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# Economic Aspiration and Method

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It would be highly appropriate on an occasion such as this to paint in bold relief some undiscovered and heretofore unarticulated broad sweep of economic change. I reluctantly discarded this topic for two compelling reasons: it was too lengthy; and my ignorance in this area turned out to be extraordinarily comprehensive. It also occurred to me that a promising topic might be developed out of where this nation seems to be going. What, for example, will be the visible coloration and composition of its economic fabric in, say, the year 2183 when Vanderbilt University celebrates its 300th anniversary? This topic seemed safe. While the speaker would not be around to receive the customary accolades for having been right, a sizeable portion of the audience would not be around to remind him of having been wrong. But then I recalled an old Danish proverb that in rough translation goes something like this: "Predictions are hazardous, especially about the future!" To hold the hazards to a minimum, I shall therefore confine myself to the past.

The topic I have chosen concerns the changing nature of organized economic enterprise, especially its social and legal environment. By organized economic enterprise I shall mean any economic entity in which decision-making is essentially composite rather than individual, of which business corporations and labor unions are the most obvious and, in terms of impact on the total economy, the most important. But by the criterion employed—decisions are essentially composite rather than individual—the average household consisting of at least one wife and husband surely falls within its ambit. Nor do I mean to imply that organized economic enterprise can be assessed without regard to the individual, *qua* individual. In truth, history seems to establish a reciprocal relationship between the two. Samuel Gompers was an individual, but it can fairly be said that from 1886 to 1924 he was also the American Federation of Labor, as was John D. Rockefeller virtually synonymous with Standard Oil. Whatever else these organizations may be in our contemporary economic society, they clearly are a great deal more than George Meany and M. J. Rathbone, their present presidents. It may not be entirely true, but it is certainly not entirely false, that where once man made the organization the organization now makes the man.

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It is not to be inferred from this that the modern American economy no longer provides rewards and incentives for individuals. On the contrary, our social institutions, including our economic institutions, both foster and preserve individual choice. But the fact is that most of what we identify as individual initiative and choice is expressed within the confines of organized business. The individual worker of an earlier era aspired to higher income through his union; the small-scale business firm seeks progress through its trade association; the individual inventor of the nineteenth century has left his garret for the corporate laboratory; even agriculture, long regarded as our last stronghold of grassroots individualism, is either organized or so regulated by government that organization is unnecessary.

I wish first, by drawing the appropriate contrasts, to show that the conduct of organized enterprise has undergone dramatic change. I have already referred to Samuel Gompers and John D. Rockefeller. While historians are not likely to view them as comrades-in-arms fighting a common cause, they sought a common economic goal for the organizations they created which could be summed up in a succinct, simple, and single word: "more." And if their tactics differed, it was only because railroad rebates furthered the ends of an oil empire, while the strike, boycott, and secession from the masses of unskilled industrial workers served those of a confederation of strong, powerful, trade unions. But both accepted the fundamentals of late nineteenth century capitalism, were keenly aware of the rewards of monopoly power, and responded instinctively to the simple and unencumbered maximizing principle on which neoclassical economics had been created.

The chronicle of the economic excesses of organized enterprise in this period, of which Standard Oil was only a part, is much too complete and too familiar to be reviewed at length here. But it is important to identify the standards by which the excesses of enterprise were measured. Classical and neoclassical economists had bequeathed to nineteenth century and early twentieth century America the simple economic doctrine of competitive *laissez-faire*. It was a doctrine of tremendous appeal for any society having historical reasons for equating political power with *arbitrary* political power. The economic doctrine of *laissez-faire* was based on the "natural" law of the market place. If left unencumbered by the political process—always capable of serious error—the natural laws of the market place rewarded each according to his economic contribution to society. "From each according to his ability, to each according to his ability" came within one word of the Marxian doctrine, but the interchange of a single word placed the two systems at opposite poles. In this context, to condemn excesses of enterprise was to condemn the system itself. The natural laws of the market place did not specify the constraints on enterprise, they simply rewarded it according to its ability to earn the maximum return. Thus, if some corporations grew in power by employing ruthless tactics against others, if the labor of women and children could be bought cheaper than that of men, if companies suppressed unions and unions suppressed companies, then that was how enterprise was expressed and how the market rewarded it. The possibility that business enterprise may govern the market instead of being governed by it occurred to some, but as late as the 1920's President Calvin Coolidge could announce as a national slogan that "The Business of America is Business," and this was usually understood to mean unrestrained business guided by market forces.

All of this has undergone dramatic change. While I do not believe that the business corporation or large labor union of the 1960's is on the brink of being confused with our eleemosynary or charitable institutions, one need not be a mid-twentieth century Solomon to distinguish either from its early twentieth century predecessor. The modern corporation customarily acknowledges in its annual report its responsibilities to the consuming public, its labor force, and its stockholders, frequently in that order. If it has one, it advertises its excellent record of research and development, labor relations, and plant safety. It becomes self-conscious over rising unemployment, and in the national interest of combating inflation it announces price increases apologetically. When the President intercedes with too much vigor, as in the case of steel last year, it even rescinds them. Corporations give millions of dollars annually to causes of higher education and various charities, and it is to be emphasized that society defines this as "corporate giving," as something not to be confused with the bequeathing of personal fortunes to colleges and universities characteristic of an earlier era.

Moreover, since the highly publicized *Smith*[1] decision was handed down by the Supreme Court of New Jersey in 1953, such corporate giving is left to the discretion of organized business management, which means that the gift need not be directly associated with any immediate and definable benefit to the corporation itself. In short, du Pont's annual appropriation for higher education no longer must contemplate "Better things for better Living through Chemistry," or the possible establishment of the University of E. I. du Pont de Nemours and Company, Inc. As one of my colleagues, John William Ward, put it in his provocative article "Private Business and Private

1. A. P. Smith Mfg. Co. v. Barlow, 13 N.J. 145, 98 A.2d 581, *appeal dismissed*, 346 U.S. 861 (1953).

Education,"[2] the *Smith* decision defined the legitimacy of corporate action so as to equate the benefit done society with the benefit done the corporation. Former Secretary of Defense Charles Wilson's famous statement, "What's good for General Motors is good for the country," was not generally greeted with enthusiastic applause, but his great error consisted of having stated the proposition in reverse order.

It would seem then that organized enterprise has become a good citizen. Corporate chicanery has given way to corporate charity, professionals have replaced privateersmen, empire has succumbed to empathy; and differences between management and labor, once fought with vicious strikes and lockouts, and settled by bloodshed and the national guard, by comparison now take on all the semblances of a spirited debate between Smith and Vassar on the explosive topic: "Resolved that a 6.5 per cent wage increase, including fringe benefits, is in the present national interest." The public has now grown accustomed to the emergence of the adversaries from the conference room locked in affectionate embrace and announcing to the world a new milestone in collective bargaining. Occasionally, of course, organized enterprise reverts to the ways of its unruly past. In the New York newspaper strike the unions displayed naked power. And the bizarre 1960 Philadelphia affair involving the electrical equipment manufacturers stands as a reminder that old fashioned conspiracy may not yet be entirely dead—a reminder, expressed in quantitative terms, that totaled about one billion dollars in fines and seven jail sentences. But significantly, Judge Ganey sternly lectured the culprits for sullying the good name of all corporate enterprise, and President Kennedy reminded the newspaper unions that their recalcitrancy showed a flagrant disregard for the public interest. These are obviously isolated exceptions to the generally practiced standard of good behavior through enlightened self-interest.

These visible changes in the conduct of organized enterprise clearly need explaining. Since a consensus prevails that the corporations and unions are still essentially economic in character and in purpose, it is appropriate to begin the search by testing the validity of some possible economic explanations, the most obvious of which lies in the classical doctrine itself. That is to say, if the earlier excesses of *laissez-faire* capitalism were attributable to the power of enterprise to govern the market, can their disappearance be attributed to strengthened market forces now capable of governing enterprise? Has the invisible hand of Adam Smith developed sufficient sinew to turn the motive of

2. Ward, *Private Business and Private Education*, 1958 Western Humanities Rev. 209, 211.

maximum private gain to public good?

If the forces of the market place have undergone any such dramatic change in the past half-century, the evidence is not to be found in the anatomy of the economy. In spite of all the frantic pronouncements that Big Business is taking over the American economy, and cries from the other side that the forces of dynamic competition are growing stronger, the striking feature of the economy is the longrun stability of its structural indexes. By far the most comprehensive study of overall concentration in the economy concludes that the relative importance of the largest 200 corporations was certainly no greater, and was probably smaller, in 1947 than in 1900. Another study shows that monopolistic industries accounted for a slightly lower proportion of total economic activity in 1947 than in 1900, but still another shows a probable slight increase in 1958 over 1947. Between 1900 and 1958 the change, if any, is insignificant. The number of business firms for every 1000 population in 1900 and today are within three-tenths of one percentage point of each other. Even the corporate revolution which Professors Berle and Means described in such awesome terms in 1932 was apparently arrested about midway in its conversion of a nation of shopkeepers into a virtual corporate society. In 1960 incorporated enterprises accounted for fifty-six per cent of the nation's output of goods and services, almost exactly the percentage they accounted for in 1929. Clearly, there is no persuasive evidence that structural change accounts for the more temperate behavior of organized enterprise. The constraining invisible hand of a competitively structured economy apparently constrains no more nor no less than it did a half-century ago.

But if the constraining forces of the market have not grown stronger, by the same line of reasoning there is no presumption that they have grown weaker, and hence other explanations for the great change in the behavior of enterprise that rest on this assumption are also of dubious validity. It is not my intention here to assess in depth the numerous and various theories of what in fact constrains modern organized enterprise. Some have long since been accorded the decent academic funeral they so richly deserved; those that survive fall far short of a consensus. I do intend to deal with one or two of the more prominent theories, chiefly because they set the stage for what I believe to be a new perspective of the issue.

Professor A. A. Berle addressed the matter in the following terms:[3] Modern corporate enterprise is at once the instrument which has rendered obsolete all economic theory and has given the United States a planned economy without government planning. The typical

3. BERLE, THE 20TH CENTURY CAPITALIST REVOLUTION (1954).

firm, argues Berle, has by virtue of its size and power been liberated from the traditional constraints that the classical theory of competitive enterprise imposes. This power is significantly understated by the conventional statistical means. The economic power of General Motors, for example, is not confined to its share of the automobile market, currently estimated at fifty-three per cent, but is greatly extended by its contractual arrangements with the multitude of small firms that supply it with everything from transmission assemblies to valve stems, and distribute its final product. These firms are merely economic appendages of the seat of corporate power. What, then, controls this power? From all visible manifestations such huge enterprises appear to be very much like the little lad who having partially mastered the technique of his bicycle, passes in review before his somewhat apprehensive parent shouting with pride, "Look, Ma, no hands." The simile is not inappropriate to Berle's thesis. While traditional market forces do not govern the corporation, it has an audience to which it must be responsive. By virtue of its size and power it resides in a veritable goldfish bowl. Any action it takes repugnant to the public interest is critically exposed in the press. Hence, it cannot exert the power it possesses to the fullest without public reprisal. Moreover, there is always the threat of government action to punish those sins press exposure may leave uncorrected. After all, in 1947 President Truman threatened to build steel plants to alleviate the "gray" market in steel, and in 1952 for a short while actually seized the industry and placed it under government management. To Berle the institutions of publicity and threat of government action now supply the controls the market once supplied, although he concedes that since none of these large enterprises are without competitors, the market still plays a modest role. But in Berle's theory the constraining forces lie outside the enterprise, and largely outside the market in which the enterprise functions.

There are also perfectly respectable theories pointing to the conclusions that the big change has come from within. Modern enterprise still confronts the traditional market constraints, but it reacts to them differently. The clearest and most rigorous of these theories has recently been set forth by Professor W. J. Baumol, who suggests that if conventional theory were to drop the assumption that the business firm attempts to maximize its profits, and substitute in its place the assumption that it attempts instead to maximize its market position, after it has once attained some minimum profit goal, accepted theory would then explain much business behavior now left unexplained. At some point firm growth becomes more important than additional immediate profits, if for no other reason than that the former assures survival with at least satisfactory profits. Firms once highly profitable have been known to die, or at least suffer serious decline. Firms that grow, by definition, avoid both.

To those of us concerned with the operative mechanics of highly industrialized societies, Baumol's theory has powerful welfare and public policy implications. As all college sophomores—and quite a few freshman—know, the historical indictment of firms with market power is that in exploiting it they also exploit the public by raising prices and restricting output. Accordingly, if firms logically and predictably substitute the goal of maximum output for that of maximum profit, the historical grounds for condemning market power disappear; the aggressiveness of enterprise operates in the public interest.

Like all thoughtful theories of responsible and thoughtful men, those of Berle and Baumol have a degree of credibility. However, I believe they both fall a good deal short of providing an explanatory hypothesis for the striking change the behavior of organized enterprise has undergone. The number of independent newspapers reached its peak around 1914. Many of them were house organs of political parties and some were in business to crusade against business. There is therefore little reason to suppose that they were less vigilant in exposing the excesses of enterprise than their 1960 counterparts. And as for growth as a goal, it would be difficult to find a period when organized enterprise put growth above all else to a greater extent than in the combination wave of 1887-1904. The reasons for the change must lie elsewhere.

The significant proximate cause, I believe, lies not in the reshuffling of the guiding incentives of enterprise or in the increased likelihood of exposure in the press, but rather in the continuous trend toward a substitution of public law for market forces. The excesses of *laissez-faire* capitalism at the turn of the century may have been many and varied, but those most frequently mentioned by the critics of that time were exploitation of unorganized labor (especially the labor of women and children), the use of questionable if not downright fraudulent means of finance, and the ruthless suppression of competing enterprises that blocked the road to unchallenged market power. In much more general terms, the decisions of organized enterprise determined the level of employment and the distribution of income. One by one all of these have been transferred from government by market forces to government by the statutory vehicles of public policy.

The specific legislative means by which many of these earlier and, in their time, legitimate excesses of a free market economy have been assigned to government by public law are reasonably familiar to all.

The Federal Reserve Act of 1913 and its amendments of the 1930's have made banking stable, above board, and honest. They have also made the interest rate, once left to the market, an instrument of national monetary policy. The Securities Exchange Act of 1934 is designed to enforce similar high standards in the corporate securities market. Comprehensive labor laws establish rigorous standards of employment, including the minimum wage. And the corporate income tax requires that at least half the profits corporations earn be turned over to the goverument for public purposes, a factor that surely is not completely divorced from recent increases in corporate giving in support of higher education.

While all of these developments have altered the behavior of organized enterprise in significant ways, I believe that the most important factor has been the spectacular alteration in the Magna Carta of the free enterprise system itself—the federal antitrust laws. The excesses of organized enterprise in fact and in theory are generally attributed to the high order of market power enterprise possesses. The simple objective of antitrust policy is to prevent the attainment of such power, and hence assure to society the benefits of a smoothly functioning, productive, and competitive economy unencumbered by the rigid regulations of the state. While opinions among the specialists varied, most agreed that up to 1950 antitrust policy had not fulfilled its appointed task with distinction.

Recent administrations may not have successfully eliminated those seats of market power inherited from a previous era, but they have clearly revitalized antitrust policy so as to prevent the enhancement of such power in the future. Since 1950 more cases have been initiated against business firms than in all the previous history of antitrust. Price discrimination, once rampant, has been attacked on all sides. Business mergers, the means by which economic empires were once created, have now become a hazardous road to growth. In 1920 a succession of mergers that brought together sixty-five per cent of the nation's steel capacity passed muster under the then prevailing standards of antitrust policy. In 1960 the merger of a shoe manufacturer and a shoe retailer accounting for a bare three and six-tenths per cent of the nation's output of shoes was declared illegal. In fact, thoughtful students of antitrust policy long sympathetic to its purposes have recently become concerned over the new and invigorated antitrust laws. They have not only demonstrated an unprecedented capacity to arrest tendencies toward monopoly, but they have also been bent to serve the ends of small business legislation. In the drive to halt activities by one firm that work to the disadvantage of others, especially if the others are smaller, they seem also to be arresting tendencies toward competition. When organized enterprise can neither monopolize nor compete, it obviously operates under a severe constraint.

It was once contended that the ghost of Senator Sherman, whose name our parent antitrust statute bears, was an invisible member of the Board of Directors of every large corporation in the United States. He has now been joined by the late Senator Kefauver, Congressman Celler, and Attorney General Robert Kennedy, and the four of them can often muster a majority vote.

Nor are the legal constraints limited to the enacted statutes. There are also the constraints imposed by the lawmakers—Congress and the President—especially that recently developed instrument of control, the congressional investigating committee. Judged from its postwar schedule, the Senate Committee on the Judiciary can scarcely claim to have had a really successful year without investigating the steel industry, unless of course it has meanwhile been much too occupied investigating automobiles, drugs, insurance, daily newspapers, television rating systems, and newsprint. These inquiries serve purposes far beyond that of enhancing the wisdom of Congress—ostensibly their original purpose. They also have the force of law without the limits codification and judicial review impose. For example, there is no law stating that the price of steel cannot be increased, and if enacted its constitutionality would no doubt be hotly contested. But at least two congressional inquiries into why steel prices *should* not rise have been sufficient to assure that steel prices *did* not rise; and on one highly publicized occasion when a steel price increase caught the responsible committee too deeply involved with the drug industry to notice, the President proved himself to be a highly effective substitute.

It is often said, frequently on the editorial page of newspapers, that Congress cannot repeal the universal laws of supply and demand. My central thesis is that while it may not have repealed them, it has imposed significant legal constraints on their operation. Much economic activity these economic laws once governed is now governed by the laws of Congress. The dramatic changes in the behavior of organized enterprise are therefore not so much attributable to any perceptible alteration in their basic economic incentives, but rather to the mounting institutional constraints on how those incentives may be exercised. Actions of business enterprise, once simply a normal and spontaneous reaction to market forces, must now be carefully checked with corporate counsel. Where once the market dictated, the law now prescribes. We now have, or are rapidly approaching, a legalistic economy.

Since the performances of a market economy have historically been so inextricably entwined with welfare economics, it would be appropriate to conclude with a few observations on whether the new legalistic economy serves the public weal better or worse than its earlier unfettered market counterpart. I expect that most would applaud the change; and unless the democratic process has itself been defective, the new economic order is by definition more consistent with the public's economic and political preferences.

But this provides no reason for complacency that all is well in Eden. I do not know when man first rose up on his hind legs and moved forward in pursuit of his economic self-interest. But the fact that he did provided society with a logical set of analytical economic tools capable of predicting certain economic results if certain assumed conditions were fulfilled. These formal analytical tools made economics the queen of the social sciences. They made it possible to apply the principles of scientific method to a vital aspect of human endeavor. Much more importantly, they provided nations—and especially this nation—with a simple system of political and economic order that endured well into the twentieth century. It was simple because it avoided most of the encumbrances of enacted law; it was orderly because it related man to his economic environment in a predictable fashion.

The legalistic economy that has been substituted in its place is neither simple nor, do I believe, orderly. It has developed not as system but as a disjointed set of piecemeal correctives. In consequence, while having gradually ameliorated the excesses of a definable economic system, it has unsystematically given rise to the equally large problems born of incoherence and inconsistency. Under the legalistic economy we have become the first acknowledged affluent society deeply concerned with its rate of economic growth. We contradictorily by law raise the prices of goods in abundance but depress the prices of goods in relatively short supply. Legal institutions have recently prohibited a single vendor of potato chips from charging slightly different prices to different customers in Cleveland, but they enable a single union official to close down all the oceanic shipping on the Atlantic seaboard. By one set of laws we permit domestic oil producers to restrict their output and artificially to raise their prices to conserve domestic oil reserves, but we at the same time restrict by law the importation of oil from abroad. We are baffled by and unable to explain the "new inflation" because the important variables of the economy have lost the systematic relationship they once bore each other. The list of inconsistencies could be greatly extended.

All this, I hope, will not be misinterpreted as advocacy for a return to the nineteenth century, or even for the primacy of economic models over the rules of law. But the legalistic economy, as was true of the market economy it replaced, has its excesses. There is, however, a distinct difference between the two. The simple market system we have laid aside not only explained but justified. The legalistic economy does neither. It defies clear articulation and is imprecisely described as a "mixed" economy.

This affords me the one occasion in this essay to say something directly associated with its title. I refer to methodology. Economics, even analytical economics, had its own day of incoherence and inconsistency. These deficiencies were exposed and corrected with the development of the concept of general equilibrium, a formal system of economic logic that owes much to the nineteenth century French economist Leon Walras. In lay terms it simply proved that we could not reason from the particular to the general without grievous error. That is, a law that apparently benefits some farmers may not only work to the net disadvantage of the entire economic community, it may even work to the disadvantage of all farmers. I know far too little about the law to urge that law schools seriously ponder this page from the history of economic method, but it is at least a fitting occasion to call it to their attention.