accompanying dealers on sales calls. Wholesalers supplied charts, prepared by their home offices, which showed how inflation could eat away at a portfolio of only bonds. They provided tables that conveyed how the stock market rose over time, even though there were events that periodically shocked the system. Wholesalers also emphasized that dealers interested in capturing the middle-income segment of the population had to be willing to go to workers' homes in the evenings after working hours, a new practice for most stockbrokers.[39]

Just as simplifying a customer's financial portfolio was a goal of dealers, simplifying a dealer's business was a wholesaler's goal. To this end, the wholesaler stressed that a business built on funds was easier for the dealer to manage than a book of many individual stocks; it was easier for the broker to monitor a couple of funds rather than a variety of individual holdings. Moreover, the wholesaler contended, if a fund performed poorly, the fund's manager was at fault, not the broker. This last point is no longer used as a selling point with dealers, but during the 1960s, when dealers feasibly could become familiar with only a few funds and could not easily change between them, this point resonated loudly. In these ways, wholesalers taught dealers that they could widen their prospect pool by focusing on middle-income workers without previous market experience, and funds could help the dealer more easily manage a larger book of business.[40]

The wholesaler also gained favor among dealers by disseminating successful business practices from one dealer to another. A prospecting strategy of investment dealer Robert S. Borovoy is an example of an idea that wholesalers

would have passed among the dealer community. Borovoy sold mutual funds in San Francisco and wanted to pursue a specific segment of the city whose inhabitants were mostly new to the practice of investing in corporate securities. His office was located near Chinatown but, not being Chinese himself, he was initially unable to market to his neighbors. So, Borovoy took a three month Chinese language course, and found, as he hoped, that his ability to communicate with the Chinese-American community garnered him substantial business.[41]

Connecting the dealer to the fund company itself was as important as the relationship between the wholesaler and the dealer. The wholesaler facilitated this connection by serving as a liaison between his investment company's leaders and the brokers. Wholesalers explained to dealers stock transactions and expectations for dividend payments, for example.[42] Wholesalers in turn communicated to their home offices ideas that they heard in the field that could help the fund company attract more shareholders. If another mutual fund company provided a type of marketing piece that dealers found particularly useful on sales calls, a wholesaler sent the piece back to his boss so that it could be reproduced. Fund companies also created new funds according to feedback from the field. During the "go-go years" of the 1960s, brokers expressed their desire for more aggressive funds. Some of Putnam's trustees, especially George Putnam himself, hesitated to start a fund more aggressive than the George Putnam Fund, which was a balance of stocks and bonds. But when they heard dealers say that they sold less Putnam and more shares of other funds because the George Putnam Fund was too conservative, the directors relented and began a fund comprised only of "growth" stocks (the Growth Fund). Such communication effectively allowed leaders of mutual funds and the dealer to work together and bring more people into the market.[43]

Separately from the wholesaler, fund directors themselves found ways to support the broker from the home office. One way was to help brokers find and keep new clients. Putnam's trustees did this in part through their fund's quarterly newsletter, *The Prudent Investor*. In the 1950s, the newsletter published multiple articles reminding shareholders of the value that their investment dealer provided. In the spring of 1952, the newsletter featured an article that emphasized how much the trustees appreciated receiving letters from shareholders who advised their friends to buy shares in the Putnam Fund. However, the trustees suggested that, in addition to referring friends to Putnam Fund more broadly, shareholders should tell "friends *about your investment dealer* and the important part he played in your becoming a shareholder."[44]

In 1955, in another article in *The Prudent Investor*, the Putnam Fund trustees lamented that many people were still unfamiliar with the benefits of stocks and were ignorant about how to find a trustworthy investment adviser for assistance. The article reminded shareholders once again of the importance of referring friends to their adviser because not enough dealers went "door to door like brush salesmen."[45] This article not only tried to send new clients to brokers, but it also suggested new ways to prospect. A fund company helping

investment dealers bring new people into the market of course helped itself grow; when approached by a prospective shareholder whose friend owned the Putnam Fund, the dealer likely would have sold the new client Putnam shares as well.

Successful mutual fund firms remained mindful that forming a social connection with dealers was as important as the relationship established within a business context. Fund executives often reached out to brokers in this way by hosting trips to the fund's home office, where brokers met with the officers and investment professionals. American Funds called their two-day trips "total immersion" programs, during which time they taught brokers about the advantages of mutual funds and imparted tips on how to sell more effectively.[46] Most funds also hosted nice dinners and evening social events. The George Putnam Fund of Boston grew famous for inviting to its annual fund meeting any dealer who could attend and hosting lunch for all at Boston's famous Union Oyster House. For its largest client, Vermont Securities, Putnam hosted a regular autumn retreat in Vermont, holding an afternoon sales meeting followed by a lobster dinner.[47]

Individual wholesalers also held social events within their respective territories in order to strengthen the bond with their dealers. Ward Bishop, creator and initial wholesaler for American Funds Distributors,[48] was known for his love of drink and conversation. He frequently took small groups of dealers out for drinks, dinner, and more drinks, all the while getting to know them personally and reminding them of the benefits of selling American Funds.[49]

Realizing that a positive image of the industry in general was essential to growth, separate companies worked together to foster an effective relationship between the industry at large and the investment dealer community. In 1949, in New York City, the fund industry held its first mutual fund convention for investment dealers. Dealers from thirty states and the District of Columbia attended. At the convention, representatives from the most prominent mutual funds hosted sessions on how to find prospects and sell funds.[50]

One of the hosts was Investors Diversified Services (IDS). Among the largest mutual fund complexes during the mid-20th century, IDS held great weight within the industry. In 1894, IDS began in Minneapolis, Minnesota, as Investors Syndicate,[51] a firm that only offered face-amount installment certificates. With this product, the buyer made payments until the certificate matured — usually in ten years — at which time he received full interest and premium upon redemption. John Tappan founded Investors Syndicate with slightly more than $2,500, and by the turn of the century, his firm had more than 1 million in assets.[52] In the mid-1930s, the firm's new president, John Ridgway, became intrigued with open-end investment companies. He made a small attempt to create one but dropped the idea within a year, realizing that the company lacked appropriate investment management expertise. In 1939, Ridgway observed the growth of investment companies. With the goals of protecting the company's business against a potential downturn in certificate sales and

relatedly, broadening the products available for sale, Investors Syndicate created its first mutual fund, Investors Mutual, Inc., in January 1940.[53]

Unlike most other firms, Investors Syndicate only sold its funds through its own sales force. When the firm commenced distributing funds, these sales representatives were faced with a large challenge: since the 1930s, they had sold against investment companies and had become adept at disparaging the product. As one salesman recalled, when a prospect expressed interest in investment trusts, the salesman used to respond, "Mr. Prospect, you mean investment mistrusts, do you not?"[54] Extensive sales retraining efforts proved successful, though, and by 1948, Investors Mutual was the largest fund in the country, with just over $126 million in assets.[55] The rapid growth of the fund through sales by its captive retail sales force motivated a few other fund management companies to experiment with such a structure, though most ultimately continued to wholesale through investment dealers.[56]

At the 1949 mutual fund convention for investment dealers in New York City, IDS executives willingly shared some of their successful sales strategies for the betterment of the entire industry. Grady Clark, the company's vice president of sales, conducted a session for non-IDS dealers on how he trained his sales forces to prospect for business and sell mutual funds. He passed along various relationship building ideas, including sending birthday cards to clients. Clark conducted this session for competitors of his own sales representatives because he realized that millions of American workers had yet to hear of mutual funds, and the best way to create awareness and confidence in the vehicle was to help one another.[57]

This collaborative sentiment was still evident eleven years later when the mutual fund, One William Street Fund, supported a contest for the most effective mutual fund sales idea. Lehman Brothers opened the fund in 1958, and it was the largest initial offering of a fund at the time. In order to encourage this popularity, the underwriter of "One Willie," as the fund was known among dealers, asked all interested securities dealers to submit their most creative sales technique, regardless of whether it was used to sell One William Street Fund or another mutual fund. At the conclusion of the contest, the underwriter published all 150 entries in a pamphlet available to any interested securities dealer. When asked why the firm would publish sales ideas featuring the funds of the competition, a sales executive explained, "We think that anything we can do to help improve the broad picture of mutual fund share sales will aid us — sooner or later — in our own primary sales assignment." The actions of this executive, and those of Grady Clark of IDS, demonstrate the industry's understanding that collaborative efforts to help dealers attract shareholders benefited the entire industry.[58]

Working together, various members of the mutual fund industry helped introduce millions of Americans to mutual funds. Leaders of fund companies were proud of their progress and their ability to provide what they saw as a simple and inexpensive means for Americans to participate in the stock market.

In 1960, Chauncey Waddell, founder of Waddell and Reed, wrote a letter to the president of another investment company saying, "The biggest social need that we are filling is the need of an investment program that will enable a person to contend with the rising cost of living . . . Our industry is the only well organized industry that is able to cope with this vitally important problem."[59]

Waddell and other leaders succeeded in large part because they conveyed this ability to investment dealers. By the early 1960s, almost half of the nearly five thousand broker-dealer firms registered with the Securities and Exchange Commission described their primary or secondary activity as selling mutual funds. Even Merrill Lynch & Company, the largest securities firm in the world, after shunning mutual funds since the firm's founding in the early 1940s, finally realized in the late 1960s that it could not fully serve its clients without offering funds.[60]

In the 1970s, however, mutual fund sales temporarily faltered. In 1973, 1974, and 1977, assets in mutual funds declined. Fund industry leaders could blame difficult stock markets to a point, but between 1972 and 1977, with the exception of one year (1974), redemptions outpaced new share sales.[61] This strongly suggested that investment dealers were turning away from selling mutual funds in favor of other products; the distribution system of independent investment dealers that had supported the industry for decades now thwarted its expansion. While mutual fund leaders could take credit for having sharply invigorated the mutual fund industry in the prior two decades, this downturn in sales in the 1970s showed distributors that they clearly needed to refine and adapt their distribution channels to a changing financial world.

NOTES

1. Board of Governors, *Flow of Funds in the United States 1939-1953* (Washington, D.C.: Federal Reserve Board, 1955), 41, 73; William D. Carter, "Mutual Investment Funds," *Harvard Business Review*, 27, no. 6, (1949): 722. The earliest year for which such information is available is 1939.
2. This paper only considers open-end investment companies due to their enduring popularity since the 1940s. Though closed-end funds were more popular in the 1920s, open-end mutual funds dominated the investment company marketplace after the 1929 Crash. For a thorough discussion of the difference in sales and performance of closed-end and open end companies prior to 1940, please see Natalie R. Grow, "The 'Boston-Type Open-End Fund' — Development of a National Financial Institution: 1924-1940" (Ph.D. diss., Harvard University, 1977), 113-122.
3. Investment Company Institute, *1973 Mutual Fund Fact Book* (Washington, D.C.: Investment Company Institute, 1974), 10.
4. Gene Smith, "The Funds are Mutual," *New York Times*, 7 September 1955, 41; "The Prudent Man," *Time*, 1 June 1959, 74.
5. The only year between 1940 and 1972 that the industry experienced minor decline was 1941, when assets fell to $401,611 from $447,959 in 1940, and the number of

shareholder accounts fell to 293,251 from 296,056. Investment Company Institute, *1973 Mutual Fund Fact Book*, 7.

6. This statement and the previous one about the 1930s refer to individual mutual funds rather than fund complexes. In other words, by 1960, Putnam Management Company operated four funds: George Putnam Fund of Boston, Growth Fund, Income Fund, and Fund for Growth and Income. Each of these funds was included in the 1960 statistic.
7. A little more than 10 percent of funds were sold directly to the public through their own retail organizations, and the remaining funds were sold by mail. House Committee on Interstate and Foreign Commerce, *Special Study of the Securities Markets*, 88th Cong., 1st sess., 1963, H. Doc. 88-95, Part 4-6, 293. Grow notes that, by the mid-1930s, wholesale distribution had become the norm, while the retail sales operation was much less frequently employed, though she fails to provide supporting statistics. Grow, 352. Robert Claude Perez, in his 1965 dissertation on the mutual fund industry's growth since the 1920s, also mentions that mutual fund leaders adopted the wholesale model early and that it gained in popularity quickly. According to his statistics, which he gathered from annual reports and prospectuses, in 1945, 89 percent of mutual fund sales occurred through independent dealers. By 1964, this had decreased to 58 percent, in large part because some large retail financial companies, such as Investors Diversified Services, Inc. and Waddell & Reed, Inc., had increased their share of fund sales from 10 to 36 percent. The remainder of shares were sold by no-load funds. (These statistics refer to funds that exceeded $100 million in 1964.) "A Critical Appraisal of the Marketing Structure and Techniques used in Distributing Mutual Fund Shares to the Investment Public," Ph.D dissertation Graduate School of Business Administration, New York University, 1965, Appendix G2. Regarding the amount of assets held by funds (with $500 million or more in assets at the end of 1964), funds that were predominantly wholesaled, in 1945, held almost 60 percent of the industry's assets versus the approximately 6 percent of assets held by retail sold funds. At the end of 1964, wholesale distributed funds held 49 percent of industry assets, while the retail sold funds held 26 percent. (The remaining assets were managed by funds with less than $500 million in assets.) Note that some of the funds in this group, such as those managed by Dreyfus and Putnam, also distributed some of their shares through retail outlets. In the figures cited regarding share sales, Perez distinguishes between shares sold through retail outlets and those sold by independent dealers. Perez, Appendix B3.
8. George Putnam, interview by Emily L. Martz, December 23, 2008, Boston, MA.
9. Grow, 544.
10. Ibid., 580; Fink, 66-67.
11. Fink, 26.
12. Ibid.
13. Open-end funds gained this exception because the leaders successfully persuaded Congressmen and President Roosevelt to treat an open-end investment company as a conduit between fund shareholders and the securities in which the fund invests. This meant that the shareholders were treated as direct owners of the securities, and therefore only the shareholders, not the shareholders *AND* the fund, paid taxes on the dividend distributions. Had mutual funds not been treated as a conduit, then

the fund and the shareholders would have paid taxes on the same distribution, essentially making shareholders pay twice — once when the fund paid the taxes out of its assets, and secondly, when the shareholders paid the government. Fink, 26-27.

14. Ibid., 26-28.
15. Ibid., 28-29, 36-37.
16. This point is one that Fink emphasizes to explain why the mutual fund industry fared well in the recent crisis relative to hedge funds and other investment products. Combined with regulations levied by the Investment Company Act of 1940, mutual funds were legally precluded from leveraging and speculative activities that were the downfall of other types of investment vehicles.
17. Between 1933 and 1940, total net assets of all open-end investment companies increased more than 600 percent, from approximately $74 million to $532 million. Grow, 412. Much of this occurred because managers of fixed trusts were creating open-end mutual funds and encouraging participants of the fixed trusts to transfer their funds. While Grow provides data about the gross sales of shares of the original three mutual funds (which indicate some upward momentum), statistics regarding sales of all open-end funds are lacking. Aggregate share sales for the original three mutual funds rose from $22 million in 1931 (the low point) to $86 million in 1935 and then to $123 million in 1936. There was a dip in 1934 to sixty-nine million shares after having been at eighty-two million the prior year. Grow, 410.
18. Closed-end investment companies' market share of all investment trusts and company securities (including fixed and semi-fixed investment trusts) shrank from 51.7 percent in 1929 to 1.6 percent in 1933. Open-end investment companies' market share grew during this same time period from 2.9 to 66.3 percent, with a particularly large jump occurring between 1931 (6.6 percent) and 1932 (21 percent). Grow, 222.
19. Board of Governors, *Flow of Funds Accounts of the United States, Annual Flows and Outstandings, 1945-1954, 1955-1964, 1965-1974* (Washington, D.C.: Federal Reserve System, 2009), 8, http://www.federalreserve.gov/releases/z1/Current/data.htm.
20. Janice Traflet, "Never Bought, Always Sold: Salesmanship, the Small Investor, and the Early Postwar Surge in Mutual Fund Participation," *Essays in Economics & Business History* 27 (2009): 5-14.
21. George Putnam Interview; "The Financing of Sales of Mutual Fund Shares," *University of Pennsylvania Law Review* 11, no. 5 (1967): 769-854.
22. Paul Cabot, interview by R.J. Tosiello, 1971, located in *Records related to investment banking, 1870-1971*, Baker Library, 1-2, 4-5.
23. Grow, 83, 84.
24. Ibid., 69-73.
25. George Putnam, "Personal Recollections of the Putnam Funds and Their Associated Putnam Companies: An Informal History, 1951-2001," (2001), 8, 9, Massachusetts Historical Society, Boston; Grow, 76-84.
26. Grow 75, 76.
27. Grow 83-88; Putnam, "Personal Recollections," 9, 10.

28. A fund complex is a group of mutual funds advised and administered by a single management company.
29. Wharton School of Finance and Commerce, *A Study of Mutual Funds: Prepared for the Securities and Exchange Commission by the Wharton School of Finance and Commerce*, 87th Cong., 2nd sess., 1966, H. Doc. 2274, 472, 473.
30. Grow, 357.
31. By the 1960s, the distribution of MIT had been relinquished to Vance, Sanders & Co.
32. Parker Corporation merged with Putnam Management Corporation in 1964, and the total number of wholesalers at Putnam after the merger was thirteen. Perez, Appendix G3.
33. Perez, Appendix G3.
34. "Own Sales Units Mutual Funds' Aim," *New York Times*, 16 April 1950, F1; George Putnam, "Personal Recollections," 23-24; George Putnam Interview.
35. The company changed its name to Edward Jones & Co. in 1982. See http://www.edwardjones.com/en_US/different/history/index.html.
36. Charles D. Ellis, *Capital: The Story of Long-Term Investment Excellence* (Hoboken: John Wiley & Sons, Inc., 2004), 72, 73.
37. Ibid., 73-75.
38. "Rapid Rise Seen in Mutual Funds," *New York Times*, 19August 1949, 25.
39. Ellis, 69; "Own Sales Units Mutual Funds' Aim," *New York Times*, F5.
40. George Putnam Interview; Louis Harvey, interview by Emily L. Martz, January 22, 2008, Boston, MA. Louis Harvey is founder and current President of DALBAR, Inc.
41. John J. Abele, "Mutual Funds: No Lures Barred for Selling," *New York Times*, 30 May 1960, 22.
42. Grow, 76, 84; George Putnam Interview; "Personal Recollections," 23-24.
43. Charley Kersten, interview by Emily L. Martz, November 19, 2008, Boston, MA. Charley Kersten is currently Vice President and Director of Communications for Putnam Investments; George Putnam Interview.
44. George Putnam Fund of Boston Trustees, *Prudent Investor*, Spring 1952, 2. Italicized emphasis is in the original.
45. George Putnam Fund of Boston Trustees, *Prudent Investor*, Spring 1955, 2.
46. Ellis, 71.
47. "Personal Recollections," 32.
48. American Funds Distributors was originally created in 1939 at the behest of Capital's founder Jonathan Bell Lovelace. The organization's original name was Investment Company Distributors, Inc., and then its name was changed to Investment Company of America Distributors, Inc. in 1944, and then to American Funds Distributors in 1951. Ellis, 10, 67.
49. Ellis, 71.
50. "Investment Men Hear How to Sell," *New York Times*, August 17, 1949, 33.
51. The company's name changed to Investors Diversified Services on March 30, 1949.
52. Company History Narrative, undated, 147.F.20.10F, Box 1. Investors Diversified Services Records. Minnesota Historical Society.

53. Company History Narrative, January 13, 1969, 147.F.20.10F, Box 1. Investors Diversified Services Records. Minnesota Historical Society.
54. Oral Histories, undated, 147.F.20.10F, Box 1. Investors Diversified Services Records. Minnesota Historical Society.
55. Nathan Belfer and Robert Weinberg, "Recent Developments in the Investment Trust Field," *Southern Economic Journal*, 16, no. 4 (1950): 452.
56. "Investment Men Hear How to Sell," *New York Times*, 33; "Own Sales Units Mutual Funds' Aim," *New York Times*, F1.
57. "Investment Men Hear How to Sell," *New York Times*, 33.
58. Clayton S. Scott, Jr., "Corporate Nicknames in the Stock Market," *American Speech* 35, no. 3 (1960): 201; "Investment Men Hear How to Sell," *New York Times*, 33; "Mutual Funds: No Lures Barred for Selling," *New York Times*, 22.
59. Letter from Chauncey L. Waddell to Ferdinand Eberstadt; August 17, 1960; Ferdinand Eberstadt Papers, Box 161; Public Policy Papers, Department of Rare Books and Special Collections, Princeton University Library.
60. House Committee on Interstate and Foreign Commerce, *Special Study of the Securities Markets*, 88th Cong., 1st sess., 1963, H. Doc., 32 (table), 95 (summary); Lehr and Eisenberg, "Mutual Fund Retailing: Aspects of Market Structure and Dealer Operations," http://www.sechistorical.org/collection/papers/1960/1964_0601_Mutual_Fund_manual.pdf; Audio Tape, "Mutual Funds," September 8, 1969, Donald Regan Papers, Recorded Sound Reference Center, Library of Congress, Washington, D.C.
61. Total sales outpaced redemptions throughout the 1970s, but total sales figures include the reinvestment of dividends and therefore require no sales effort. Investment Company Institute, *2007 Investment Company Fact Book*, 94.