Banker John Train

'Amputations' of Workers And Auto Plants Necessary

The following article, "Investing Like Mr. Morgan, Not Like Mr. Ford," was published April 1, 2006, by John Train, and is available at web.mac.com/train.ontrack. Train refers to his grandfather, Charles H. Coster, a partner of J.P. Morgan, who was in charge of Morgan's takeovers of the U.S. railways that had been built by government-subsidized nationalist industrialists. J.P. Morgan was famous for his vow, never to invest in any enterprise that was not "complete" already; that is, Morgan would not put a penny into the creation of new industry. As EIR *documented in its Sept. 29 issue, Train is a kingpin in the bankers' "secret government," and a decades-long enemy of Lyndon LaRouche.*

In the course of studying the techniques of great venture capital investors, I have noticed a number of common traits. J.P. Morgan, of whom my grandfather was a partner, had a cardinal rule: look first at the character of the people involved.

You could not get money out of his firm if he had any doubts about your integrity, skill or industry. The quality of the business was secondary, although of course he looked long and hard at that too. This emphasis on integrity is probably a more welcome conception today than at many other times, what with the sequence of horrible scandals we have been seeing. One minute management claims the company is going great guns, and a few months later it declares bankruptcy.

Incidentally, in a science-based company it is much more important for the CEO to have business skill than scientific skill. It is like the story of Machiavelli, who was a military theorist as well as a political theorist, trying to explain to his patron an idea he had about infantry tactics. The Duke took him out into the courtyard of the palace, called for a box for him to stand on, and told him to give the necessary orders to the palace guard. In a few minutes he had them tied up in a hopeless tangle. The Duke called over the guard's commander, who had been watching the performance, and Machiavelli showed with a stick in the sand what he had in mind. With a few orders the commander straightened the men out and got them into the desired formation.

Big ideas are one thing and execution another, particularly in business. It follows that an inventor is almost never the right CEO for a company. Indeed, with wonderful exceptions, the founder of a company is not likely to be the right CEO either. You need an experienced manager, who knows all about finance, marketing, coping with regulation, handling personnel, dealing with unions and the like. . . .

For that matter, the venture capital investor should always consider Train's Fourth Law: *Most Things Don't Work.* Rather than invest at an early stage, when all the money gets perhaps forty percent of the deal, which probably won't make it, one is usually better advised to be patient until the company is a going concern, with a quoted stock, enjoying established markets and have strong management in place, and then wait for a market washout, when you can buy in on the basis of just the cash in the bank, getting the whole company for nothing. These moments come along quite regularly. J.P. Morgan was once asked what he thought the market would do. "It will fluctuate," he replied, portentously. This sounds like a putdown of a presumptuous question, and yet it is a great investment truth: You can count on the market collapsing from time to time, and then recovering and going to overvaluation.

One question you hear a lot in venture capital is, "What about the exit?" People with a proposition often start talking from the first about when they are going to get out. I don't like to hear that. I'd prefer to hear the entrepreneur talk about achieving his dream in full—being married to it.

As a banker, Morgan was always concerned with cash. The typical cause of death in new companion companies is not the failure of the conception, but, rather, working capital asphyxiation. If there isn't enough cash to let the company function comfortably, the CEO may spend more time fending off creditors than operating the business itself, a disastrous situation. By this I mean cash flow, not profits. If the company's taking in more from sales than its costs, before depreciation, then it's airborne, not sinking, and can carry on indefinitely. Counting profits can come later, and dividends later still.

A final Morgan characteristic was the ability to decide important questions without dithering. The CEO of a company you are thinking of backing should possess this quality. He should have enough knowledge and enough self-confidence to settle issues briskly. Let the competitors have their long committee meetings—which may not reach or render any good conclusions anyway. One time during a financial panic, with banks failing one after another, a group of terrified bankers came to Morgan in his famous library. He studied the situation, and, writing off a number of banks whose situation was hopeless, answered, "The rot stops here," telling the group that they had to guarantee the solvency of a particular bank that could be saved, so that all those that were in still better condition could rise above challenge. So too the competent CEO must be able to abandon a losing project or a losing division to concentrate his cash and his attention on the good ones.

Ford and GM just announced major cutbacks in their U.S. operations, which are hemorrhaging cash. Also, they say they will reverse their traditional policy of producing what customers weren't buying, just to keep the plants running and the unions happy. Should not young Mr. Ford and his counterparts have had the courage and skill to perform the major amputations required to save the main body of their companies ten years ago?