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THE FORMATION OF AMERICAN MARKETING AND ITS BASIC CHARACTER

by

Kazuyoshi Hotta

1. Preface

In looking back upon the history of American capitalism, we can point out as one of its outstanding features the growth of the so-called three major regional sections and the struggle among them. The three sections were formed, as is well known, in the 1st half of the 19th century, especially through the process of the internal improvement—the creation of the American system—advocated by the moment of the War of 1812–14, being closely related with the foundation of domestic markets. As Bogart et al. have expressed it, "the American people, who had hitherto faced the Atlantic Ocean and had been especially concerned with their relations to Europe, now turned their backs to the coast and devoted themselves to matters of internal policy and development."[1] And capital and labor were converted from familiar domestic and foreign commerce to speculation on land in the West as well as manufacturing in the Northeast.

The internal improvement brought about the rapid growth of domestic commerce by stimulating the development of transportation systems on one hand and the industrial specialization among the three sections on another. This was to tell that in America, which had long been laid on the status of economic colony of Britain and unable to find outlets of its products other than foreign trade, inland markets to absorb most of them were being formed, and to mean that the regional specialization of industry and the formation of urban economy were advancing. The differences of industrial groundwork of the three sections may be described as the Northeast depending mainly on commerce and manufacturing, the Middle-West on agriculture and mineral-resource exploitation, and the South on plantation staple. This industrial specialization, of course, resutled in the growth of production through regional division of labor and that of commerce to intermediate between regions. The flow of inter-sectional trade can be broadly divided, according to Schmidt,[2] into three patterns. The first is business between the Middle-West and the South utilizing the so-called Ohio-Mississippi system; second, coastal trade between the Northeast and the South along the coasts of the Gulf of Mexico and the Atlantic; third, trade between the East and the West through canals, the Great Lakes and railways.

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1) E. L. Bogart & D. L. Kemmerer, *Economic History of the American People*, Longmans, Green & Co., 1951, p. 215.

2) L. B. Schmidt, "Internal Commerce and the Development of National Economy before 1860," *Journal of Political Economy*, vol. 47, December, 1939, p. 800f.

Of course we don't say such flourishing domestic commerce immediately represents "marketing activities" with which we are concerned. This is evident in view of the character of market and product which constitute the two determinants to define marketing. That is to say, throughout the 1st half of the 19th century the markets remained to be local ones, widely scattered and homogeneous, while the products supplied by small-scale producers were simple, unspecialized and indiscriminate. Under such conditions most of goods were distributed through the network of sedantary merchants, and in such a sense, a static and uniform system of distribution was prevalent as has been pointed by Porter & Livesay.[3]

On such a distribution system the three sections, while maintaining complementary interdependency, on another hand were exhibiting sharp contrasts of interests about internal and foreign policies reflecting the difference of economic groundwork. Nevertheless, through the basis of the development process of internal commerce there was fixed a dynamic move in the market structure of America—whose industrialization had to be achieved amid the international division of labor set up on the Axis of Britain through the 1st half of the 19th century—, that is, the establishment of local market areas and the intensification of social division of labor. The Report of the Secretary of the Treasury for 1847–48 (Walker Report), for example, stated that "the value of our products exceeds three thousand millions of dollars....Of this $3,000,000,000 only about $150,000,000 are exported abroad, leaving $2,850,000,000 at home, of which at least $500,000,000 are annually interchanged between the several states of the Union."[4] Again by Andrews's Report for 1851–52 internal trade for the period recorded 1,461 million dollars, comprising 157 million by the Great Lakes, 170 million by rivers, 594 million by canals and 540 million by railways.[5]

The rapid growth of domestic commerce, as was described by Walker and Andrews, was estimated to have reached an annual amount of 1,500 million dollars by 1860,[6] allowing us to conceive that such growth played a role of inducing the formation of national markets in America. On this point Schmidt says the rapid rise and growth of the internal commerce of the United States was closely related with the end of the War of 1812 and, he appreciates "the rapid extension of internal commerce after 1815 gave rise to regional specialization, developed metropolitan economy, and diminished the dependence of the maritime and

3) Cf. G. Porter & H. C. Livesay, *Merchants and Manufacturers: Studies in the Changing Structure of 19th Century Marketing*, The Johns Hopkins Press, 1971, p. 2.

4) *Report of the Secretary of the Treasury*, December 9, 1847, in Bogart & Kemmerer, *op. cit.*, p. 305; and in G. R. Taylor, *The Transportation Revolution: 1815–1860*, Holt, Rinehart & Winston, Inc. 1951, p. 174.

5) I. D. Andrews, *Trade and Commerce of the British North American Colonies and the Trade of the Great Lakes and Rivers*, 1853, p. 905, in Bogart & Kemmerer, *op. cit.*, p. 305; in Schmidt, *op. cit.*, p. 818 and in Taylor, *op. cit.*, pp. 174–5.

6) Bogart & Kemmerer, *op. cit.*; E. R. Johnson et al. *History of Domestic and Foreign Commerce of the United States*, vol. 1, pp. 250–51.

staple-producing sections on Europe... [and the fact] marked the transition of the United States from colonial to national economy." Further he goes on to say, to observe the annual per-capita value of American exports from the end of the 18th century to the mid-19th century they decreased by a half "from $22.83 in the decade 1791–1800 to $11.27 in the decade 1841–50."[7] He thus pictures the relative decline of foreign trade against the sharp rise of internal commerce, pointing out the formation of domestic markets. Anyhow, such growth of internal commerce inevitably compelled the structure of commerce to change, and through the process the subjective body of marketing came to be established as the pivot of economic society.

II. *Transformation of the Structure of Commerce*

(1) Specialization by the steps and functions of commerce

In the early 19th century inter-regional transfer of commodities relied mainly on river-borne transport. Coastal cities of natural waterways and adjacent communities had dominant influences over the commerce of interior land. Urban merchants of early times were engaged in coastal trade and foreign trade, often by their own ships, or acted as agents for British merchants, and at the same time operated as wholesalers and retailers in the distribution of products. Specialization by steps was not yet seen in the structure of commerce except in some of bigger cities. They were non-specialized all-purpose merchants "who dealt in a wide variety of goods ranging from lace to iron bars."[1] In addition they managed transportation, finance and insurance for goods on their own capital account, and also worked as brokers or factors[2] with good knowledge on the scattered local markets. In short, the merchants of this period were generally in an undifferentiated state of function. Such basic character of early-day merchants, however, gradually began to change through the above-said internal improvement, the westward shift of the frontier, the rapid increase in population[3] and the industrialization policy stimulated by the British industrial revolution. The industrialization in America, with the cotton industry making its main axis alike with Britain's, gave an incentive to other related industries and caused

7) Schmidt, *op. cit.*, p. 798.

1) Porter & Liversay, *op. cit.*, p. 5.

2) Broker or factor is, so to speak, a product of mercantilism and entirely a middleman. They connected sellers and buyers for the sake of other people and were generally specialized in some single line of commodity. Their actions were never on their own account (capital calculation). They earned commission by performing the said functions.

3) For example, by the first census of 1790 the population of the United States was less than 4 million persons, which increased to 9,640 thousand by 1820 and to 31,400 thousand by 1860. (Cf. U.S. Bureau of the Census, *Historical Statistics of the U.S.: from Colonial Times to 1957*, 1960, p. 8 also see, Yasaka Takagi, America, Meizen-Shobō, 1948.)

expansion and deepening of market relations.[4] Again the population increase by an inflow of immigrants was reflected on commerce in the form of enlarged volume of trade.

Under these situations the conventional all-purpose merchants began to specialize by the medium of increasing trade. For example, they came to be specialized as exporters or importers, wholesalers or retailers, and by commodity lines dealt. Functionary also they showed a tendency toward specialization, that is, the emergence of specified-functional merchants. During this period merchants were making the axis of economic activities and their position superior to manufacturers' was the basic picture. Yet with such functional specialization among them the system of distribution was doubtless changed.

The immediate factors that gave birth to the new distribution system were the expanded and deepened market relations and the increase in trade with the growth of population. And those who played an important part here were jobbers and commission merchants. At least until the Civil War these middlemen (=specialized wholesalers) were true functioning as the basic unifier of economy in that they adjusted the flow of goods, helped and promoted improvement of transportation, and supplied credit and capital. They often sought commission business for the outlet of surplus money resources, took leadership in founding manufacturing firms,[5] and furthermore furnished manufacturers as well as farmers with working and long-term fixed capital to sustain production.

In America, where a state of capital shortage continued throuhgout the 1st half of the 19th century, financial aid to manufacturing, which was regarded as adventurous and unstable business, was often refused even by commercial banks, and so it was these specialized wholesalers that extended credit over many firms to facilitate them to raise capital money. On the other hand local merchants

4) In Britain the cotton industry had been completely placed on the factory system through the invention of the fly-shuttle by Kay in 1733, the jenny in 1764, the mule in 1779 and the power loom by Cartwright in 1785 as well as the use of steam for motive power. Such British cotton industry dominated extensive overseas markets being assisted by the foreign policy to lead many underdeveloped nations to a biased position of cotton-ware market and raw-materials supplier. Needless to say, America, notably the South, was being placed within the range of this policy. For instance, American exports of raw cotton were less than 5 million pounds annually in the 1790s, which rose to more than 385 million in the 1830s and to more than 1 billion in the 1850s. (Bureau of the Census, *op. cit.* p. 547). However, because of the easiness of new entry as regards technology and capital this industry gradually extended into developing countries with low-level capital accumulation. In America also it grew rapidly since the 1820s. This stimulated demand for machinery for work and motive power and the development of transportation for the expanded markets, which further awakened demand for iron and steel, machinery and other producer's goods.

5) T. Marbury, "Domestic Trade and Marketing," in H. F. Williamson, ed., *The Growth of the American Economy*, 2nd ed., Prentice-Hall, Inc., 1951. pp. 511–52; Porter & Liversay, *op. cit.*, pp. 7–8.

who came to commercial cities in the East, mostly once a year, for purchasing were managing general stores in rural areas. Thus it was these general-retailers that constituted the main channels of rural trade almost through the whole 19th century. At that period of cash shortage and a confused currency system, buying on credit was common among farmers, i.e., major customers, and so such general-retailers themselves asked intermediary wholesalers for long-term credit along with assortment of commodities. In such a case what made the ground of financial credibility were their monopolistic position in local markets and the function of collecting products. They were enjoying monopoly on local markets experiencing little competition except by peddlers. In addition they were almost the sole passage of transferring local products to other areas, performing collection and consigning to intermediary wholesalers.[6] Thus one of the principal business of the latter was to accept such consignment and inversely supply local retailers with imported and home-manufactured goods.

Contrastively as for the merchants of the rising inland cities and the North-east where manufacturing had developed earlier, it was rather usual to lie in a process of competition. Under the pressure of the presence of mass-transactions based on mass-demand of urban inhabitants and the attendant competition, they were orienting toward specialization of some extent and taking a step to specialty stores of, e.g., dry goods, food or harware. At the same time they purchased in bulk, so bulky as to be able to function as jobber, and reselling to the general-stores of adjacent areas. Such urban merchants, especially wholesalers, operated as consignment sellers or agents for manufacturers, and furthermore financed for the expansion of manufacturing by their usable funds, as was mentioned already.

As the result of such progress of specialization in the sector of commerce (=structural rationalization) after 1815 merchants came to exert stronger control on their specialty fields through better knowledge on them than did former merchants who carried multi-purposive and -comprehensive functions. However, on another hand such stronger control and higher efficiency were accompanied by unstability of merchants' position in the economic system. That is to say, formerly the all-purpose merchants—engaged in all kinds of activities related to trade, finance, transport, storage, collection of information, etc.—had been allowed to reign over the economic system as the leading unifier and to stand aloof from environmental changes for the very reason of such basic character. Now, the appearance of specialty merchants differentiated by specified commodity lines or functions realized more economically-rational activities, and rendered stronger control to merchants than in the case of all-purpose forerunners. Thus far the specialty merchants took leadership in economy, yet the advance of specialization increased dependency on specified commodity lines or specified functions and hence it became impossible for them to remain isolated from the effects of environmental fluctuations. They became more unstable compared with the transcendental being

6) Marbury, *op. cit.*, p. 511.

in the economic system (all-purpose merchants) and were changed to a being subject to circumstances.

As the specialty merchants, especially wholesalers, came to hold such character, their position as the dominant leader of economy came to be menaced by modern manufacturing enterprises.

(2) Decline of merchants' position and self-reliance of manufacturers

As regards the event that merchants were obliged to evacuate the position of basic unifier of economy, various causes are conceivable. The most fundamental one is relevant to changes in the character of market and product. For example, the transformation of markets from scattered and small-scale to concentrated and big-scale ones, the differentiation of products and the appearance of technically complicated products have been often mentioned. Where these changes have essential influences there is born a tendency toward direct contact between producer and customer, which causes a structural transformation of distribution, that is, elimination of middlemen.

Now, essential ones of the changes in the character of market are the emergence of oligoply accompanying the rise of big firms and the concentration of market due to the growth of cities. In the case of America the market relations had been expanded and deepened with the development of the cotton industry and thereby induced iron, machinery and mining industries since the early 19th century, which was further accelerated by the rapid progress of railway. The American railway industry developed receiving gratis grant of land and materials for construction from States and the Federal Government, while on another hand issuing stocks of a vast amount as joint-stock corporations. The large demand flowing from this industry gave stimulus to related materials-supplier industries and invited new entries into these. Among such materials-suppliers those with spare financial resources, e.g., those taking partnership with commercial capitalists, had early realized backward integration.

In addition, due to the divisional system of management, which such a big body as railway companies had to introduce, orders flowed out from purchase divisions directly to materials suppliers, and since they were often desinged on professional specifications there was born contact between technical personnel of railways and suppliers. Thus by the medium of the development of railways, in the related supplier industries such selling increased importance as was directed to those customers who were relatively of small numbers yet gave a large quantity of orders, in place of unspecific small-scale customers of large numbers. In other words, in accompany with the expanding scale and decreasing numbers of both sellers and buyers, producers found it more efficient to perform wholesaler's function by themselves than to rely on the conventional independent merchants.

Alike with the case of producer's goods industries, also in consumer's goods there were created intensive markets in accompany with the growth of cities.

While in the small-size and scattered local markets middlemen with a facilitating function were indispensably required, the growth of thick markets by dense urban population continuously generated a huge quantity of demand, hence sales, which allowed manufacturers to create their own sales forces to take charge of wholesale functions. Of course this needed improved transportation and communication systems. Where these were available manufacturers of consumer's goods showed a move to control wholesale activities in urban areas by their own hands. Such a tendency of eliminating middlemen depended, to speak broadly, on the formation of urban markets with mass-demand, or the emergence of partial oligopoly on some particular phase of successive steps of distribution, that is, materials to finished products. This tendency was not one directly supported by the conditions for the birth of modern marketing, in other words, the interests of traditional network of distribution and those of manufacturers exhibit severe opposition by the medium of competitive relations defined by the structure of industry. For instance, although in the recession time following the 1857 panic destructive competition was developed under diminishing demand and falling prices, it was merchants that strategically systematized stabilization of prices and pooling of orders.[7] In this sense the tendency of eliminating middlemen observed in some sectors was not one due to inadequate ability of merchants or request for the sake of competition among oligopolists. In fact it was only after 1873, notably in the late 19th century, that the industrial structure began to show an overall transformation and oligopolization advanced over almost all major industries.

And where middlemen were unsuitable for merchandizing, that is, where products were of technically complicated nature and of relatively high price, and hence close contact between producer and consumer (e.g., exhibition, instruction, repair, and so on) was necessary, often a unique structure of distribution was seen. For instance, manufacturers of machinery, electrical equipment, harvester, office machinery, etc. had to accomodate such services as technical consultation, instruction of operation, spare parts, repair facilities and so forth. Unacquainted with these matters, commission agents and brokers were very unsuitable to distribution channels. Accordingly for industries dealing with these products it was impossible to rely on the traditional channels, and they were obliged to create systems of selling by themselves.

Similarly in the case of industries that required special facilities for storage, transport or selling, and where middlemen were not glad to invest money in these, such a tendency appeared. In the industries of ice, meat, banana, beer, etc. it was necessary to overcome the perishability of these goods in order to secure potential urban markets getting over the boundaries of limited local selling. Although this problem was solved for the production process by improved refrigeration, the existing distribution channels hesitated or refused to go into such investment for the adoption of new techniques needed to distribute those

7) Porter & Livesay, *op. cit.*, pp. 3–4, 11, 119.

goods. Here again producers were unable to depend on the customary channels and forced to develop new ones through investment of a large amount. As above, where the conventional merchants did not show necessary responses, producers themselves subrogated intermediaries. Such industries did appear.

The elimination of middlemen for the reason of changing character of market and product, however, was to turn to the essential factor of modern marketing being assisted by the extended concentration in economy and the exposure of over-production as well as by the consequent transformation in the structure and behavior of competition. Yet the birth of marketing of this sense had to be waited until the close of the 19th century. In the phase preceding to it generally markets remained to be dispersed and unconcentrated nature except in some cities, and direct contact between producer and customer was only a particular case. So the tendency to eliminate middlemen seen in some specific sectors can be regarded to have been a primitive element of modern marketing.

From this point of view it is necessary to grasp the decisive factors that brought about changes in the relation between merchants and manufacturers. As was mentioned already, through the economic development in the 1st half of the 19th century specialization by commodity lines or functions proceeded among merchants. While this gave birth to more rationalized and efficient distribution of goods, it was combined with an effect of making merchants subject to environmental changes. Beside this, as the traditional, scattered markets began to show internal structural transformation, objective conditions were completed to enable manufacturers to take charge of the wholesale functions. Throughout this period, however, generally manufacturers sold their products simply to wholesalers in order to evade possible troubles and expenses attendant to selling to varied and unspecific customers, and to keep aloof from uncertainty of collecting prices. Merchants placed themselves on such a position despite the changes in environmental conditions just because of the financial power of merchants. For this period manufacturing of America was being chronically worried by the lack of capital. Accordingly capital money wanted and raised by manufacturing firms, except some industries, was generally mosaic consisting of personal investments of proprietors or partners, borrowings secured on real property, and short-term credit or advance by merchants engaging in material supply or sales activities of manufactured goods. These funds did not immediately fulfil the need of long-run fixity of capital inherent in manufacturing. These had to be inserted into long-term capital by writing obligations or renewing them on necessary occasions. Such a means of finance was accompanied by high-interest charge, which worked as a factor to swallow up profits even at boom times and increased pressure of fixed debt in recession times, leading to weed-out of marginal firms and deepening of depression.[8]

8) *Ibid.*, p. 118. However, the cotton industry alone, some of whose products had grown up to possess international competitive power, was enjoying a favored

It was the Civil War that gave a Copernician change to such a financial state which characterized manufacturing of the 1st half of the 19th century. The appearance of Lincoln on the stage in 1860, following the 1857 panic, rendered inevitable the confrontation between the South and the North, which was so serious as was enough to crush prevalent optimism on business. Having broken out, however, the War opened up for manufacturers a way toward continuous mass-demand, price rise, shorter term of payment, transaction on cash and approach to capital market.

The emergence of mass-demand by the War furnished manufacturers with seller's market. This resulted by itself in the increase in commodity prices and the acceleration of inflation, which were further spurred by the circulation of the greenback paper. The greenback dollar had never recovered its par price during the War, falling to 45 cents on gold value by the summer of 1864.[9] Under these situations most manufacturers obtained capability of price control, unthinkable before the War, and gained enormous profits that did more than cover the increasing costs of materials and labor. Amid such a war boom an entrepreneur did not hesitate to write "I am in no hurry for peace."[10] In addition, manufacturers' burdens of past debts were depreciated to one-third or one-fourth of the prewar level. The larger profits and the depreciated debts; these two events not only cut off the vicious cycle of capital-raising by debt, but also enabled many firms to clear off their debts and furthermore to make long-term capital investment with their own funds. This is seen in the rise of the ratio of manufacturers' capital assets to GNP from 3.4% ($137 million) in 1859 to 6.9% ($441 million) in 1869.[11] Thus being freed from dependency on merchants' finance in the aspect of long-term capital investment, as regards short-term working capital as well manufacturers went the way toward self-reliance.

The self-reliance in short-term capital depended much on the sharp fall of the value of money due to inflation and the issue of the greenback. This meant increases of risks attendant to long-term credit, and hence affected the way of goods transaction. That is to say, the appearance of excess demand and the acceleration of inflation in the war time enabled manufacturers to insist on business on short-term credit or cash. Since in this way manufacturers' profits

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position in raising money resources. It was able to avail investments by stockholders, retained incomes, or loans from financial intermediaries such as banks and insurance companies. By about 1860 it had relatively high ability of payment. (Cf. M. T. Copeland, *The Cotton Manufacturing Industry of the United States*, 1917, Reprints of Economic Classics, A. M. Kelley, 1966, pp. 14–15; my paper "Kokunai Shijō-ron no Seisei," *Mita Shōgaku Kenkyū*, vol., 15, No. 3.)

9) H. U. Faulkner, *American Economic History*, 8th ed., Harper & Row, Publishers Inc., 1959, Japanese transl. by K. Ohara, vol. 2, p. 670.

10) Quoted from W. W. Watts to Huston & Penrose, Feb. 12, 1862, Luckens Steel Company Papers, in Porter & Livesay, *op. cit.*, p. 120.

11) Porter & Livesay, *op. cit.*, p. 124.

were realized at once with sale to merchants, not only short-term working capital became securable but also burdens of interest payable for borrowings or advance payment decreased, cutting off the said vicious cycle. In addition manufacturers regained independency about management which had been restricted by the financial reliance on merchants. It became possible to avoid intervention of merchants about the sorts of goods to be produced as well as prices and other conditions of transaction.

Again the Civil War was a mediator for the development of American capital markets, providing a moment to link the money of general people with the manufacturing sector. That is, Government's bonds for war finance, amounting to 2,846 million dollars on Sept. 1, 1865, the largest prior to 1917,[12] were floated through capital markets, and the proceeds were mostly handed over to manufacturers as payment for Government's procurement of goods. And for manufacturers who were paid with government's obligations a new way of discount on private banks was opened. Thus business connection was settled between manufacturers and financial institutions, say, for the first time. Now manufacturers had got over the status of "adventurous business." As they came to be recognized as important clients by financial institutions, on the other hand some of merchants were specialized as financiers. This implied new specialization among merchants and abandonment of the distribution function. Thus through contact with private banks carrying trade finance and financial institutions having evolved from brokers and commission merchants, transfer of people's funds to the manufacturing sector was steadily advanced after the War, and there was established specialization in the commerce sector (=fall of wholesaler's position=change to selling agent).

III. Rise of Big-Scale Firms and Oligopolization in Industries

The Civil War, while fostering structural and functional specialization in the commerce system still further, made decisive the decline of merchants' position and the self-reliance of manufacturers in the economic world. The vast amount of demand, and that for standardized goods, side by side with the enactment of the protective tariff acts of 1862 and 1864 as well as the acceleration of inflation by the issue of the greenback, did suffice to provide manufacturers with seller's market and to stir up their willingness to expand production,[1] and promoted the trend toward mass-production of standardized goods and hence to large-scale mechanized industries. And through these processes control over business activities was concentrated on the hands of firms of limited numbers

12) Faulkner. *op. cit.*, Japanese transl. *op. cit.*, vol. 2, pp. 664–666.

1) W. C. Kessler, "Business Organization and Management," in H. Williamson, ed., *The Growth of the American Economy*, 2nd ed., Prentice-Hall Inc., 1951, p. 603; Porter & Livesay, *op. cit.*, esp. Chaps. 7, 8. Industries of woolen textile, shoes and iron and steel products gained most greatly.

and large scale.

The concentration of business which had been observed since earlier times in the railway sector, spreaded at this period by the weight placed on production and the orientation to scale expansion as well as by the cut-off of marginal firms through the postwar depression, and after the 1870s it advanced rapidly in the mining, processing and manufacturing industries. For the thirty five years after the Civil War there was a prolonged fall of prices, including the two panics of 1873 and 1893 called "the worst in the American history."[2] On the other hand this period saw level-ups of relations around market such as the technical improvements in textile and iron and steel manufacture, the development of steam power and the construction of railway network. In many industries business scales were expanded in order to control important sections of market, and pursuit of economic efficiency through integration and combination was intended. That was pursuit of technical efficiency implying evolution of machinery, specialization of labor and plant, and vertical integration of successive steps of production. The scale expansion of individual plants led to bigger business units through integration or combinations in the 1870s. This move is observed in the fact that, with the number of manufacturing remaining almost unchanged, capital investments in manufacturing showed an increase of 65% and output of 58%.[3]

It did not take long for such rises of large-scale plants and firms to fall into over-capacity at this period generally pierced with a recessionary phase, which affected to deepen and prolong depression. However, excepting some years of the most serious scene, demand was expanding, being supported by the increase in population. For example, up to 1890 American inhabitants grew at a rate of 25% for every ten years, and this trend continued later on though the rate showed some decline.[4] Needless to say, immigrants contributed to such increases, totaling to 27,772 thousand persons between 1861 and 1916. With over-capacity on one hand and expanding demand on another, competition for market control was inevitably sharpened. That is to say, the general over-capacity, by the medium of the expanded demand, affected individual firms unequally. The keen competition took a form that bigger enterprises with large-scale plants expelled

2) Cf. W. L. Thorp, *Business Annals*, National Bureau of Economic Research, 1926, pp. 77–80.

3) J. S. Bain, "Industrial Concentration and Anti-trust Policy," in Williamson, *op. cit.*, p. 617. That the scale of production unit was growing larger is seen in the increase in the average estimate of capital amount per establishment from 19 thousand dollars in 1879 to more than 36 thousand (U.S. Bureau of the Census, Historical Statistics of the United States: From Colonial Times to 1957, Government Printing Office, 1960, pp. 409–10).

4) Kessler, *op. cit.*, p. 605. Tomoyuki Ishihama, *America-Shihonshugi-Hattatsu-shi*, Kōdosha, 1948, p. 171. Immigrants for every ten years from 1861 to 1910 were: (in 1000 persons):

1861～1870	2, 315	1891～1900	3, 844
1871～1880	2, 812	1901～1910	8, 795
1881～1890	5, 247		

rivals of small and less efficient plants out of business. It involved thorough-going price-cutting war with advantageous capital and cost differences for a background as well as moves to oppress competition of rivals by means of strong market control in local markets.

What worked to intensify such competition further was the continuous development of railway network. Between 1880 and 1890 railways of about 70 thousand miles were constructed, which drove many lines to competition through better service and lower rates. This meant lower transportation costs for manufacturers, notably of big ones, and hence emancipated them from narrow local markets. As the result major firms which had established control over local markets came to be connected with direct competition for sale on a single national market. Under this situation price-cutting war unescapably led to destructive competition for all participants.

With the advance of such a tendency competing firms of many industries began to endeavor to adjust and maintain the structure of prices at profitable levels and further to gain extra profits. For the serious price-cutting war was never their aim itself but merely a temporary means to effect elimination of competition and fortification of control in the end. The confrontation of big firms on national markets, however, was not easy to settle so long as it relied on price cutting, only to invite a destructive situation. In order to evade such a misery, to eliminate competition and to strengthen control, another way, namely, business combination was taken.

The move of combination appeared after the 1873 panic, gradually advanced from 1879 to 1896 and then rapidly developed between 1897 and 1904. Wishes to control supply of goods and to eliminate competition for the aim of extra profits were born strongly among those industries that needed a high ratio of fixed cost such as railway, iron and steel manufacture and mining, and also in the fields of oil and tobacco some competitors went into such an attempt though in a relatively small number. Business combination was first devised as a series of gentlemen's agreements pools, but gradually advanced to the form of trust or holding company with stronger binding force.

Pool is an interest agreement to divide profitable business and to control prices among participant members, taking the form of allocating transactions, areas or markets. It was seen in the railway, brewing, iron and steel, and wire industries, but proved less effective for price control. The pool of railway companies was judged to be an offence against the Interstate Commerce Act in 1887. Again in 1896 the Trans-Missouri Freight Association was sentenced to illegality by the Supreme Court. So after 1887 pools decayed and there appeared a pattern of agreement likely to be more effective and lawful, i.e., trust.

Trust is a system by which stockholders, who conclude a trust agreement, entrust common shares to the board of trustees and in turn received trust certificates, and the trustees exercised full control on the assets of trust with absolute competency. This system utilized the customary legal concept of trust in the custom law, while on the other hand intending to escape application of the custom-law provision that prohibited joint-stock companies from holding shares of other companies. This was employed first by the Standard Oil Company in 1882, and subsequently the trusts of whisky, sugar, lead, cottonseed oil and so on were organized. The powerful control by trust, however, aroused counterpower against itself such as the antitrust laws enacted by several States after 1889 and the Sherman Antitrust Act by the Federal Government in the next year. Although the Sherman Act did not bear any effects worthy to mention, the dissolution of North River Sugar Refinery in 1890 ordered by the New York State Court and that of the Standard Oil trust in 1892 by the Ohio State Court dealt a decisive blow to combination by this form, which was further retarded by the 1893 panic and subsequent recession. However, these judical decisions alluded to nothing about monopolization itself, standing on the reason alone that these trusts offended the competence warranted by licence. So they could not prevent the move toward monopolization.[5]

As a way to avoid application of antitrust laws and to proceed to monopoly the system of holding company was employed at the most active period of combination, 1897 to 1904. This was a device to govern other companies by holding or controlling some portion of shares, and use prevalently being induced by the amendment of the corporation law in the States of New Jersey, West Virgina, Delaware, Maine and so forth. Between its first appearance and 1904 business integration advanced more or less in almost all major industries until there remained few fields still to conquer. The aspect of combination as of 1900 is shown in the table below. The marked progress of combination in the form of holding company, however, came to invite regulation on monopolization itself, as will be studied later in this paper.

Aspect of Business Combination (as of 1900)

Industry	Combinations	Divisions Involved	Industry	Combinations	Divisions Involved
Iron and steel	40	447	Leather ware	5	100
Food	22	282	Paper & printing	7	116
Chemicals	15	250	Lime, glass & stone products	15	180
Nonferrous metals	11	89			
Drinks	28	219	Lumber	8	61
Vehicle	6	65	Miscellaneous	16	118
Tobacco	4	41	Total	185	2, 040

(Source: T. Ishihama, *America Shihonshugi Hattatsushi,* Kodosha, 1948, p. 217)

Thus by about 1905 almost all major industries showed oligopolistic structure or had a strong oligopoly core, with the power of market control concentrating

5) Faulkner, *op. cit.*, Japanese transl., vol. 2, pp. 557–558.

on a few number of big firms. For example, 318 cases of combination were seen up to 1904, and annually on average 301 firms disappeared through merger in ten years from 1895 to 1904. The 318 firms after merger had absorbed 5,200 individual manufacturing plants, and were estimated to hold about 40% of the total manufacturing capital at the time.[6] Seventy eight combinations of the largest scale administered one-half of respetcive sectors, 57 more than 60% and 26 more than 80%.[7]

The process of such business merger lasted even after 1905 till the mid-1930s though at a slower pace and more selectively. It is well known that in the in-between 1920s there was seen a dramatic progress of concentration. It appeared mainly in new industries such as automobile, radio and film, in some industries such as food processing, metals and oil, and in public utilities, notably electric power and gas, for which a huge amount of capital was necessary and regional monopoly was legally authorized by the government.

The concentration and combination in many industries, especially in the "age of trust mania up to 1904," "transformed many industries formerly characterized by many small and medium-sized firms, into those in which one or a few very large enterprises occupied leading positions. It laid the foundation for the industrial structure that has characterized most of American industry in the twentieth century."[8] With such a stage being once arrived at, the former pattern of competition gave way to complicated competitive relations among giant industrial capitalists. In other words, by this period the competitive behavior showed a change under the flank pressure of the structural transformation of American industries, leading to the substantial foundation of modern marketing.

Now, before going into the problems of marketing at its birth, it may be necessary to cast a glance at the factors that supported the above-observed moves. For it is unoverlookable that these factors composed the objective condition to prepare for the establishment of the subjective body of marketing, and furthermore some of them were directly related with competition itself and hence made the force that gave orientation to the formation, development and refinement of marketing.

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6) Cf. J. S. Bain, *Industrial Organization*, 2nd ed., John Wiley & Sons, Inc., 1968, pp. 104–5; J. Moody, *The Truth about the Trust*, Moody Publishing Co., 1904, pp. 485–87; R. L. Nelson, *Merger Movements in American Industry: 1895~1956*, Princeton Univ. Press, 1959, p. 34.

7) Moody, *op. cit.* As of 1909 oligopoly was predominant in the industries of tobacco, oil, rubber, primary metals and electrical appliances, while those of cotton textile clothings, wood, furniture, paper, printing and leather were non-concentrative. (Cf. Porter & Livesay, "Oligopolists in American Manufacturing and Their Products; 1909~1963," *Business History Review*, vol. 43, No. 3, 1969, p. 283.)

8) Nelson, *op. cit.*, p. 5.

IV. Background of Business Combination——mainly referring to the antitrust policy

As explained in the previous section, where large firms of a few number confronted each other on a single national market by the medium of price, competition often inclined to be destructive, so destructive as to render profit completely unexpectable. Facing such a situation firms pursued bigger plants and organizations that might realize higher technological efficiency, and groped means to exert control over competition or to eliminate it. And the means adopted as most simple was controlling of supply and promotion of combination. Generally combination took the form of uniting several firms of an industry into a single joint-stock company or holding company, through which closing of inefficient plants, expansion of efficient ones and vertical integration of varied types were performed. As the result in some cases virtual monopoly was realized, while in others concentrative oligopoly was formed, that is, a large share of production capacity of an industry was placed under control by a single firm and the rest was left to a few number of firms big as well as small.[1]

Now, for the foundation of such big firms enormous accumulation of capital was necessary, to whose implementation much contribution was made by the licence of incorporation. Although already before the Civil War some joint-stock companies with monopolistic or special privileges existed for turnpike, canal or railway construction, these were licenced case by case by special act and through deliberation by the legislature. For example, in Vermont companies incorporated under special act counted 42 in 1836, which increased to 58 in 1865 and to 66 in 1870[2] The request for founding joint-stock companies was intensified by the moment of the Civil War, leading to the enactment of the general corporation law in many States. Under this law the way of establishing a joint-stock company was opened up to every one who applied for it, on equal conditions. And the standards in the corporation law became more relaxed than were formerly.

The first step of mitigating regulations on corporation is said to have been the general corporation law of limited nature introduced by New Jersey in 1849, yet what worked effects most essentially in the sense of changing standards of joint-stock company was the approval of holding company of 1888 in this State.[3] Formerly holding companies had been permitted only under particular circumstances but since 1890, following the legislation in New Jersey, the move to simplify the corporation law extended over many States as well. Thus, after this period new-born big enterprises took the form of joint-stock company and

1) H. G. Seager & C. A. Gulick, *Trust and Corporation Problem*, Harper & Bros., 1929, pp. 49–71.
2) Kessler, *op. cit.*, p. 609, fn. 14.
3) Cf. H. W. Stoke, "Economic Influences upon the Corporate Laws of New Jersey," *Journal of Political Economy*, vol. 38, No. 5, Oct. 1930, pp. 551–79.

combination among firms was typically realized on the pattern of holding company.[4]

With the growth of corporate undertakings, brokers engaged in stock-market or securities business as well as investor bankers came to hold an important position in the American economy. The spreading of joint-stock company, along with the increases in output as well as employees, generated need of a huge amount of capital. In many industries it proved apparent that such a means as proprietor's enterprising or partnership was inadequate to raise necessary funds for large mechanized firms.[5] It was investment bankers that fulfiled this need, who at the same time were feeling the necessity of avoiding destructive competition from the viewpoint of safety of invested funds. For this reason bankers often intervened in the problem of management and further proceeded to control on industries. By directing business combination banks and other financial intermediaries were able to gain swelled capital and commissions in a large amount, and hence their profit-seeking behavior worked as an important factor that fostered combination.

And some aspects of American legal institutions were closely related with the advance of combination. Typical ones of such were the Federal patent law and antitrust laws. The former granted exclusive privileges to useful and original invention about production and sale for seventeen years. To get a patent facilitated one or a few firms to shut out rivals and to establish monopolistic or highly concentrative control in the relevant industry for an appreciably long time. In ten years between 1890 and 1900, when combination was actively advanced, patents counting 234,956 were authorized.[6] It is also unignorable that the Federal antitrust laws were relevant to the progress of combination, though seemingly paradoxical.

At the period prior to the merger movement the Federal Government had been setting forth the well-known laissez faire for the principle of economic policy. Exceptional, however, was the protective tariff policy which had been taken since the early 19th century. Notably the high tariff system, continued from the Morrill act of 1861 almost up to the mid-1930s, not only was deviation from the laissez faire philosophy but also furnished a favorable condition for the growth of big firms and combinations.[7] Excepting such a tariff policy,

4) Bain, Industrial Organization, pp. 67–8.
5) As other advantages attendant to the joint-stock company system we can mention limited liability of proprietor, easy management by the separation between ownership and business, lower costs by the division of competence, and monopolistic control by means of affiliated firm (inclusion of external economy.)
6) Faulkner, *op. cit.*, Japanese transl. *op. cit.*, vol. 1, p. 327, vol. 2, p. 525. It may be seen that this number of patents is very large compared with 276 for 1790–1800, 6,460 for 1841–50 and 25,250 for 1850–60.
7) While most trusts including Standard Oil and American Tobacco obtained few or no direct benefits from tariff, the sugar trust enjoyed monopolistic profits.

however, merely regulations of minimum degree were put forth on the belief that competition among private business enterprises in the domestic market would provide a sort of appropriate, automatic control to the interests of all people.

The early phase of combination involving predatory competitive tactics, restrictive agreements and pools were governed by such a belief. Repulsion against the acts of big firms, however, became strong on the side of farmers and smaller firms directly suffering damages on profits. Especially farmers set up earnest campaign against combination as a part of their political plans asking for relief from the inflationary currency reform, in addition to their opposition to high railway rates and protective tariff for manufactured goods. Such antagonism was thrusted on the government as the demand for prevention and regulation of monopoly by the Greenback Party in 1880 and by the Anti-Monopoly Party in 1884. Again in 1888 the Republican, Democratic, Prohibition and United Labor Parties took up this demand in their platforms. Amid such moves twenty seven States or quasi-States of the South and the Middle-West made legislation for the aim of preventing or destructing monopoly one State after another up to the end of 1890. And fifteen States provided it a principle in their constitutions. These laws anew and more clearly stipulated existing prohibition of monopolization or restriction of competition by the custom law, but were subject to limitation due to the property of state law. That is, a law of a single State was unable to check activities of combinations incorporated in other States, possibly of mild attitude. Since generally combinations extended their business on a nation-wide scale, the status of single-State law resulted in a situation that such laws were almost ineffective, in other words, combination was left free.

The rise of opinions against monopoly generated demands for the Federal law to break such limitation. Meanwhile in 1888 an investigation conducted by the committees of the House and New York State Senate confirmed the evils of monopoly, and in Dec. 1889 President Harrison presented the President's Message to the Congress asking for legislation to control trusts of collusive character. Thus the Sherman Antitrust Act was born in 1890. It is to be noted that this was enacted not for its own sake but for an intention to pass the Mackinley protective tariff act, that is to say, it was utilized to appease farmers' strong opposition.[8]

The basic principles of the Sherman Act, comprising eight Sections, are

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H. O. Havemeyer, its first president, dared to say publicly "the mother of all trusts is the customs tariff." (Faulkner, *op. cit.*, Japanese transl. by Ohara, *op. cit.*, vol. 2, p. 551.)

8) Bain, *op. cit.*, "Industrial Concentration," p. 625; Faulkner, *op. cit.*, Japanese transl. by Ohara, *op. cit.*, vol. 2, pp. 570–71, 715–16. In the 1888 President election the customs problem made a big issue for the first time in the American history. By the Mackinley Act duties were raised to 49.5% on average.

shown in the 1st and 2nd. "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby decleared to be illegal" (§1); "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor", (§2). And the Act approved fines and imprisonment to the offender as well as threefold indemnity to the injured. However, these provisions were too simple and comprehensive, and in addition were lacking in the clear definition of "contract, combination..., or conspiracy, in restraint of trade or commerce," in particular leaving much room of interpretation of the concepts of "restraint" and "monopolization." Because of these defects and the lack of Government's concern on enforcement, little effect was born for the first fifteen years. Especially the decision of the Supreme Court on the U.S. vs. E.C. Knight case (156 U.S. 1) revealed impotency of this Act about monopolization and greatly retarded determination of the scope of its application. The ground of the decision was that the Act should be applied only to such monopoly as might restrict trade, and mere acquisition of sugar refineries or refining is not commerce in the strict sense in the Constitution; monopolization in manufacturing affects commerce only indirectly and incidently; it is not monopoly in inter-state commerce; and hence be exempt from the application. Thus the Court rejected dissolution of the monopolistic combination which acquired four rival plants in Pennsylvania, placed almost all refineries of the United States under the single ownership, and controlled more than 95% of sugar refining. Furthermore the Court stated that the real intent of the Congress is not limitation of the rights of corporation to acquire, control or dispose assets, and that the Act possesses no validity of application to monopolization or restriction by integration or merger which is inevitably accompanied by transfer of assets, thus suggesting even a possibility of overall exemption for all sorts of restriction. However, this decision, which seems rather likely to promote merger, was later removed by the two dicisions of illegality upon two railway agreements of 1897 and 1898 (U.S. vs. Trans-Missouri Freight Association, 166 U.S. 341; U.S. vs. Joint Traffic Association, 171 U.S. 505), and the decision on the U.S. vs. Addyston Pipe and Steel Co. case. In the latter mentioned case a competition-restrictive agreement among iron pipe manufacturers was held illegal because the members of the pool were related with trade across State borders. This was an important decision in the point that it alluded to the "per se rule" of illegality,[9] that is, any behavior leading to trade restriction and monopoly is in itself illegal regardless of circumstances. Notwithstanding these decisions, it was only by the Northern Securities Co. et al. vs. U.S. case of 1904 (193 U.S. 360) that the Sherman Act was confirmed

9) Bain, *op. cit. Industrial Concentration*, p. 626; A. Phillips, *Market Structure, Organization and Performance*, Harvard Univ. Press, 1962, pp. 200–1.

to be applicable to merger, integration or other business combination accompanied by transfer of assets. This may be seen in the fact that until this year combination advanced intensely. While thus combination was left almost unconstrained, the Act was often utilized to suppress labor movements. For instance, against the Pullman strike of 1894 the court laid injunction for the reason that the act of the union was a conspiracy impeding interstate commerce, and again in the Dunburry Hatters case (Loewe vs. Lawlor 235 U.S. 522) the union members were decided to be liable for the loss incurred on the company by boycott extending over several States up to the sum total of their personal wealth. This was by the application of the Sherman Act. Furthermore, the validity of labor union itself was doubted, and even such courts appeared that held that labor unions are illegal combinations by reason of restrictive codes and practices in the light of either the custom law or the Sherman Act.[10]

Under the antitrust policy applied on such "creative interpretation of law" there was seen alarming development of merger after the American-Spanish War. Against this, muckrakers' repulsion appeared toward abuse of monopolistic power and oppressive attitudes neglecting public interests by big firms. This movement of exposing the real facts of monopoly, being combined with the spirit of the time of populism and progressivism, gave birth to public opinions asking for reform. It was a current of thought based on the idea that state be responsible for active work for people's welfare. It pursued realization of the ideal of democracy by sweeping away the evils arising from adhesion between industry and politics, and in the economic aspect required intervention of state rejecting laissez faire and selfish individualism.[11]

Against the background of this thought, vigorous attacks on trusts began after 1902. In this year President T. Roosevelt accused trusts in a canvassing tour and in the next year Congress passed three laws to regulate big firms: *act to quicken court trials* giving priority to Federal Government's suits pursuant to the Interstate Commerce Act or the Sherman Act; the Elkins Act prohibiting rebate of railway freight, a wrong practice of railway business; act to found the Department of Commerce and Labor with a subordinate bureau—the Federal Bureau of Corporations—to make diligent investigation into the organization, conduct and management of corporations. And in this year a suit was brought about against a holding company, the Northern Securities Co. which was controlling the stocks of competing railway companies of Great Northern, Northern

10) Faulkner, *op. cit.* Japanese transl. by Ohara, vol. 2, pp. 573–4, 609. It was after the Clayton Act (1914) that by a new orientation labor unions were exempted from application of antitrust laws and effective regulation on firms was set forth for the main object of laws.

11) Cf. R. Hofstadter, *The Age of Reform: from Bryan to F.D.R.*, Alfred A. Knoff Inc., 1955, Japanese transl. by M. Saito, et al., America-Gendaishi, Misuzu-shobō, 1967; Y. Takagi, America, Meizen-shobō, 1948; and ditto, Kindai-America-Seijishi, Iwanami-shoten, 1957.

Pacific and Chicago-Birlington-Quincy, intending monopolization of transportation in the Northwest. In the following year the Supreme Court held that the company was in itself illegal in that it constrained interstate commerce, and it should not be exempt from application of the Sherman Act for the mere reason that it was a holding company authorized under the New Jersey corporation law.[12]

Beginning with this decision, the progressives idea marked steps toward its implementation including the enactment of the Pure Food and Drug Acts and the Meat Inspection Act of 1906. However, until several years later it was not established that monopolization in manufacturing should pose an offence against law, partly being affected by the calm-down of the first merger movement. Nevertheless the effort of earnest enforcement of the Sherman Act, started under Roosevelt's regime, was followed by Taft's and Wilson's governments. For example, during the period of Roosevelt 19 civil and 25 criminal actions were taken on the Federal Court, while for the Taft's and Wilson's (first) periods the cases, including that of restrictive agreements, counted 43 and 53 respectively. Especially between 1905 and the World War I attempts were advanced to disolve existing combinations which were controlling industries. Notable issues for this "trust busting" period were with the Standard Oil of New Jersey and the American Tobacco, for both of which dissolution was ordered in 1911 by reason of offence against the Sherman Act.

The Standard Oil, virtually controlling oil refining, contended in the trial that its control over subordinate firms was a natural result of the growth of individual ones and there was neither conspiracy nor combination that restricted trades. Against this both the circuit court and Supreme Court judged that the companies concerned were in conspiracy about various unjust methods such as oppression of competitors or predatory pricing strategies and ordered dissolution. So the Standard Oil prorated the shares of 33 component companies to stockholders of the holding company. The American Tobacco was a trust formed in 1890 by five companies which were keenly competing each other on manufacture, distribution and sale of cigaretts making up 95% of national produce. This trust, intending expansion of business, began thoroughgoing price-cutting war in the field of chewing-tobacco to acquire five big producers in 1898, and later on acquired and shut down thirty rival firms at the expense of more than 50 million dollars. This was also ordered dissolution for the reason that an aim to set up monopoly and control over tobacco trade obviously existed and actions to drive out rivals were taken.[13]

These two cases, however, did not go so far as to affect much the structure and the character of competition of American industries. Rather we could say

12) Bain, *op. cit.*, Industrial Concentration, pp. 626–627; H. U. Faulkner, *op. cit.*, Japanese transl. by Ohara, *op. cit.*, vol. 2, pp. 560, 574–575.

13) E. M. Singer, *Antitrust Economics; Selected Legal Cases and Economic Models*, Prentice-Hall, Inc., 1968, Japanese transl. by H. Ueno, et al., pp. 47–48.

the courts tacitly acknowledged the changes in the capitalistic market structure and the inevitability of market behavior conforming with them. For, first, the court decisions referred only to such competition-restrictive acts among big firms as were publicly overt, and hence were biased to the formal aspect of competition, that is, the aspect which was not market control, in terms of the concept of monopoly.[14] Accordingly it was impossible to allude to such transformed competition as was characteristic to highly concentrated industries, and virtual co-operation such as the live-and-let-live policy was not taken up as the object of regulation. Secondly, an unignorable change in the interpretation of the anti-trust law was brought about by the "rule of reason" which was introduced in the Standard Oil case and then applied to the American Tobacco case. That is to say, the said per se rule of the Sherman Act, which had been observed in the Trans-Missouri Freight Association, Addyston Pipe and Steel and Northern Securities cases, was rejected. Under this per se rule, whether or not there were actual control, destructive competition, financial collapse or abuses of price cutting, any agreement to fix price, conspiracy to put an unjust change on the price structure, any arrangement about spheres of purchase and sale, or any other tacit collusion had been adjudged illegal in itself.[15]

Contrastively, by introducing the rule of reason the intent of the law was confined to be restraint of trade that "monopolize, or attempt to monopolize," and consequently it was tried to distingush good trusts from bad ones on the basis of "particular acts intended" to eliminate competitors or to constrain their competitive power.

This inclination was fundamentally followed by the decisions on the U.S. vs. United Shoe Machinery case of 1918 and the U.S. vs. U.S. Steel case of 1920. The judgement was that any combination controlling the whole or substantial part of an industry is not in violation of the Sherman Act unless it generally oppresses competitors, or forces coordination to them, or excludes them from markets. In other words, scales alone do not imply illegality, and so long as current market behavior is in good order and room of free competition is at least preserved, there shall be excuse from responsibility covering past illegal conducts.

Thus through these periods essential alteration in the interpretation of the Sherman Act was seen. Because the regulation by the Act was not directed to the phenomenon of industrial concentration or market control itself, nor to its effects on competition, concentration came to be accepted as fait accompli. Stillmore, it may be said that these decisions had an effect of instructing big firms to make deliberation so as not to come to complete monopoly, to avoid such "acts illegal in intention" as predatory tactics and to maintain competition if

14) E. S. Mason, *Economic Concentration and the Monopoly Problem*, Harvard Univ. Press, 1957, p. 342.
15) Phillips, *op. cit.*

only formally.[16]

In order to cover such defect of legal regulations, in 1914 the Clayton Act was promulgated prohibiting discriminative pricing, additional posts of directors of a company in other competing companies, transactions with binding conditions, and maneuvres through holding company. And furthermore the Federal Trade Commission Act was enacted to regulate unfair competition. However, the actual transformation of the market structure was such that did not always allow honest enforcement of the laws. Far from that, since the Webb-Pomerene Export Trade Act of 1918 warranted measures to exclude application of the Sherman and Clayton Acts,[17] merger was rather stimulated.

V. Transformation of Market Behavior——foundation of modern marketing

As has been studied in the above, the merger in America at the turn of century changed its form from pool to trust and then to holding company. The factors that supported such transformation were internally economies of scale (cost differentials) and externally the institutional elements which worked very favorably on the growth and development of big firms. Among the external factors, characteristic were industrial policies, notably the antitrust policy. Although they worked only subsidiarily on the formation of merger, their role was more active on the aspect of market behavior of such organizational forms.

Now, the wish of individual firms to pursue economies of scale (=motive to extra profit) is the base of capitalistic enterprising, which has to be realized through competition on markets. This market competition is at the same time a process of cutting off marginal firms, hence of constructing concentrative market structure. This process comprises two patterns. One is that an oligopolistic market exists since the formative stage of the industry concerned, and another is that such a market is arrived at through competition and merger starting from an early state of pure or monopolistic competition.[1] The former pattern arises where oligopolistic control of materials or technologies exists, or where huge equipment, hence capability of raising a large amount of capital, is necessary. This is also the case where no existing network of distribution is feasible due to particular conditions of selling. For example, in the above-mentioned case of necessary facilities of exposition, exhibition and service or special equipment of distribution, ability of raising a large amount of long range fixed capital is required, and as the result generally the industry takes oligopolistic structure since its beginning. When production equipment is huge the benefit of scale

16) Cf. Seagar & Gulick, *op. cit.*, especially arguments on the typical cases of merger under the Sherman Act.

17) L. T. Fournier, "The Purposes and Results of the Webb-Pomerene Law," *American Economic Review*, vol. 22, March 1932, pp. 18–33.

1) J. S. Bain, *Price Theory*, Holt, Rinehart & Winson, Inc., 1952, p. 270.

economies is large, and for the sake of profitable operation output of individual firms each must keep a large share of the total produce of the industry. Accordingly in those industries with a large minimum-optimum scale, firms capable of obtaining profit are small in numbers, and hence oligopoly is inevitable, even if relatively large demand is provided. Again where oligopoly exists on account of technological factors, any fundamental change of structure is unexpectable unless some discontinuous technical progress produces superiority in cost differentials. For even if there were marked increases in demand or new entries by gradual development of technology, the superiority of foregoing firms with established market control would not diminish. Stillmore, if efforts of product differentiation were being made by forerunners, hardship facing later-going firms would be very great.

The second pattern of oligopoly, i.e., through competition and merger, was seen in America at the formative period of marketing as extra-profit pursuing behavior on a basis of cost-differentials, as has been observed at the beginning of this section. Some comments, however, may be necessary on this point. Manufacturing firms, being freed from financial dependency on merchants by the medium of the temporary excess-demand at the time of the Civil War, were exclusively concerned with the problem of production and strived for profit by higher efficiency. The results were the birth of some big firms and the entry of petty ones from speculative motives. So long as demand was on a continuous increase, it would have taken time for the scale expansion of firms under the pursuit of efficiency to turn to the direction of intensifying competition. However, the accidentally created demand fell down sharply with the end of war. Conseqeuntly economies of scale turned to be a powerful weapon of competition. This made the very ground of the cruel tactics employed by big firms in the vigorous struggle for market control, being accelerated by the narrowed market attendant to the levelled-up organic composition of capital. Well-known examples of such tactics were the conducts of Standard Oil which intended expulsion of rivals by the secret agreements with railways and every other means and those of American Tobacco which performed predatory price cutting, imitation of brands, and coercement of boycott of rivals' products to dealers.[2] These were in themselves keen capitalistic competition, yet at the same time aimed at exclusion and suppression of competition. Thus marketing, our theme, appeared foremost as a means of excluding and suppressing competition to establish monoply. This original character of marketing may be convincible in view of the fact that the first-round merger movement was advanced even in such industries as were irrelevant to economies of scale, and that combination appeared mostly in boom times. If merger and fusion truly aimed at efficiency they should have occurred in recession times rather than in boom periods. The reality was contrary. In boom times, when demand shows active responses, smaller firms

2) Bain, "Industrial Concentration," p. 622.

were absorbed or placed under control by big ones. And the early-stage marketing acted at the gunlock therein.

By the by, when weeding-out of marginal firms takes place, the "marginal" in the industry comes to have a larger scale. This means that markets to which the marginal supply grow wider and more extensive, cost differentials become smaller, and differences of financial ability also are narrowed. Predatory competition under such a condition would need severer price cutting on extensive markets than did formerly. Nevertheless, now that marginal firms on this stage may be provided with stronger financial power, competition becomes unlikely to settle for an appreciably long time. This is especially so where product differentiation has been promoted. In other words, here to enter predatory competition will possibly drive related firms to a destructive situation, and so there will be a turn to non-price competition particular in oligopolistic markets. This is to mark a shift from simple marketing to diversified and refined one.

This refinement of marketing was assisted by the antitrust policy, as above mentioned. It was only through the Addyston Pipe and Steel and Northern Securities cases that the law began to display their effects. These two cases are noteworthy in that the adjudgment of per se illegality of monopolistic acts was drawn out. However, by this stage the first-round merger movement was already drawing to its close. Although the trust-busting movement lasted for some length later on, the introduction of the rule of reason in 1911 meant a decision that antitrust laws were to be applied only to overt predatory competition or "acts intended" to exclude and suppress competition, which resulted in a setback of this movement. This decision may be said to have instructed some certain action-guide to enterprises which were finding hardship in price competition on the narrowed cost differentials under oligopoly. The said guide was, while on one hand leaving a competitive situation through sales promotion, on another to push a live-and-let-live policy in the aspect of price by means of leadership or cooperative behavior (tacit collusion) on outputs or market territories by trade association.[3)]

Non-price competition was deployed typically by national advertising on differentiated products. Although advertising on the ground of product differentiation became the major method of competition, the purpose of the subjective body of marketing was still extra profit. In place of the former formula of weeding out marginal firms, control of their markets and realization of high price and profit,[4)] now the device was confirmation of trade-marks through national advertising and fixing of high price by it, say, "selling at the market plus" as named by Shaw.[5)] In order to attain such an aim in narrowed markets it was

3) Seager & Gulicke, *op. cit.*, p. 306.
4) F. Morishita, "Managerial Marketing no Gendaiteki Seikaku," *Keiei Kenkyū*, No. 40, pp. 6–7.
5) A. W. Shaw, *Some Problems in Market Distribution; Illustrating the Application of A Basic Philosophy of Business*, Harvard Univ. Press, 3rd ed., 1951, pp. 49–50, 57–59.

neecssary to perform "more intensive cultivation of markets"[6] and to "transfer to his differentiated product a portion of the demand that formerly found expression in the purchase of the stock commodity."[7] If the markets were, as pictured by Shaw, those that "wide extremes in purchasing power exist, [and] millions have a purchasing power scarcely sufficient to obtain for themselves the barest necessities of life,"[8] non-price competition had to become fierce struggle for market. However, this was not the whole problem. The competitive situation at the steps of distribution at that time was enough to make keen competition for profit among manufacturing firms fruitless. So efforts were made to decrease the number of successive steps of distribution by advertising products differentiated by brands directly on markets or by using their own salesmen. Here we can see the basic character of marketing, that is, elimination of middlemen. And this is nothing but the control of distribution channels backed by the interests of manufacturing firms.

6) *Ibid.*, p. 43.
7) *Ibid.*, p. 50.
8) *Ibid.*, p. 45.