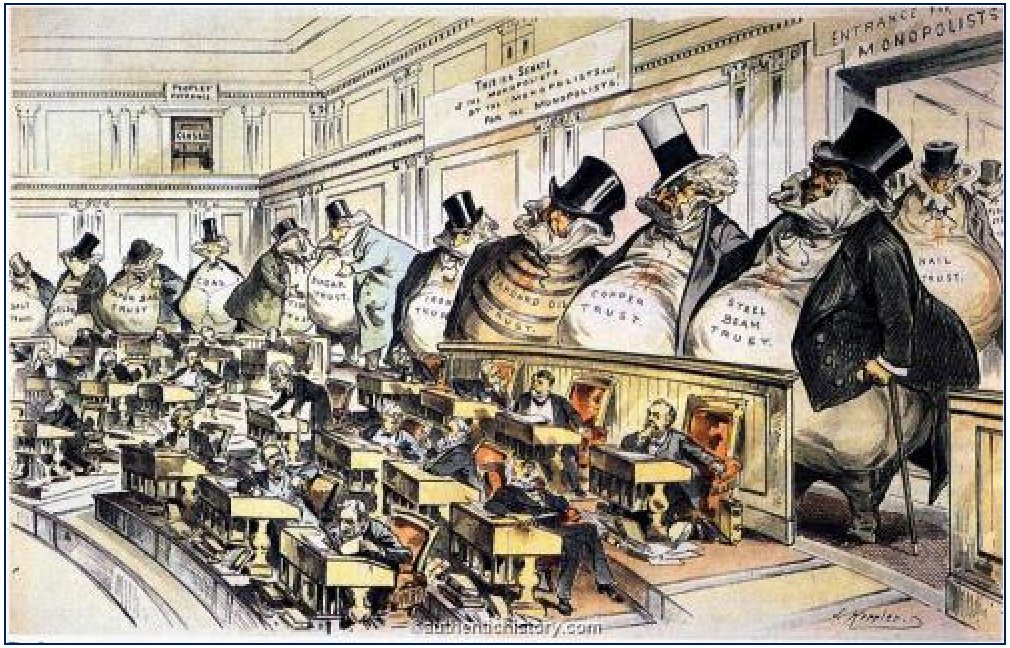
# The American Business Revolution: Corporate Consolidation in the Nineteenth Century

## An Online Professional Development Seminar





**Volker Janssen**

Associate Professor
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AMERICA *in* CLASS®
*from the* National Humanities Center

## GOALS

1. Students can describe business competition as a dynamic process of organization, technological development, and financial innovation.
2. Students can illustrate how businesses make decisions in response to their times and environments, not simply in accordance with economic models.
3. Students can discuss the vagaries of economic growth in the Gilded Age.
4. Students understand the economic benefits and disadvantages of consolidation.
5. Students can discuss the challenges economic consolidation poses in a democracy.
6. Students can discuss the relationship between the world of finance—Wall Street—and of industry—Main Street.
7. Students want to learn more about how the American economy has worked over time.

# From the Forum

- How did the Supreme Court affect corporate consolidation during this period?
- What is the difference between a trust and a holding company?
- How does business consolidation, past and present, affect class divisions in this country?
- Who benefited from corporate consolidation?  Who suffered?
- Was corporate consolidation an inevitable step in the evolution of capitalism?

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Teaching American History Grant Scholar
in Illinois and California

*Convict Labor, Civic Welfare:*
*Prisons and Rehabilitation in mid-twentieth century America*.
(Oxford University Press, forthcoming)

*Minds and Matters: Technology in California and the West*.
(University of California Press, 2012)

"A Tale of Two Crises: A Comparative View of the
Political Economy of the 1920s and 2000s." in
*When Government Helped*. (Oxford UP, forthcoming)

"When the Jungle Met the Forest:
Public Work and Civil Defense in California's Prison Camps."
http://www.journalofamericanhistory.org/teaching/2009_12/

*The Great Depression and the New Deal. A Study Guide*
(U.S. Academic Decathlon, 2009).

# The American Business Revolution: Corporate Consolidation in the Nineteenth Century

1. The Booms and Busts of the New Economy
2. The Costs of Economic Contraction
3. Strategies for Survival: Collusion and Corruption
4. The Lessons of '93: The Morganization of America
5. The Debate over the Great Merger Wave in 1901
    - Russell Sage, "A Grave Danger to the Community."
    - James Hill, "Industrial & Railroad Consolidations: Their Advantages to the Community."
    - Charles R. Flint, "Industrial Consolidations: What they have accomplished for Capital and Labor."
6. Corporate Power and the Federal Government
7. Corporate Power and the 20th century U.S. Economy

# 1. The Booms and Busts of the New Economy

A. The Gilded Age: Growth or Stagnation?

B. American railroads
- in industry and the market
- on Wall Street

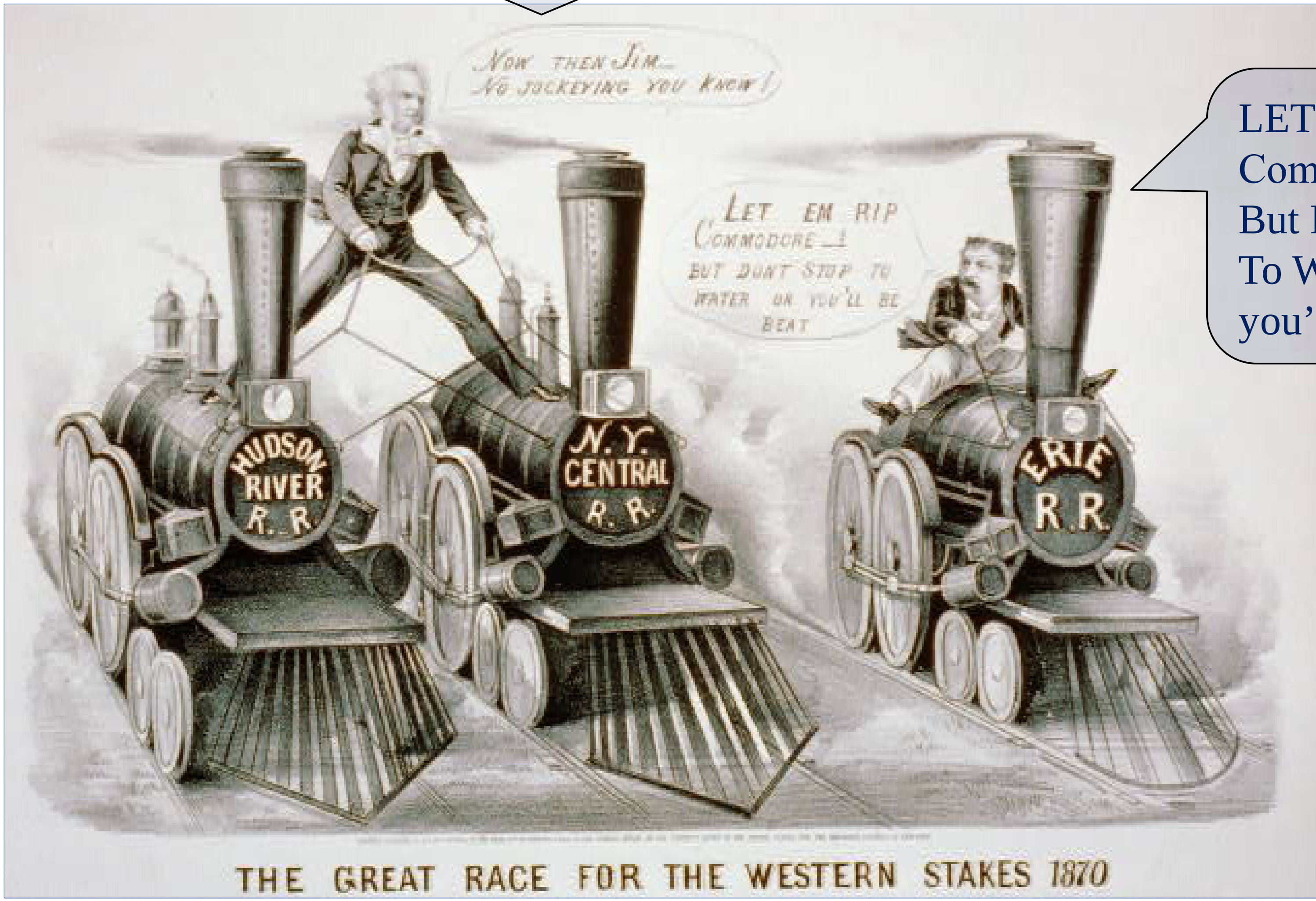
C. Railroads and Robber Barons

D. Railroads as public utilities

# "The great race for the Western stakes 1870."
# New York, Currier & Ives, c1870, March 5.

Now then Jim…
No Jockeying you know!

LET EM RIP
Commodore—
But Don't Stop
To Water or
you'll be beat



# 2. The Costs of Economic Contraction

A. The Anatomy of Financial Crises:
- Banks and Notes
- Gold
- The Price Mechanism

B. The role of government
- The principle of laissez-faire
- Federal gridlock
- Republican Consensus:
  Deflation, Tarrifs, and Gold Standard

# 2. The Costs of Economic Contraction

PANIC, AS A HEALTH OFFICER, SWEEPING THE GARBAGE OUT OF WALL STREET.

"Panic, as a Health Officer, Sweeping the Garbage out of Wall Street." Despite the ghastly appearance of the figure representing financial panic, this *New York Daily Graphic* cover cartoon of September 29, 1873, subscribed to the belief that such financial busts, cleansed the economy.

For a zoomable version: http://superitch.com/?p=7234

# 3. Strategies for Survival: Collusion and Corruption

## I. Competitive Strategies of American Industries in the Gilded Age

### A. Brand producers

- Small-quantity
- Highly differentiated
- High quality

- Stable business
- Stable prices
- Little innovation

Examples:
Fine linen paper, Quaker Oats

**Characteristics:**
Family-owned or old partnerships
Skilled labor
Small to moderate size
Moderate capitalization/low debts

### B. Mass producers

- Large volume
- Homogenous
- Simple

- No pricing power
- Aggressive innovation
  Examples: Bessemer furnace, Bonsack cigarette machine, barbed wire, glucose, wood-pulp paper
- New raw materials
  Examples: Western copper, Pennsylvania petroleum

Examples: sugar, petroleum, beef, newsprint paper, whiskey, cast-iron pipe, some tobacco products

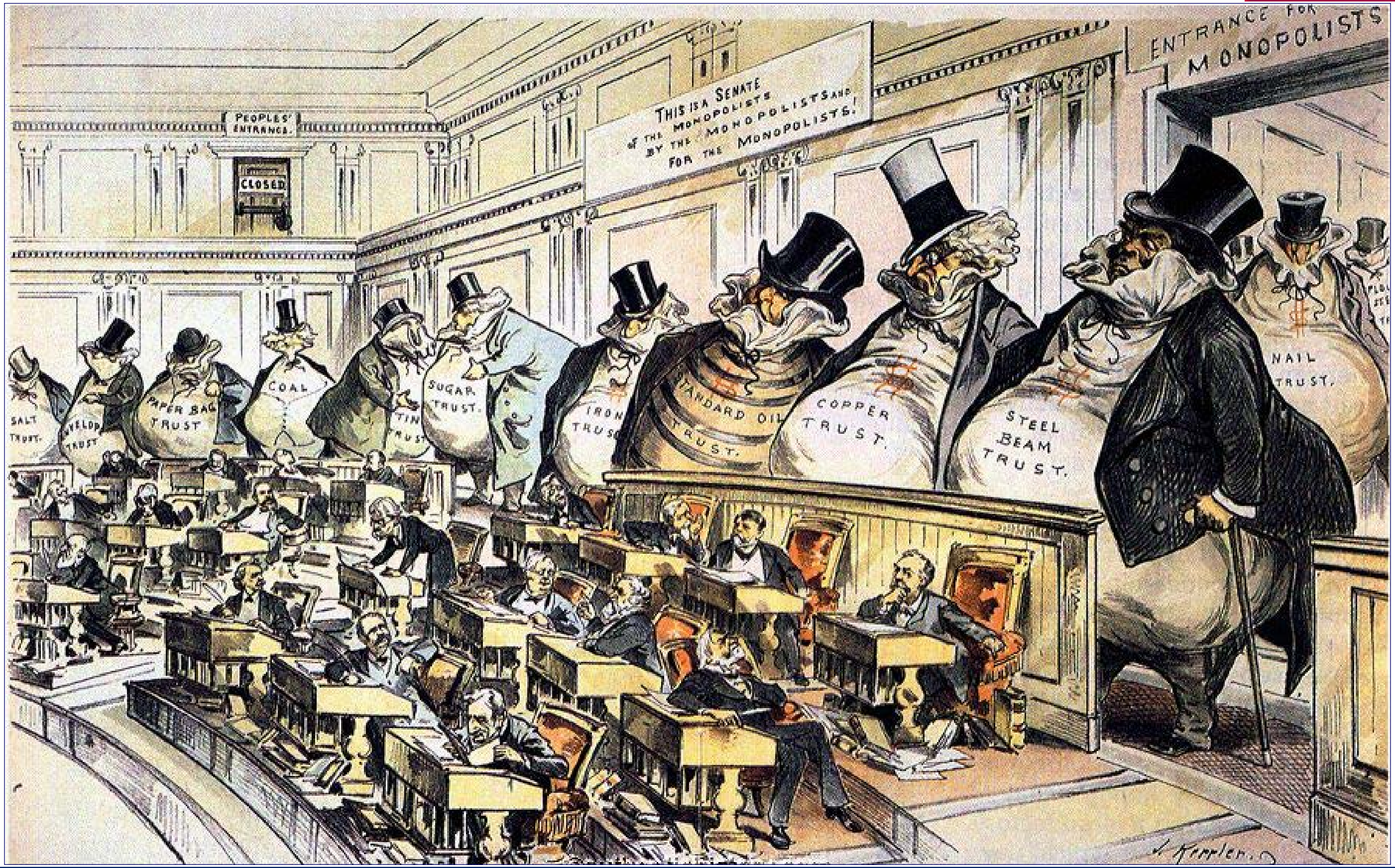
**Characteristics by 1890:**
Large-scale
High capitalization / high debt burden
Vertical Integration (Marketing and Raw Materials)

# 3. Strategies for Survival: Collusion and Corruption

## II. Securing the Aid of Government

A. The absence of federal regulation
B. State governments and industry lobbies
C. Party “machines”

# 3. Strategies for Survival: Collusion and Corruption




This cartoon, “The Bosses of the Senate,” from *Puck* magazine January 23, 1889 shows rotund monopoly businesses towering over obedient lawmakers in the Senate. Above them appear Lincoln’s words at Gettysburg altered to this: “This is the Senate of the Monopolists, by the Monopolists, and for the Monopolists.”

For a larger image: http://www.authentichistory.com/1898-1913/1-industrialization/1-becoming/index.html

# 3. Strategies for Survival: Collusion and Corruption

## III. Survival Strategies of Mass Producers in the Gilded Age

A. **"Gentlemen's Agreements" –** informal agreements that set and maintained prices

B. **"Pools" –** Markets assigned in portion (territory or volume) to participant sellers

C. **'Profits Pool" –** Central pooling of net income and redistributed by percentage of total sales
  - Not durable
  - Not enforceable

D. **Trust** – Stockholders of previously competing firms hand their shares to a group of trustees and receive "certificates of trust"
  - popular in kerosene, sugar, whiskey, cottonseed oil, salt, rubber boots, gloves
  - On public record – soon outlawed at state and federal level

E. **Holding Companies –** Corporations that owned securities of other companies
  - **New Jersey** Incorporation Statutes in 1889 allow holdings within and across state borders
  - Benefits: No cash needed, no rules for value assessment,
  - Key device in **horizontal** integration and expansion
  - Holding Companies could control individual corporations with relative majority of voting stock

# 4. The Lessons of ‘93: The Morganization of America

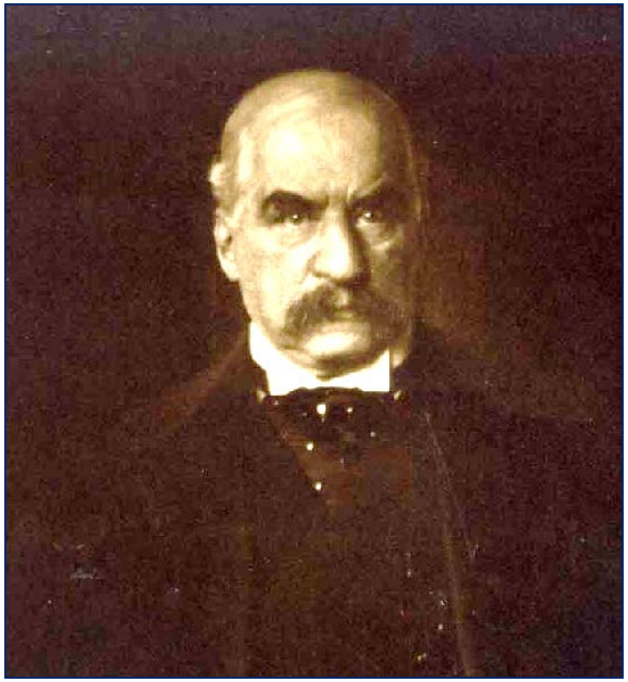
## III. Survival Strategies of Mass Producers in the Gilded Age

**A. The Crisis of 1893**

- Financial panic
- The Morgan Bail-Out
- Unemployment, Bankruptcies, and Poverty
- Political Unrest

**B. The Morganization of American corporations**

- Investment firms, lawyers, and industries
- Money Trusts: Saviors  - or a new Aristocracy?



**J.P. Morgan:**

(1837-1913), began as an accountant for banking firms until he became a partner in a company in 1871, which was reorganized as J.P. Morgan and Company in 1895. A coldly rational man, Morgan reorganized railroads after 1885, by gaining control of large amounts of stock. In 1896, Morgan embarked on consolidations in the electric and steel industries, creating the world's first billion-dollar corporation: U.S. Steel. By the early 1900s, Morgan was the main force behind the “Money Trusts,” controlling virtually all the basic American industries.

# 5. The Debate over the Great Merger Wave

**1. Russell Sage (1816-1906)**

This New York financier and politician was a member of Congress before the Civil War (Whig Party), a director of the Union Pacific (Transcontinental Railroad), Western Union Telegram, and sat on the Board of the Stock Exchange on Wall Street. His close association with Jay Gould and his own trial for usury makes him one of the Robber Barons. The famous Russell Sage Foundation was created by his second wife after his death.

**2. James J. Hill (1838-1916)**

Known as the "Empire Builder," James Hill entered the railroad business in the Panic of 1873 and gained notoriety as CEO of the Great Northern Railway that dominated the Northwest, Northern Great Plains and Upper Midwest. In 1901 he formed the Northern Securities Company together with J.P. Morgan merging three great railroads. Northern Securities was ordered to dissolve by Theodore Roosevelt.

**3. Charles R. Flint (1850-1934)**

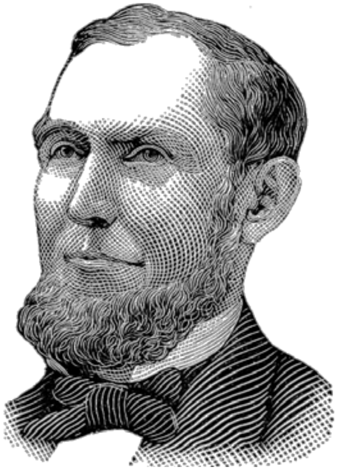
Charles R. Flint was an American businessman, best known as the founder of the Computing-Tabulating-Recording Company which later became IBM. In 1892, he merged several companies to form U. S. Rubber. In 1899 he repeated the same to form American Chicle. He was also responsible for the formation of American Woolen in 1899. For his financial dealings he earned the moniker "Father of Trusts."

# 5. The Debate over the Great Merger Wave: Russell Sage

…to me, there seems to be something very slight-of-hand in the way in which industries are doubling in value, as at the touch of the magician's wand. Here we have **a factory**—a good, conservative, productive investment which may be turning out anything from toys to locomotives. It **falls into the hands of the consolidators, and, whereas it was worth $50,000 yesterday, to-day it is worth $150,000—at least on paper. Stocks are issued; bonds are put out; and loans are solicited, with these stocks as security.** The man who owned the factory could probably not have borrowed over $10,000 on it. Now, however, when the $50,000 plant is changed into a stock issue of $150,000 bankers and financiers are asked to advance $60,000 or $70,000 on what is practically the same property, and many of them from all accounts, make the advance.

## The Question of Value

What determined the market value of any company traded on the stock market according to Russell Sage?



# 5. The Debate over the Great Merger Wave: Russell Sage

It is truly remarkable, the increase which has taken place in requests for loans based on industrials. **No one can even estimate the amount of money that has been advanced on securities of this class**; but it is a conservative estimate to say that industrial loans are as ten to one compared with conditions a few years ago. This is apparent from the business offered at my office from day to day. **The volume of money in the country is entirely inadequate to meet anything like the demands that are made on collateral of this class.** In fact, we have gotten away entirely from the old idea of making the money of the country the basis of our trading. Instead, there is thrown into the business world, to be used as a trading medium, millions upon millions of new stocks, the real value of which is yet to be determined. As soon as this is thoroughly realized, we may look for trouble, pending a readjustment. This can be predicted with perfect safety....

## The Impact on the Supply of Money

According to Russell Sage, what impact did stock trading have at all on the money supply?

# 5. The Debate over the Great Merger Wave: Russell Sage

The consolidations of today begin at the very outset with capitalizations that cast all past experiences into the shade, and that almost stagger the imagination. **The [U.S.] steel combination now forming... is to start off with a capitalization of $1,000,000,000. This is more than one-half of the National Debt.** It is one-seventieth of the entire wealth of the United States. […] It will be seen, therefore, that this company's issue of securities will represent practically one-half of the entire volume of money in America. In a year or two, if precedents count for anything, this capitalization will be very largely increased, and that in spite of the fact that stockholders in the Steel Company, which was the basis of the new combination, got three shares of stock in the new company for one in the old—scores of millions being thus added to the interest-earning securities in the United States, by merely the stroke of a pen.

**The danger of super-size corporations**

What was remarkable about the capitalization of US steel at $1 billion? What were Russell Sage's concerns?

# 5. The Debate over the Great Merger Wave: Russell Sage

It is true that this company has had enormous success, and that it has benefited the community. […] It has made its owners, the capitalists, very rich, and it has acted well by its employees and by consumers.
But if consolidation has produced all these things, it has also, in the case of this company, produced a feeling of unrest and disquiet, industrial and political, that threatens, sooner or later, to bring serious results. […] The complaints of practices have been voiced generally by men who were driven to the wall in trade competition, because they could not dispute the market with a concern so magnificently organized.
But the very groundlessness of most of the complaints ought to be viewed by conservative men as a danger signal. Such complaints, persevered in as they have been, show that the community opposes the idea embodied in this great monopoly…

**Discussion**

What made the Standard Oil Company problematic, according to Russell Sage? Discuss.

# 5. The Debate over the Great Merger Wave: Russell Sage

Sir Richard Tangye, the great English iron master and economist, gives us an unprejudiced view of what may come of the wholesale attempt to kill off legitimate competition. He says:

*America will one day awake to the stern reality of the evil and when its terrible nature is fully realized some strong legislation must follow.*
*I believe if legislation does not step in and treat these men as it would treat other deadly enemies of the state, there will be such an uprising in the States as has not been since the accession of Abraham Lincoln to supreme power. ...*

**Discussion**

What did Russell Sage think was the most dangerous thing about the trend in consolidations? Discuss.

# 5. The Debate over the Great Merger Wave: James Hill

There is one thing that the people who deal lightly with the new business scheme, and who want to sweep it aside as a menace, forget. **We have reached a stage in our national development where business must be done on a different plan from that which served us well half a century ago.** [...] we must keep pace with the times. We have reached a period where the old-fashioned methods will prove inadequate, if the masses of the people are to continue in the enjoyment of the prosperity to which they are entitled. There are too many people to be fed, housed and clothed to permit of the wasteful system which would maintain a horde of idle middlemen. **People in this country live better today than they ever did before in their lives. This is due, I believe, very largely to the improved methods of production.** There are fewer drones in the hive...

## Financial Consolidation as an Historical "Phase"

What was James Hill's final "somewhat historical" argument in defense of consolidation? Explain.

# 5. The Debate over the Great Merger Wave: James Hill

There is in the community a general feeling of hostility towards the railroad and industrial consolidations that have been effected and towards those that are now under way.
[…]Much of it has come, undoubtedly, through the teachings of the newspapers and...through the speeches of political orators. It began when the "trust" came into being as the result of an effort to obviate ruinous competition. The "trust" was found a very cumbersome structure, and the law of the land declared it illegal. It was not a consolidation in any sense of the term, and differed entirely from the business scheme under which the consolidations of today are being effected and operated. **Under the "trust" system the stocks of various and competing organizations were trusteed in the hands of a few men, to whom was given absolute and unqualified power to do what they saw fit with the properties placed under their control.**

## Trusts and the Concentration of Power

Why did James Hill concede that trusts were not a "healthy arrangement?"

# 5. The Debate over the Great Merger Wave: James Hill

The point, therefore, made by Mr. Sage, that a factory worth $50,000 today is necessarily improperly rated at $150,000 tomorrow, because it has been combined with others under one managerial head, has not all the force that might appear from the bald statement of the facts as Mr. Sage puts it. **A property is not necessarily worth only what it represents in the way of real estate, building and plant. It is worth rather what it represents in earning capacity**; and, if, under a combination, its earning capacity is trebled, because of the economy of production, it is not unreasonable to say that its value has been trebled, even though nothing tangible has been added to its material assets.

## The Value of Assets vs. the Value of Promise

Compare and contrast the way that Russell Sage and James Hill determine the value of the company.

# 5. The Debate over the Great Merger Wave: James Hill

The new system in force today is neither illegal nor...harmful to the community. But the people at large have not yet learned to distinguish between the new and the old, and the odium attaching to the "trust" is visited on the consolidation. The old scheme left intact all the corporations it found in existence. In the nature of things, no economy in production could be effected. […]

Certain plants were shut down to restrict the output, […] [and] Increased profits, therefore, could generally be obtained only by an increase of price for the product, **[…]. Under the new system, a different usage prevails. Operating expenses are reduced by combining a number of institutions under one management. […] Economies are effected by the direct purchase of material in large quantities**, or, better still, by adding to the combination a department for the acquisition and control of the sources from which raw material is drawn...

## Consumer Benefits of the Holding Company

How did James Hill compare the trust with the holding company? Compare the two.

# 5. The Debate over the Great Merger Wave: James Hill

**The workingmen benefit** also in another direction, where the concern for which they work is backed by ample capital and has the benefit of concentrated management. **They are assured the use of the most perfect machinery.** A big concern can afford to make improvements and put in the latest machinery, because such improvements and machinery necessarily add to the productiveness of the plant at a rate that will soon make good the expenditure. The smaller concern, while it realizes this fact, is unable to avail itself of the latest appliances, because it has not the necessary capital to invest.

Another advantage of prime importance to the workingmen is that **they may easily participate in the profits of these enterprises by investing their savings in the shares** of the more solid and prosperous concerns.

## Worker Benefits of the Holding Company

How did workers fare in the consolidation of US steel?

# 5. The Debate over the Great Merger Wave: James Hill

The aim in business, as in politics, is to do the greatest good to the greatest number; and the greatest number...is apparently benefited by the consolidations. Almost every improvement that helps the masses brings injury to individuals here and there. The building of a railroad into new territory puts the owner of the stage coach out of business. Trolley cars that have sprung up all over the country have done grave damage to the local hackmen and livery stable keepers. But the community which is brought into touch with the outer world by a new railroad, and the village or town that gains the advantage of cheap and quick transportation by means of the trolley car, are benefited so much more than the stage owners and hackmen are injured, that the balance is easily in favor of the improvements.

**Discussion**

According to James Hill, what is the purpose of business? Do you agree?

# 5. The Debate over the Great Merger Wave: James Hill

This is the theory of the new business consolidations, and their promoters, judging by the results attained so far, believe that it will work out—that it is a good policy and a wise one for everybody. Should experience prove that it is not a good condition for the people at large, it will very soon be upset. Politically, the scheme has never been passed upon as yet; and, if it proves a good scheme, it may never be a distinct issue in politics. If the prosperity of the country (much of which, I believe, is due to the consolidations and economies effected so far) continues, the people will be content to let well enough alone. If, however, it is shown that we are on the wrong track, and that consolidations are harmful to the people in general, as has been so frequently stated, the question will undoubtedly be settled at the polls....

## Discussion

Why did Hill believe that consolidations had to benefit the people? How did he justify this claim? Do you agree?

# 5. The Debate over the Great Merger Wave: Charles R. Flint

Instead of concentrating the wealth of the country in the hands of a few people, the consolidations have had exactly the reverse effect. Where, under the old conditions, there were a hundred stockholders, there are to-day a thousand or two thousand. Never before was there such a wide distribution of manufacturing interests. The great bulk of the stocks is held, not by the very rich, but by the moderately well-to-do. The control under the new system is not vested, as it was under the old, in the hands of a few abnormally rich men, but it rests with the majority of stockholders, whose numerical strength is growing every day. The danger to the community today lies not in the centralization of manufactures, in industrial consolidations, but in the centralization of wealth in the hands of a few men. This centralization was made possible by the old conditions of individualism.

**Discussion**

Charles R. Flint described the complaints that trusts are a political and economic menace as "absurd." Why? Do you agree?

# 5. The Debate over the Great Merger Wave: Charles R. Flint

Money, when based on sound considerations, as our currency is today, is but an expressed form of wealth. Stocks and bonds of the new steel combination, represent quite as much an expressed form of wealth as the currency. They supplement the money in circulation, and, always provided that they are not the mere output of a printing press, serve as tokens of valuable property. Such stocks and bonds are quite as important an item in the wealth of a country as its currency. As the business system of a country expands, the need, relatively, of money grows less. Instead of the actual interchange of gold and silver in commercial transactions, there comes a system of credit. The amount of business transacted on credit in the United States today is over two thousand times as great as that transacted in exchange for gold and silver.

## The Rise of Paper and the Declining Significance of Gold

What is Flint's response to Russell Sage's remark on the relationship between stocks and the money supply.

# 5. The Debate over the Great Merger Wave: Charles R. Flint

Viewing the matter from every standpoint, the business man is benefited when he operates as a member of a combination instead of as an individual. His property is in the shape of stocks and bonds which he can market at a moment's notice, instead of in the shape of a plant, on which it would be impossible to realize anything like its value at a forced sale. In case of his death, or disability, he leaves to his family a property that runs along uninterruptedly. The death of any one individual has little, if any, effect on the general business prosperity of the combination, and the tokens of interest held by the family of a deceased stockholder continue to bring their return just as steadily as though the man himself stood at the helm. In the case of an individual corporation, no matter how well organized or how well established, business failure is almost inevitable when the head of the corporation dies....

## Continuity and Flexibility in Financial Holdings

Flint stated that "the businessman has benefited when he operates as a member of a combination instead of as an individual." What did he mean?

# 5. The Debate over the Great Merger Wave: Charles R. Flint

Labor is immeasurably benefited by the new conditions. The tendency under natural laws would be for wages to gradually decline to the level of the wages paid in other countries, but the industrial combinations have sustained the wages of the American wage-earner. **Today, the tendency is to a minimum of profits and a maximum of wages. Any concern whose profits become abnormal at once invites competition.** Naturally, these profits are reduced, and the consumer, who is the workingman, reaps the benefit. If the profits are not sufficiently abnormal to invite competition, the workingman again comes to the front, for he demands a larger share of the earnings in the form of increased wages. In either case, then, the wage-earners, as the great body of the community, reap the greatest advantages that come out of more economical production....

**Worker Benefits of the Holding Company**

According to Flint, who are the beneficiaries of consolidation?

# 6. Corporate Power and the Federal Government

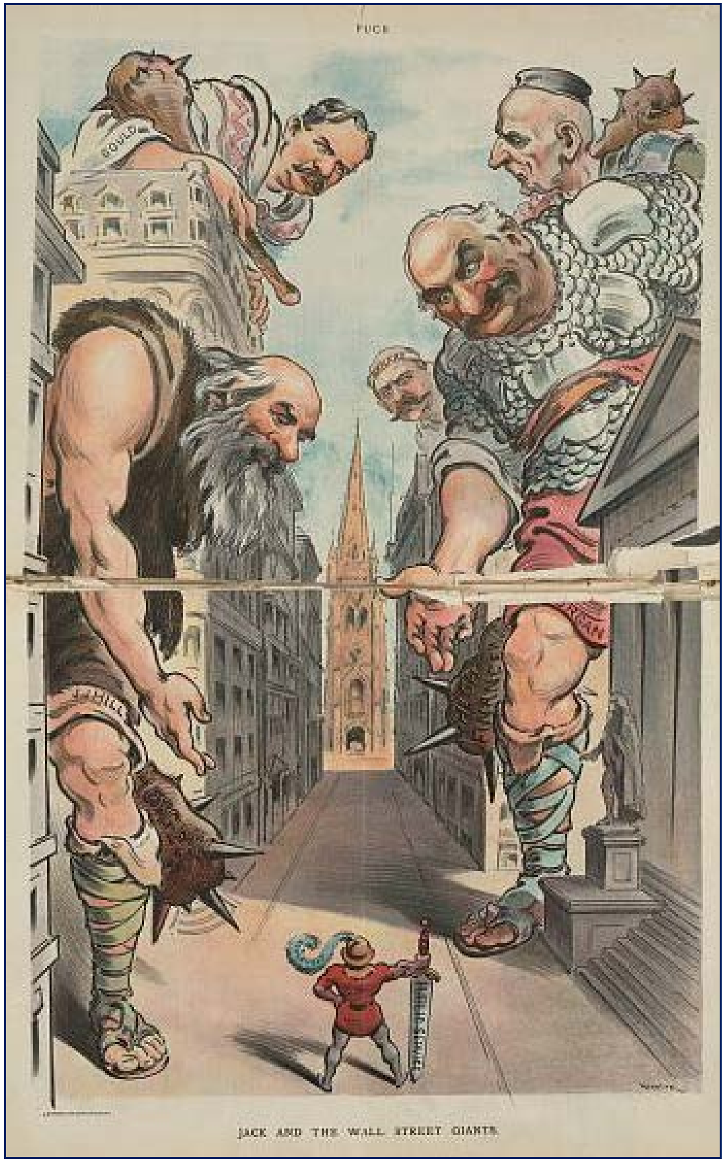
## The Federal Response to the Merger Wave

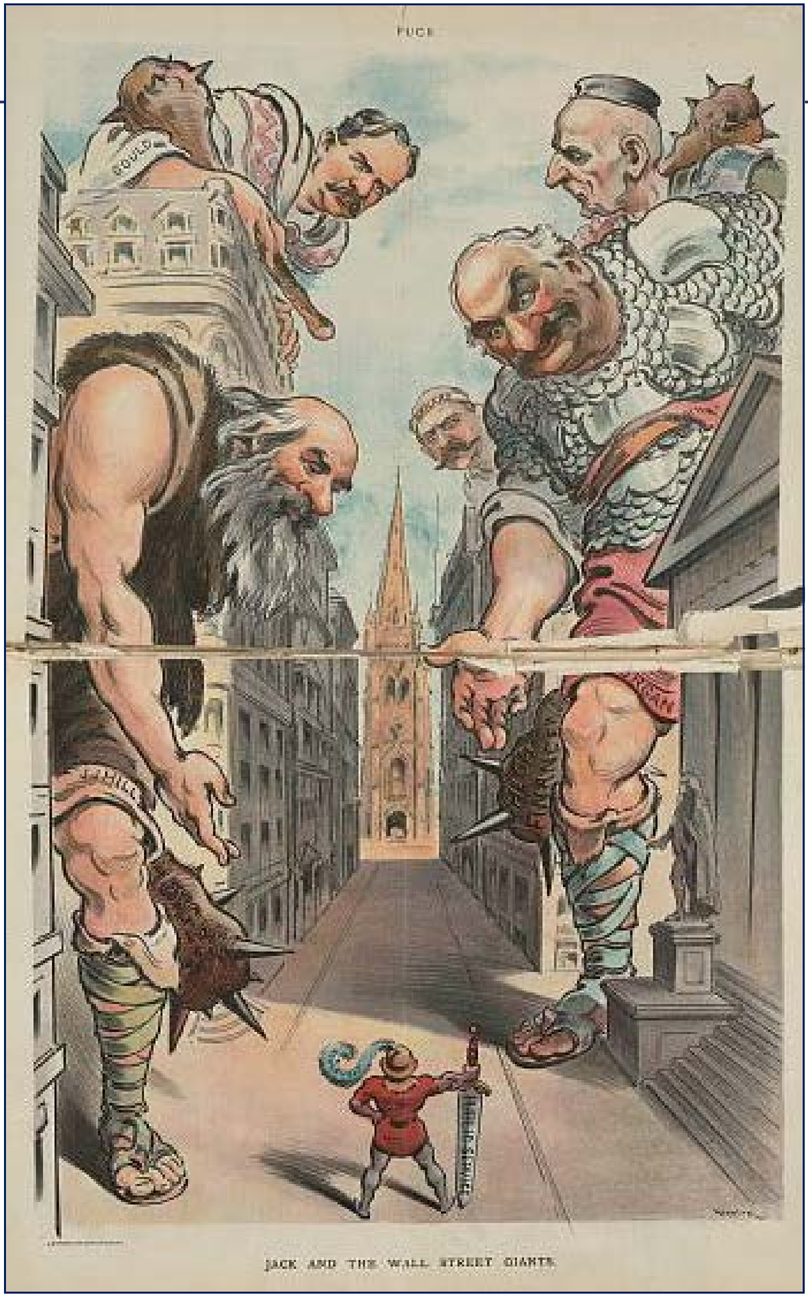
- The Interstate Commerce Commission (1887)
- The Sherman Anti-Trust Act (1890)

- The role of the United States Supreme Court
  - ✓ Corporate Personhood and Property rights
  - ✓ Freedom of Contract
  - ✓ United States v. E. C. Knight Co., (1895)

- Theodore Roosevelt, the Trustbuster
  - ✓ Swift & Co. v. United States (1905)
  - ✓ The Stream of Commerce Clause

- The Hepburn Act of 1906
- Woodrow Wilson, Corporate Diplomat
- The Federal Trade Commission 1914






This illustration, "Jack and the Wall Street Giants," shows a diminutive President Theodore Roosevelt standing on Wall Street, holding a large sword labeled "Public Service" before giant capitalist ogres labeled "JJ Hill" holding a club labeled "Merger", "Morgan" holding a club labeled "High Finance", and "Rockefeller, Oxnard, and Gould". Appeared in *Puck* magazine January 13, 1904. Artist is Udo J. Keppler.

Library of Congress
http://www.loc.gov/pictures/item/2010652337/

# 7. Corporate Power and the 20th century U.S. Economy

## Corporate Power in a Consumer Society

A. World War I as stimulus for big business
B. The Twenties, 1919-1932
   I. Hoover’s Dept. of Commerce and “Associationalism”
   II. Corporate Welfare
   III. The manufactured stock bubble
C. The New Deal, 1933-1940
   I. Organization for Survival
   II. Change of Course in the Supreme Court
   III. How Corporations benefitted from industrial unionism
D. World War II 1941-1945
   I. The Triumph of Corporate America
   II. The growth of International Corporations
E. Postwar Affluence after 1945
   I. Corporations and the American Way of Life
   II. Unions and the Popularization of the Stock Market
F. Globalization and the Revival of Free Market Ideology, 1979-
   I. Deregulation
   II. Anti-monopolism as a critique of globalization

Final slide.

Thank You