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Preface

This twelfth edition continues a long effort to tell the story of how forces in business, government, and society shape our world. As always, since the last edition, a stream of events has dictated the need for wide, and sometimes deep, revision. Accordingly, we have updated every chapter to include new ideas, laws, personalities, and publications.

While current events move rapidly over the surface of our subject matter, the underlying principles and relationships at its core lie undisturbed. As in every edition, we adapt to the flow of ephemera, but we also continue the work of building insight into the basic nature of the discipline. So, while current events will play havoc with the look of this edition, we believe that discussions about the plain nature of business, government, and society interrelationships are stronger and will endure longer than in our previous volumes.

We carry on our effort to give more prominence to global and comparative aspects of the subject matter. More than in previous editions we focus on business activities, ideas, and civil society networks that span borders. Although we emphasize current events, we continue to provide historical background. Often, what is fresh in our memory is but the periodic display of an enduring phenomenon. We explain the ancient origins of the tension between wealth and virtue, discuss how great industries shaped nations, and study personalities from the past who have left a lasting imprint.

With this edition we also continue a strong and spirited collaboration between father and son extending now over 30 years.

THE CHAPTERS

The new edition brings many changes. Key updates and additions in the chapters include these.

- Chapter 4, "Critics of Business," contains a new section on the globalization of critics, which discusses progressive civil society, neoliberalism, and the global justice movement.
- Chapter 5, "Corporate Social Responsibility," is revised extensively to incorporate international developments, specifically, the rise of new global norms, civil regulation, soft law, and multistakeholder initiatives. This reflects rapid evolution in the practice of corporate social responsibility.
- Chapter 6, "Implementing Corporate Social Responsibility," now focuses more on management processes for carrying out responsibility strategies. It introduces a new model of implementation. It also discusses new market-driven styles of philanthropy.
- Chapter 7, "Business Ethics," updates students on the executive fraud prosecutions from turn-of-the-century scandals. It includes a new, extended discussion about the ethical dimensions of corporate culture.

- Chapter 9, "Business in Politics," now explains how business continues to dominate the political arena following the Abramoff scandals and recent reforms designed to limit both corporate lobbyists and corporate political donations.
- Chapter 10, "Regulating Business," is a new chapter that replaces two chapters in previous editions. It covers how regulation works, how it affects corporations, its costs and benefits, and its use in other nations.
- Chapter 11, "Multinational Corporations," is a fundamentally new chapter about the impact of MNCs in global markets, particularly in emerging economies, and the international codes intended to regulate their activities. It contains short case stories about Weatherford International, Drummond Company, and Wal-Mart and Mattel.
- Chapters 13 and 14, the two chapters on business and the environment, are revised to report advances in scientific understanding. There are new discussions of ecosystems and carbon markets.
- Chapter 18, "Corporate Governance," is rewritten to better explain evolving relationships of share owners, boards of directors, and management. It contains a new discussion of backdating and a more detailed analysis of executive compensation practices.

THE CASE STUDIES

Every chapter, except Chapter 1, concludes with a case study. The cases illustrate one or more central themes in the chapter. Three new cases are added to this twelfth edition.

- "David and Goliath at the WTO" tells how the tiny island nation of Antigua and Barbuda challenged the United States in the World Trade Organization. It hosts offshore Internet gambling businesses and argued that U.S. laws prohibiting most Internet gambling were an unfair trade barrier.
- "Harvesting Risk" is the story of a pesticide manufacturer in Los Angeles with a distinctive strategy. It buys the rights to older and more dangerous pesticides from big agrichemical companies that have moved on to more advanced, safer products. Then it makes big profits selling them in niche markets where they are still legal.
- "High Noon at Hewlett-Packard" takes readers into a boardroom power struggle over the proper role of directors. It invites discussion of the pretexting scandal and the downfalls of CEO Carly Fiorina and Chairman Patricia Dunn.

CHAPTER-OPENING STORIES

As in past editions, we begin each chapter with a true story about a company, a biographical figure, or a government action. Seven new stories appear in this edition.

- "The Bill & Melinda Gates Foundation." The Gates Foundation endowment is larger than the GDPs of 112 countries, but the problems it confronts are large too. Can the genius behind Microsoft make a dent in them?

- "'Today's verdict is a triumph of our legal system . . .'' Of all the executives put on trial in the corporate fraud scandals, Bernard Ebbers at WorldCom got the longest sentence—25 years—a retribution exceeding that given to mafia hit men and ordinary murders. Were his crimes that bad?
- "The Abramoff Scandals." This story unfolds the scandal in the stories of four men it consumed—Jack Abramoff and Representatives Tom DeLay (R-Tex.), Bob Ney (R-Ohio), and Randy "Duke" Cunningham (R-Calif.).
- "Annals of Regulation: The FCC and CBS." After exposure of Janet Jackson's breast in Super Bowl XXXVIII, the Federal Communications Commission gave CBS the maximum fine permitted by law for broadcast indecency. The story describes how the agency acted and raises the question of the fine's fairness.
- "The Commerce Railyards." Diesel exhaust from a complex of four railyards raises cancer risks for the population of Los Angeles. The story explains those risks and illustrates the small, unseen dangers of industrial pollution.
- "The Employment Non-Discrimination Act of 2007." For the first time, the House of Representatives passed a bill to give gays, lesbians, and bisexuals the same employment rights that other Americans were given in the Civil Rights Act of 1964. The bill has not yet become law. Should it?
- "Backdating with Dr. McGuire." Remarkably, Dr. William McGuire, the CEO of UnitedHealth Group, always seemed to receive option grants on days when his company's stock price hit quarterly and yearly lows. When a study published in *The Wall Street Journal* put the odds against picking these dates by chance at one in 200 million, forces were set in motion that ended Dr. McGuire's career.

SUPPORT MATERIALS FOR INSTRUCTORS

The *Online Learning Center*, at www.mhhe.com/steiner12e, includes sample course outlines, chapter objectives, case study teaching notes with answers to the case questions, term paper topics for each text chapter, and a test bank covering chapters and case studies, including multiple-choice, true/false, fill-in, and essay questions.

A set of *PowerPoint®slides* highlighting chapter topics is available for use in classroom lectures.

A *Computerized Test Bank* contains all the questions in the print test bank. It is a powerful system that allows tests to be prepared quickly and easily. Instructors can view questions as they are selected for a test; scramble questions and answers; add, delete, and edit questions; create multiple test versions; and view and save tests.

An *Online Learning Center* also features resources for both instructors and students. The site offers downloadable supplements for instructors, and interactive exercises and self-quizzes designed to enhance student understanding of text material. Go to www.mhhe.com/steiner12e.

Chapter One

The Study of Business, Government, and Society

Exxon Mobil Corporation

ExxonMobil is the largest publicly traded international oil company. Although it is headquartered in Irving, Texas, and most people regard it as an American company, 69 percent of its sales, which were $366 billion in 2006, are in more than 200 other countries.[1] Its main business is discovering, producing, and selling oil and natural gas, and it has a long record of profiting more at this business than its rivals.

ExxonMobil cannot be well understood apart from its history. It descends from the Standard Oil Trust, incorporated in 1882 by John D. Rockefeller as Standard Oil of New Jersey. Rockefeller was a brilliant strategist and organizer who crushed competitors. He believed that the end of imposing order on a youthful, rowdy oil industry justified the use of ruthless means. As Standard Oil grew, Rockefeller's values defined the company's culture; that is, the shared assumptions, both spoken and unspoken, that animate its employees. If the values of a founder such as Rockefeller are effective, they become embedded over time in the organization. Once widely shared, they tend to be exceptionally long-lived and stable.[2] Rockefeller emphasized cost control, efficiency, centralized organization, and suppression of competitors. And no set of principles was ever more triumphant. Standard Oil once had more than 90 percent of the American oil market.

Standard Oil's power so offended public values that in 1890 Congress passed the Sherman Antitrust Act to outlaw its monopoly. In 1911, after years of legal battles, the trust was finally broken into 39 separate companies. After the breakup, Standard Oil of New Jersey continued to exist. Although it had shed 57 percent of its assets to create the new firms, it was still the world's largest oil company. Some companies formed in the

[1] Figures in this paragraph are from Exxon Mobil Corporation, Form 10-K 2006, filed with the Securities and Exchange Commission, February 28, 2007.

[2] See, for example, Edgar H. Schein, *The Corporate Culture Survival Guide* (San Francisco: Jossey-Bass, 1999), part one.

breakup were Standard Oil of Indiana (which was later renamed Amoco), Atlantic Refining (ARCO), Standard Oil of California (Chevron), Continental Oil (Conoco), Standard Oil of Ohio (Sohio), Chesebrough-Ponds (a company that made petroleum jelly), and Standard Oil of New York (Mobil). In 1972 Standard Oil of New Jersey changed its name to Exxon, and in 1999 it merged with Mobil, to form ExxonMobil.

Rockefeller's influence is buried in the passage of time, but ExxonMobil's actions remain consistent with his nature. It has a centralized and authoritarian culture. Cost control, capital productivity, and strict financial controls are emphasized in operations. Profit is an overriding goal, and projects must meet strict criteria for return on investment. Unlike Southwest Airlines or Google, where having fun is part of the job, performance pressure at ExxonMobil is so intense that it "is not a fun place to work."[3] Over many years it has consistently bettered industry rivals in its favorite measure, return on average capital employed, just like the old Standard Oil Trust. And competitors still find it a ferocious adversary. The company says simply that it "employs all methods of competition which are lawful and appropriate."[4]

ExxonMobil is a massive organizational force, shaping international markets, pushing against competitors, and influencing governments. However, today it exists in a more difficult environment than did Rockefeller's dominating trust. As in the old days, its power is contested and limited by the interplay of economic, political, and social forces. Only now those forces are more leveling.

Markets are more contested. ExxonMobil pumps only 8 percent of the world's daily output of oil and controls less than 1 percent of petroleum reserves. These figures are far lower than in the 1950s when Exxon was the largest of the Seven Sisters, a group of Western oil firms that dominated worldwide production and reserves, including the huge Middle East oil fields.[5] Now its largest competitors are seven state-owned oil companies, often called the "new Seven Sisters," whose output dwarfs that of yesteryear's titans.[6] The biggest, Saudi Aramco, is 3.5 times the size of ExxonMobil in daily output and has 32 percent of world reserves.[7]

The rise of these state-owned oil companies reflects a new resource nationalism in developing nations that want to recapture oil profits from foreign firms. Climbing crude oil prices since the late 1990s have made oil reserves more valuable, leading many countries to take over oil fields. This happened to ExxonMobil in Venezuela. It lost 2 percent of daily production in 2007 when the government seized projects valued at $4.5 billion.[8]

ExxonMobil is on a treadmill, constantly searching for new oil and natural gas supplies to compensate for declining production in existing fields. Output from a mature

[3] Fadel Gheit, a former employee and leading oil industry analyst, quoted in Geoff Colvin, "The Defiant One," *Fortune*, April 30, 2007, p. 88.

[4] See, for example, Exxon Mobil Corporation, Form 10-K 2006, p. 2.

[5] The Seven Sisters were Exxon, Mobil, Shell, British Petroleum, Gulf, Texaco, and Chevron.

[6] These new "seven sisters" are Saudi Aramco (Saudi Arabia), Gazprom (Russia), China National Petroleum Company (China), National Iranian Oil Company (Iran), Petróleos de Venezuela S.A. (Venezuela), Petrobras (Brazil), and Petronas (Malaysia).

[7] Government Accountability Office, *Crude Oil*, GAO-07-283, February 2007, fig. 9.

[8] Chris Kraul, "Exxon, Conoco Drop Venezuela Oil Projects," *Los Angeles Times*, June 27, 2007, p. C3.

field drops 5 to 8 percent a year. To maintain profitability the company pursues new reserves wherever they are located, taking political risks and abiding unrest and corruption. In Iran and Venezuela ExxonMobil's assets were appropriated. In Chad, Angola, Nigeria, and Equatorial Guinea, it paid dictators for access to oil. Indonesian troops guard its facilities against attacks by rebel forces.[9]

Governments are more powerful and relations with them more complex than in the past. ExxonMobil's operations are restricted by the laws and regulations of each country in which it does business. In the United States alone approximately 200 federal agencies and bureaus impose rules and standards on the company. Only a handful of these existed in Rockefeller's day. In foreign countries ExxonMobil faces import and export restrictions, production taxes, price controls, and regulations to protect nature. In 2006 it supported governments by paying $101 billion in taxes worldwide, a sum exceeding the combined revenues of Dell and Microsoft.

ExxonMobil also faces a demanding social environment. As a leader in the world's largest industry, it is closely watched by environmental, civil rights, labor, and consumer groups—some of which are actively hostile. For years the company has agitated environmentalists by rejecting the scientific case for global warming. Alone among major oil companies, it refuses to make significant investments in renewable energy sources such as ethanol, solar, wind, or tidal. A former CEO called such investments "a complete waste of money."[10] Energy from renewables is more expensive to produce than energy from oil, gas, and coal, which will be the dominant sources of energy far into the future. Therefore, ExxonMobil shuns renewables, which lack promise of satisfying its lofty return on capital standards.

ExxonMobil got a good public caning because for years it funded the research of groups that denied global warming. In 2006 Britain's scientific academy, the Royal Society, took the unprecedented step of writing to the company's management, asking that it stop "misinforming the public."[11] Then two senators, Olympia Snowe (R-ME) and John Rockefeller IV (D-WV), the great grandson of the company's founder, sent a letter to the CEO and members of its board of directors. They asked that ExxonMobil end its "climate change denial strategy" because it was adversely affecting the credibility of the United States in the international community."[12]

Such pressure led CEO Rex Tillerson to grant publicly that the world is warming. But he did not make any notable strategic changes.[13] His reversal of belief failed to satisfy critics, especially ExxposeExxon, a coalition of environmental groups that opposes the company's policies. The coalition includes Defenders of Wildlife,

[9] The company faces murder charges brought by villagers who claim it was complicit when government troops attacked area natives sympathetic to the rebels. See *Doe v. Exxon Mobil Corp.*, 473 F.3d 345 (2007).

[10] Lee Raymond, quoted in "The Unrepentant Oilman," *The Economist*, March 15, 2003, p. 64.

[11] David Adam, "Scientists Attack Climate Change Denial," *The Guardian Weekly*, September 29, 2006, p. 14.

[12] Quoted in Steven Mufson, "At Exxon Meeting, a Storm Outside but Calm Within," *Washington Post*, May 31, 2007, p. D2.

[13] Jeffrey Ball, "Exxon Softens Climate-Change Stance," *The Wall Street Journal*, January 11, 2007, p. A2.

Greenpeace, the Natural Resources Defense Council, the Sierra Club, and the Union of Concerned Scientists. This league of greens continues to hound the oil giant. Its banner outside the firm's 2007 shareholder's meeting read "No Planet, No Dividends."

As a corporate citizen ExxonMobil funds worldwide programs to benefit education, communities, health, nature, and the arts. Its largest contributions, about 25 percent of the total, go to higher education. Other projects range from a $13 million campaign to save the world's tigers from extinction, an appropriate project since the tiger is the company's brand symbol, to sponsorship of free poetry readings in Singapore, where the company owns a chemical plant. In 2006 ExxonMobil gave $139 million to such efforts. This is a large sum from the perspective of an individual. However, for ExxonMobil it was one-twenty-sixth of 1 percent of its $366 billion revenues, the equivalent of a person making $1,000,000 a year giving $385 to charity. Does this giving live up to the elegant example of founder John D. Rockefeller, the great philanthropist of his era?

The story of ExxonMobil raises central questions about the role of business in society. When is a corporation socially responsible? How can managers know their responsibilities? What actions are ethical or unethical? How responsive must a corporation be to its critics? This book is a journey into the criteria for answering such questions. As a beginning for this first chapter, however, the story illustrates a range of interactions between one large corporation and many nations and social forces. Such business–government–society interactions are innumerable and complicated. In the chapter that follows we try to order the universe of these interactions by introducing four basic models of the business–government–society relationship. In addition, we define basic terms and explain our approach to the subject matter.

WHAT IS THE BUSINESS–GOVERNMENT–SOCIETY FIELD?

In the universe of human endeavor, we can distinguish subdivisions of economic, political, and social activity—that is, business, government, and society—in every civilization throughout time. Interplay among these activities creates an environment in which businesses operate. The business–government–society (BGS) field is the study of this environment and its importance for managers.

To begin, we define the basic terms.

business
Profit-making activity that provides products and services to satisfy human needs.

Business is a broad term encompassing a range of actions and institutions. It covers management, manufacturing, finance, trade, service, investment, and other activities. Entities as different as a hamburger stand and a giant corporation are businesses. The fundamental purpose of every business is to make a profit by providing products and services that satisfy human needs.

government
Structures and processes in society that authoritatively make and apply policies and rules.

Government refers to structures and processes in society that authoritatively make and apply policies and rules. Like business, it encompasses a wide range of activities and institutions at many levels, from international to local. The focus of this book is on the economic and regulatory powers of government as they affect business.

society
A network of human relations composed of ideas, institutions, and material things.

idea
An intangible object of thought.

value
An enduring belief about which fundamental life choices are correct.

ideology
A bundle of values that creates a particular view of the world.

institution
A formal pattern of relations that links people together to accomplish a goal.

A *society* is a network of human relations that includes three interacting elements: (1) ideas, (2) institutions, and (3) material things.

Ideas, or intangible objects of thought, include values and ideologies. *Values* are enduring beliefs about which fundamental choices in personal and social life are correct. Cultural habits and norms are based on values. *Ideologies*—for example democracy and capitalism—are bundles of values that create a certain world view. They establish the broad goals of life by defining what is considered good, true, right, beautiful, and acceptable. Ideas shape every institution in a society.

Institutions are formal patterns of relations that link people together to accomplish a goal. They are essential to coordinate the work of individuals who have no personal relationship with each other.[14] In modern societies, economic, political, cultural, legal, religious, military, educational, media, and familial institutions are salient. There are multiple economic institutions including financial institutions, the corporate form, and markets. Collectively, we call these business.

Figure 1.1 shows how a range of institutions supports markets. Capitalism as an economic system shows wide variation in the nations where it exists because supporting institutions grow from unique historical and cultural roots. In developed nations these institutions are highly evolved and mutually supportive. Where they are weak, markets work in dysfunctional ways. An example is Russia, which introduced a market economy after the fall of communism.

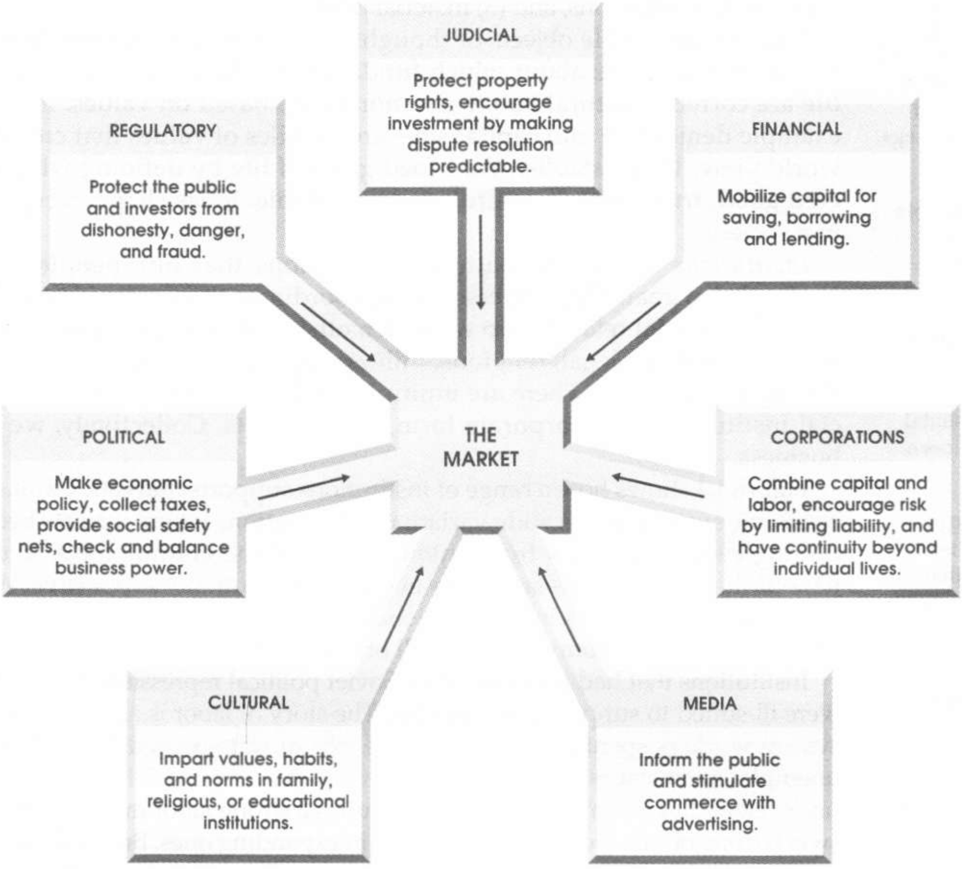
Institutions that had evolved under Soviet political repression and state planning were ill-suited to support a free market. The story of labor is an example. In the old system workers spent lifetimes in secure jobs at state-owned firms. There was no unemployment insurance and, since few workers ever moved, housing markets were undeveloped. A free market economy requires a strong labor market, so workers can switch from jobs in declining firms to jobs in expanding ones. But in Russia the development of a labor market was arrested. The government did not yet provide unemployment benefits to idled workers, so there was no safety net. And housing markets were anemic. Company managers, out of basic humanity, were unwilling to lay off workers who got no benefits and who would find it difficult to move elsewhere.[15] As a result, restructuring in the new Russian economy was torpid. The lesson is that institutions are vital to markets.

Each institution has a specific purpose in society. The function of business is to make a profit by producing goods and services at prices attractive to consumers. A business uses the resources of society to create new wealth. This justifies its existence and is its priority task. All other social tasks—raising an army, advancing knowledge, healing the sick, or raising children—depend on it. Businesses must, therefore, be managed to make a profit. A categorical statement of this point comes from Peter Drucker: "Business management must always, in every decision and

[14] Arnold J. Toynbee, *A Study of History,* vol. XII, *Reconsiderations* (London: Oxford University Press, 1961), p. 270.

[15] Joseph E. Stiglitz, *Globalization and Its Discontents* (New York: W. W. Norton, 2002), p. 140.

FIGURE 1.1 How Institutions Support Markets



action, put economic performance first."[16] Without profit, business fails in its duty to society and lacks legitimacy.

material things Tangible artifacts of a society that shape and are shaped by ideas and institutions.

The third element in society is *material things*, including land, natural resources, infrastructure, and manufactured goods. These shape and, in the case of fabricated objects, are partly products of ideas and institutions. Economic institutions, together with the extent of resources, largely determine the type and quantity of society's material goods.

The BGS field is the study of interactions among the three broad areas defined above. The primary focus is on the interaction of business with the other two elements. The basic subject matter, therefore, is how business shapes and changes government and society, and how it, in turn, is molded by political and social pressures. Of special interest is how forces in the BGS nexus affect the manager's task.

[16] *Management: Tasks–Responsibilities–Practices* (New York: Harper & Row, 1973), p. 40.

WHY IS THE BGS FIELD IMPORTANT TO MANAGERS?

To succeed in meeting its objectives a business must be responsive to both its economic and its noneconomic environment.[17] ExxonMobil, for example, must efficiently discover, refine, transport, and market energy. Yet swift response to market forces is not always enough. There are powerful nonmarket forces to which many businesses, especially large ones, are exposed. Their importance is clear in the two dramatic episodes that punctuate ExxonMobil's history—the 1911 court-ordered breakup and the 1989 *Exxon Valdez* oil spill.

In 1911 the Supreme Court, in a decision that reflected public opinion as well as interpretation of the law, forced Standard Oil to conform with social values favoring open, competitive markets. With unparalleled managerial genius, courage, and perspicacity, John D. Rockefeller and his lieutenants had built a wonder of efficiency that spread fuel and light throughout America at lower cost than otherwise would have prevailed. They never understood why this remarkable commercial performance was not the full measure of Standard Oil. But beyond efficiency, the public demanded fair play. Thus, the great company was dismembered.

In Alaska a sudden crisis changed ExxonMobil's political and social environments, leading to billions of dollars of sanctions. Today ExxonMobil operates its tanker fleet with extreme care. It has new environmental safeguards and randomly tests crew members for drugs and alcohol. Remarkably, it is now so disciplined that it measures oil spills from its fleet of tankers in teaspoons per million gallons shipped. In 2003 it reported losing less than one teaspoon per million gallons.[18]

Recognizing that a company operates not only within markets but within a society is critical. If the society, or one or more powerful interests within it, does not accept a company's actions, that firm will be punished and constrained. A basic agreement or *social contract* exists between the business institution and society. This contract defines the broad duties that business must perform to retain society's support. It is partly expressed in law, but it also resides in social values.

social contract
An underlying agreement between business and society on basic duties and responsibilities business must carry out to retain public support. It may be reflected in laws and regulations.

Unfortunately for managers, the social contract is not as clear-cut as are the economic forces a business faces, as complex and ambiguous as the latter often are. For example, the public believes that business has social responsibilities beyond making profits and obeying regulations. If business does not meet them, it may suffer. But precisely what are they? How is corporate performance measured? To what extent must a business comply with ethical values not written into law? When meeting social expectations conflicts with maximizing profits, what is the priority? Despite these questions, the social contract contains the expectations of society, and managers who ignore or violate it are courting disaster.

[17] For discussion of this distinction see Jean J. Boddewyn, "Understanding and Advancing the Concept of 'Nonmarket,'" *Business & Society,* September 2003.

[18] Exxon Mobil Corporation, "All Ahead Safe," *National Journal,* March 20, 2004, p. 888 (advertisement).

FOUR MODELS OF THE BGS RELATIONSHIP

Interactions among business, government, and society are infinite and their meaning is open to interpretation. Faced with this complexity, many people use simple mental models to impose order and meaning on what they observe. These models are like prisms, each having a different refractive quality, each giving the holder a different view of the world. Depending on the model (or prism) used, a person will think differently about the scope of business power in society, criteria for managerial decisions, the extent of corporate responsibility, the ethical duties of managers, and the need for regulation.

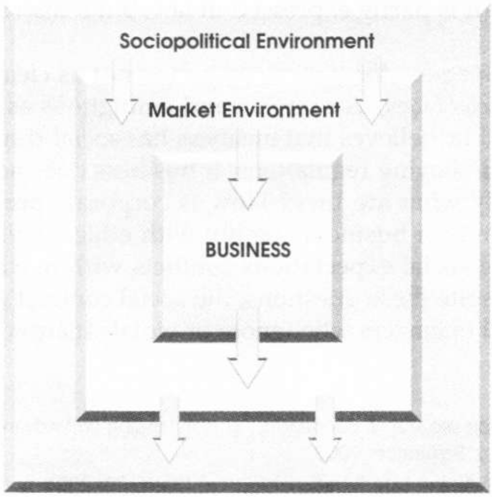
The following four models are basic alternatives for seeing the BGS relationship. As abstractions they oversimplify reality and magnify central issues. Each model can be both descriptive and prescriptive; that is, it can be both an explanation of how the BGS relationship does work and, in addition, an ideal about how it should work.

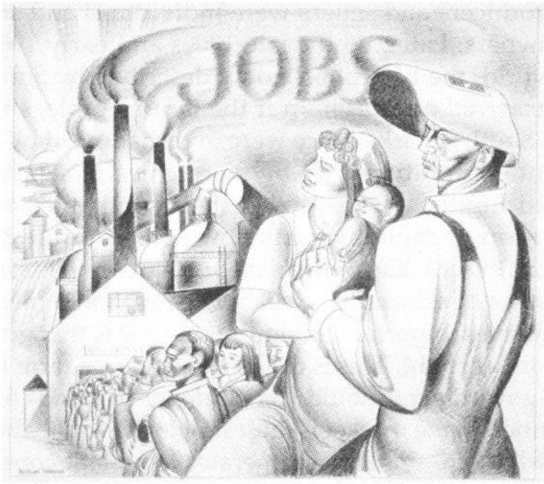
The Market Capitalism Model

The market capitalism model, shown in Figure 1.2, depicts business as operating within a market environment, responding primarily to powerful economic forces. There, it is substantially sheltered from direct impact by social and political forces. The market acts as a buffer between business and nonmarket forces. To appreciate this model, it is important to understand the history and nature of markets and the classic explanation of how they work.

Markets are as old as humanity, but for most of recorded history they were a minor institution. People produced mainly for subsistence, not to trade. Then, in the 1700s, some economies began to expand and industrialize, division of labor developed within them, and people started to produce more for trade. As trade grew, the market, through its price signals, took on a more central role in directing

FIGURE 1.2 **The Market Capitalism Model**





***Full Production and Full Employment under Our Democratic System of Private Enterprise*, ca. 1944, a crayon and ink drawing by Michael Lenson, an artist working for the Works Progress Administration Federal Art Project. Lenson focuses on the virtues of market capitalism.** Source: The Library of Congress, Prints & Photographs Division, LC-USZC4-6568.

market economy The economy that emerges when people move beyond subsistence production to production for trade, and markets take on a more central role.

capitalism An economy in which private individuals and corporations own the means of production and, motivated by the desire for profit, compete in free markets under conditions of limited restraint by government.

the creation and distribution of goods. The advent of this kind of *market economy*, or an economy in which markets play a major role, reshaped human life.

The classic explanation of how a market economy works comes from the Scottish professor of moral philosophy Adam Smith (1723–1790). In his extraordinary treatise, *The Wealth of Nations*, Smith wrote about what he called "commercial society" or what today we call *capitalism*. He never used that word. It was adopted later by the socialist philosopher Karl Marx (1818–1883), who contrived it as a term of pointed insult. But it caught on and soon lost its negative connotation.[19] Smith said that the desire to trade for mutual advantage lay deep in human instinct. He noted that the growing division of labor in society led more people to try to satisfy their self-interests by specializing their work, then exchanging goods with each other. As they did so, the market's pricing mechanism reconciled supply and demand, and its ceaseless tendency was to make commodities cheaper, better, and more available.

The beauty of this process, according to Smith, was that it coordinated the activities of strangers who, to pursue their selfish advantage, were forced to fulfill the needs of others. In Smith's words, each trader was "led by an invisible hand to promote an end which was no part of his intention," the collective good of society.[20] Through markets that harnessed the constant energy of greed for the public welfare, Smith believed that nations would achieve "universal opulence." His genius was to demystify the way markets work, to frame market capitalism in moral terms, to extol its virtues, and to give it lasting justification as a source of human progress. The greater good for society came when businesses competed freely.

[19] Jerry Z. Muller, *The Mind and the Market: Capitalism in Modern European Thought* (New York: Knopf, 2002), p. xvi.

[20] Adam Smith, *The Wealth of Nations*, ed. E. Cannan (New York: Modern Library, 1937), Book IV, chap. II, p. 423. First published in 1776.

In Smith's day producers and sellers were individuals and small businesses managed by their owners. Later, by the late 1800s and early 1900s, throughout the industrialized world, the type of economy described by Smith had evolved into a system of *managerial capitalism.* In it the innumerable, small, owner-run firms that animated Smith's marketplace were overshadowed by a much smaller number of dominant corporations run by hierarchies of salaried managers.[21] These managers had limited ownership in their companies and worked for shareholders. This form of capitalism has now spread throughout the world. Nowhere does it work exactly like Smith's theory. Nevertheless, the market capitalism model continues to exist as an ideal against which to measure practice.

managerial capitalism
A market economy in which the dominant businesses are large firms run by salaried managers, not smaller firms run by owner-entrepreneurs.

laissez-faire
An economic philosophy that rejects government intervention in markets.

The model incorporates important assumptions. One is that government interference in economic life is slight. This is called *laissez-faire,* a term first used by the French to mean that government should "let us alone." It stands for the belief that government intervention in the market is undesirable. It is costly because it lessens the efficiency with which free enterprise operates to benefit consumers. It is unnecessary because market forces are benevolent and, if liberated, will channel economic resources to meet society's needs. It is for governments, not businesses, to correct social problems. Therefore, managers should define company interests narrowly, as profitability and efficiency.

Another assumption is that individuals can own private property and freely risk investments. Under these circumstances, business owners are powerfully motivated to make a profit. If free competition exists, the market will hold profits to a minimum and the quality of products and services will rise as firms try to attract more buyers. If one enterprise tries to increase profits by charging higher prices, consumers will go to a competitor. If one producer makes higher-quality products, others must follow. In this way, markets convert selfish competition into broad social benefits.

Other assumptions include these: Consumers are informed about products and prices and make rational decisions. Moral restraint accompanies the self-interested behavior of business. Basic institutions such as banking and laws exist to ease commerce. There are many producers and consumers in competitive markets.

The perspective of the market capitalism model leads to these conclusions about the BGS relationship: (1) government regulation should be limited, (2) markets discipline private economic activity to promote social welfare, (3) the proper measure of corporate performance is profit, and (4) the ethical duty of management is to promote the interests of shareholders. These tenets of market capitalism have shaped economic values in the industrialized West and, as markets spread, they do so increasingly elsewhere.

There are many critics of capitalism and the market capitalism model. As promised by its defenders, capitalism has created material progress. Yet there are trade-offs: It is argued that capitalism creates prosperity only at the cost of rising inequality. Karl Marx believed that owners of capital exploited workers and used imperialist foreign policies to spread markets. Others believe that markets erode virtue. The avarice, self-love, and ruthlessness that energize them are base values that drive out virtues such as love and friendship. Another

[21] Alfred D. Chandler, Jr., "The Emergence of Managerial Capitalism," *Business History Review,* Winter 1984, p. 473.

enduring fear is that markets place too much emphasis on money and material objects. Pope John Paul II, for example, cautioned against a "domination of things over people."[22] Critics see these problems as inherent to markets. Still other criticisms focus on the flaws that sometimes, perhaps inevitably, appear in them. Without correction they may reward conspiracies and monopoly. Also, the profit motive has led companies to pollute and plunder the earth.

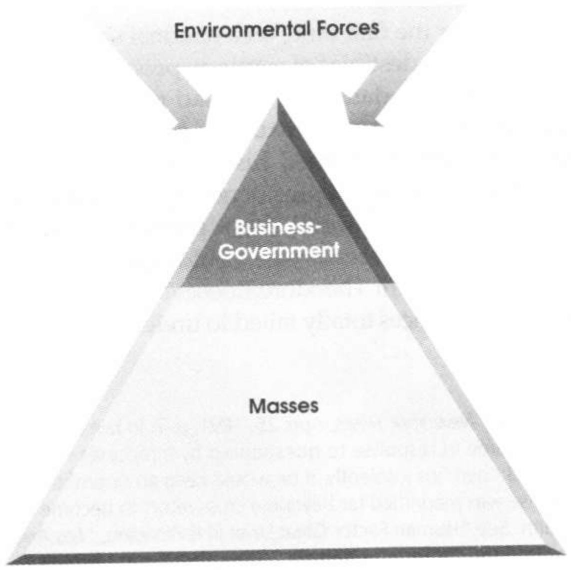
All these criticisms of capitalism are pronounced today, but none are new. They represent a series of recurrent attacks that wind through the Western philosophical tradition. Adam Smith himself had some reservations and second thoughts. He feared both physical and moral decline in factory workers and the unwarranted idolization of the rich, who might have earned their wealth by unvirtuous methods. In his later years, he grew to see more need for government intervention. But Smith never envisioned a system based solely on greed and self-interest. He expected that in society these traits must coexist with restraint and benevolence.[23]

The ageless debate over whether capitalism is the best means to human fulfillment will continue.[24] Meanwhile, we turn our discussion to an alternative model of the BGS relationship that attracts many of capitalism's detractors.

The Dominance Model

The dominance model is a second basic way of seeing the BGS relationship. It represents primarily the perspective of business critics. In it, business and government dominate the great mass of people. This idea is represented in the pyramidal, hierarchical image of society shown in Figure 1.3. Those who subscribe

FIGURE 1.3 The Dominance Model



[22] Encyclical Letter, *Centesimus annus,* May 1, 1991, p. 16.

[23] *The Theory of Moral Sentiments,* ed. E. G. West (Indianapolis: Liberty Classics, 1976), pp. 70–72. Originally published in 1853.

[24] Muller, *The Mind and the Market: Capitalism in Modern European Thought,* pp. x–xiv.

to the model believe that corporations and a powerful elite control a system that enriches a few at the expense of the many. Such a system is undemocratic. In democratic theory, governments and leaders represent interests expressed by the people, who are sovereign.

Proponents of the dominance model focus on the defects and inefficiencies of capitalism. They believe that corporations are insulated from pressures holding them responsible, that regulation by a government in thrall to big business is feeble, and that market forces are inadequate to ensure ethical management. Unlike other models, the dominance model does not represent an ideal in addition to a description of how things are. For its advocates, the ideal is to turn it upside down so that the BGS relationship conforms to democratic principles.

In the United States, the dominance model gained a following during the late nineteenth century when large trusts such as Standard Oil emerged, buying politicians, exploiting workers, monopolizing markets, and sharpening income inequality. Beginning in the 1870s, farmers and other critics of big business rejected the ideal of the market capitalism model and based a populist reform movement called populism on the critical view of the BGS relationship implied in the dominance model.

populism
A political pattern, recurrent in world history, in which common people who feel oppressed or disadvantaged seek to take power from a ruling elite seen as thwarting fulfillment of the collective welfare.

Populism is a recurrent spectacle in which common people who feel oppressed or disadvantaged in some way seek to take power from a ruling elite that thwarts fulfillment of the collective welfare. In America, the populist impulse bred a sociopolitical movement of economically hard-pressed farmers, miners, and workers lasting from the 1870s to the 1890s that blamed the Eastern business establishment for a range of social ills and sought to limit its power.

This was an era when, for the first time, on a national scale the actions of powerful business magnates shaped the destinies of common people. Some displayed contempt for commoners. "The public be damned," railroad magnate William H. Vanderbilt told a reporter during an interview in his luxurious private railway car.[25] The next day, newspapers around the country printed his remark, enraging the public. Later, Edward Harriman, the aloof, arrogant president of the Union Pacific Railroad, allegedly reassured industry leaders worried about reform legislation, saying "that he 'could buy Congress' and that if necessary he 'could buy the judiciary.'"[26] It was with respect to Harriman that President Theodore Roosevelt once noted that "men of very great wealth in too many instances totally failed to understand the temper of the country and its needs."[27]

[25] "Reporter C. P. Dresser Dead," *New York Times,* April 25, 1891, p. 7. In fairness to Vanderbilt, the context of the remark is elusive. It came in response to questioning by a reporter who may have awakened Vanderbilt at 2:00 A.M. to ask, perhaps insolently, if he would keep an unprofitable route in service to the public. Vanderbilt's response was magnified far beyond a cross retort to become the age's enduring emblem of arrogant wealth. See "Human Factor Great Lever in Railroading, "*Los Angeles Times,* October 20, 1912, p. V15; and Ashley W. Cole, "A Famous Remark," *New York Times,* August 25, 1918, p. 22 (letter to the editor).

[26] Quoted from correspondence of Theodore Roosevelt in Maury Klein, *The Life & Legend of E. H. Harriman* (Chapel Hill: University of North Carolina Press, 2000), p. 369.

[27] Ibid., p. 363.

This 1900 political cartoon illustrates a central theme of the dominance model, that powerful business interests act in concert with government to further selfish money interests. Although the cartoon is old, the idea remains compelling for many.
Source: © Bettmann/CORBIS

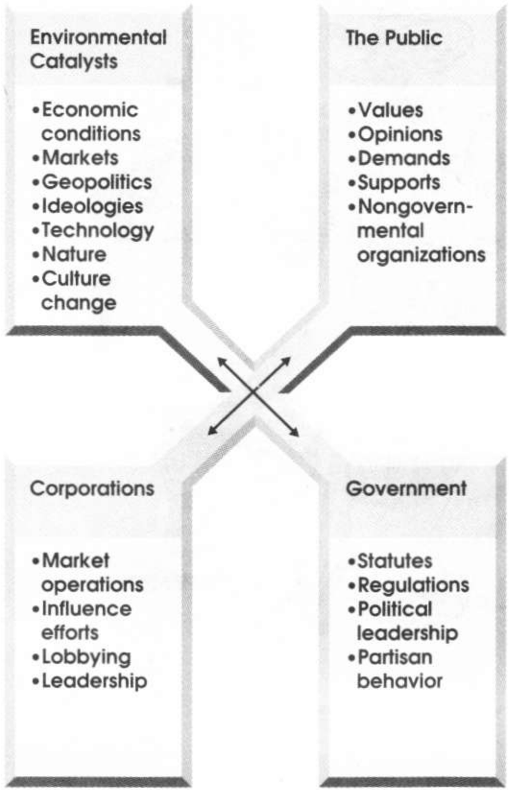
The populist movement in America ultimately fell short of reforming the BGS relationship to a democratic ideal. Other industrializing nations, notably Japan, had similar populist movements. Marxism, an ideology opposed to industrial capitalism, emerged in Europe at about the same time as these movements, and it also contained ideas resonant with the dominance model. In capitalist societies, according to Karl Marx, an owner class dominates the economy and ruling institutions. Many business critics worldwide advocated socialist reforms that, based on Marx's theory, could achieve more equitable distribution of power and wealth.

In the United States the dominance model may have been most accurate in the late 1800s when it first arose to conceptualize a world of brazen corporate power and politicians who openly represented industries. However, it remains popular. Ralph Nader, for example, speaks its language.

> Over the past 20 years, big business has increasingly dominated our political economy. This control by corporate government over our political government is creating a widening "democracy gap." The unconstrained behavior of big business is subordinating our democracy to the control of a corporate plutocracy that knows few self-imposed limits to the spread of its power to all sectors of our society.[28]

[28] "Statement of Ralph Nader," in *The Ralph Nader Reader* (New York: Seven Stories Press, 2000), pp. 3 and 4.

FIGURE 1.4
The Countervailing Forces Model



In recent years fear of transnational corporations has given the dominance model new life in a global context. Running for president in 2004, Nader tried "to rescue our public authorities from the corporate government of big business," particularly "large multinational corporations" that are "increasingly and pervasively replacing the sovereignty of the people."[29]

The Countervailing Forces Model

The countervailing forces model, shown in Figure 1.4, depicts the BGS relationship as a flow of interactions among the major elements of society. It suggests complex exchanges of influence among them, attributing dominance to none.

This is a model of multiple or pluralistic forces. Their strength waxes and wanes depending on factors such as the subject at issue, the power of competing interests, the intensity of feeling, and the influence of leaders. The counter-

[29] See "Ralph Nader Announcement of Candidacy: Toward a 'New Birth of Freedom' and Justice, "February 23, 2004, and "In the Spirit of the Common Good—A Request for Views" (undated), both at www.votenader.org.

vailing forces model reflects the BGS relationship in industrialized nations with democratic traditions. It differs from the market capitalism model, because it opens business directly to influence by nonmarket forces. Many important interactions implied in it would be evaluated as negligible in the dominance model.

What overarching conclusions can be drawn from this model?

1. Business is deeply integrated into an open society and must respond to many forces, both economic and noneconomic. It is not isolated from its social environment, nor is it always dominant.
2. Business is a major initiator of change in society through its interaction with government, its production and marketing activities, and its use of new technologies.
3. Broad public support of business depends on its adjustment to multiple social, political, and economic forces. Incorrect adjustment leads to failure. This is the social contract at work.
4. BGS relationships continuously evolve as changes take place in the main ideas, institutions, and processes of society.

stakeholder An entity that is benefitted or burdened by the actions of a corporation or whose actions may benefit or burden the corporation. The corporation has an ethical duty toward these entities.

primary stakeholders Entities in a relationship with the corporation in which they, the corporation, or both are affected immediately, continuously, and powerfully.

secondary stakeholders Entities in a relationship with the corporation in which the effects on them, the corporation, or both are less significant and pressing.

The Stakeholder Model

The stakeholder model in Figure 1.5 shows the corporation at the center of an array of mutual relationships with persons, groups, and entities called *Stakeholders.* Stakeholders are those whom the corporation benefits or burdens by its actions and those who benefit or burden the firm with their actions. A large corporation has many stakeholders. These can be divided into two categories based on the nature of the relationship. But the assignments are relative, approximate, and inexact. Depending on the corporation or the episode, a few stakeholders may shift from one category to the other.

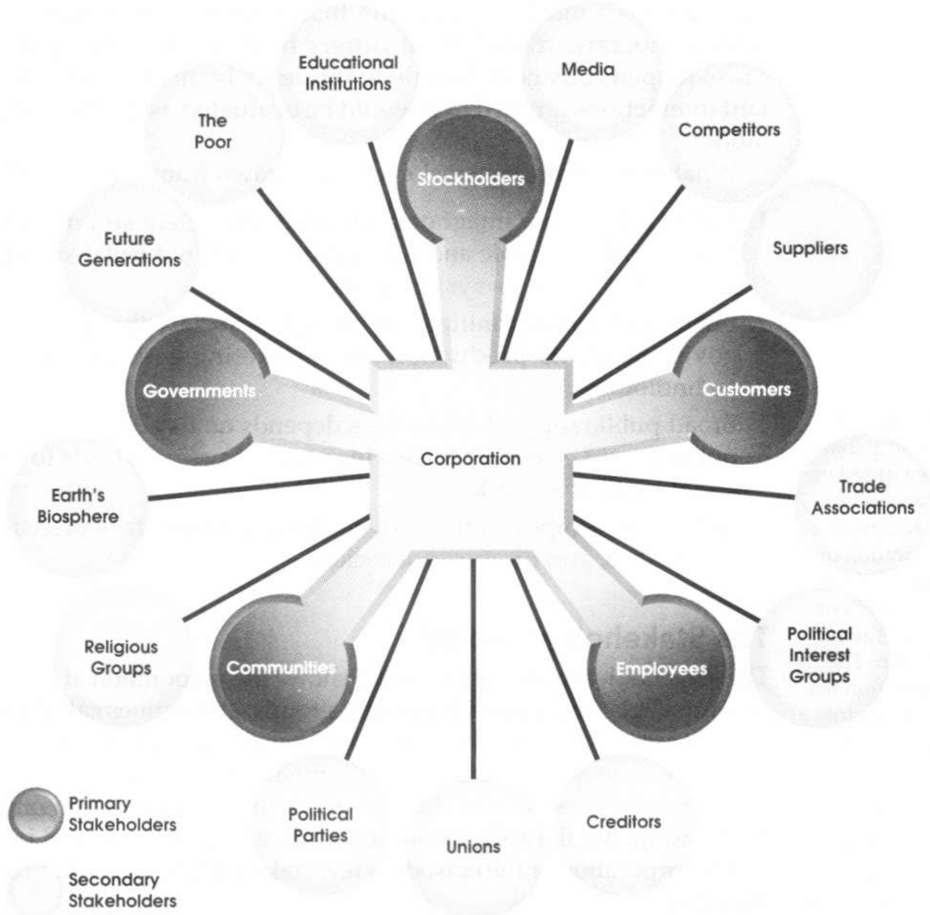
Primary stakeholders are a small number of constituents for which the impact of the relationship is immediate, continuous, and powerful on both the firm and the constituent. They are stockholders (owners), customers, employees, communities, and governments and may, depending on the firm, include others such as suppliers or creditors.

Secondary stakeholders include a possibly broad range of constituents in which the relationship involves less mutual immediacy, benefit, burden, or power to influence. Examples are activist groups, trade associations, and schools.

Exponents of the stakeholder model debate how to identify who or what is a stakeholder. Some use a broad definition and include, for example, natural entities such as the earth's atmosphere, oceans, terrain, and living creatures because corporations have an impact on them.[30] Others reject this broadening, since natural entities are represented by conventional stakeholders such as environmental groups. Some include competitors because, although they do not work to benefit

[30] See, for example, Edward Stead and Jean Garner Stead, "Earth: A Spiritual Stakeholder," *Business Ethics Quarterly,* Ruffin Series no. 2 (2000), pp. 321–44.

FIGURE 1.5
The Stakeholder Model



the firm, they have the power to affect it. At the furthest reaches of the stakeholder idea lie groups such as the poor and future generations. But in the words of one stakeholder advocate, "[s]takeholder theory should not be used to weave a basket big enough to hold the world's misery."[31] If groups such as the poor were included in the stakeholder network, managers would be morally obliged to run headlong at endless problems, taking them beyond any conceivable economic mission.

The stakeholder model reorders the priorities of management away from those in the market capitalism model. There, the corporation is the private property of those who contribute its capital. Its immediate priority is to benefit one group—the investors. The stakeholder model, by contrast, is an ethical theory of management in which the welfare of each stakeholder must be considered as an end.

[31] Max Clarkson, *A Risk-Based Model of Stakeholder Theory* (Toronto: The Centre for Corporate Social Performance & Ethics, 1994), cited in Robert Phillips, *Stakeholder Theory and Organizational Ethics* (San Francisco: Berrett-Koehler, 2003), p. 119.

Stakeholder interests have intrinsic worth; they are not valued only to the extent that they enrich investors. Managers have a duty to consider the interests of multiple stakeholders, and because of this, "the interests of shareowners . . . are not always primary and never exclusive."[32]

Stakeholder management, then, creates duties toward multiple constituents of the corporation—duties not emphasized in the practice of market capitalism, which tends toward domination of the environment and enrichment of shareowners. Management must raise its gaze above profits to see and respond to a spectrum of other values. One group of scholars, for example, urges that corporations "should adopt processes and modes of behavior that are sensitive to the concerns and capabilities of each stakeholder constituency."[33] The stakeholder model is intended to redefine the corporation. It rejects the shareholder-centered view of the firm in the market capitalism model as "ethically unacceptable."[34]

Not everyone agrees. Critics of the stakeholder model argue that it is not a realistic assessment of power relationships between the corporation and other entities. It seeks to give power to the powerless by replacing force with ethical duty, a timeless and often futile quest of moralists. In addition, it sets up too vague a guideline to substitute for the yardstick of profits for investors. Unlike traditional criteria such as return on capital, there is no single, clear, and objective measure to evaluate the combined ethical/economic performance of a firm. According to one critic, this lack of a criterion "would render impossible rational management decision making for there is simply no way to adjudicate between alternative projects when there is more than one bottom line."[35] In addition, the interests of stakeholders so vary that often they conflict with shareholders and with one another. With respect to corporate actions, laws and regulations protect stakeholder interests. Creating surplus ethical sensitivity that soars above legal duty is impractical and unnecessary.[36]

Some puzzles exist in stakeholder thinking. It is not clear who or what is a legitimate stakeholder, to what each stakeholder is entitled, or how managers should balance competing demands among a range of stakeholders. Yet its advocates are compelled by two arguments. First, a corporation that embraces stakeholders performs better. A corporation better sustains its wealth-creating function with the support of a network of parties beyond shareholders. Put bluntly by one advocate of the stakeholder perspective, "[e]xecutives ignore stakeholders at the peril of the survival of their companies."[37] Second, it is the ethical way to manage because stakeholders have moral rights that grow from the way powerful corporations affect them. Irrespective of academic debates, in practice many large

[32] James E. Post, Lee E. Preston, and Sybille Sachs, *Redefining the Corporation: Stakeholder Management and Organizational Wealth* (Stanford, CA: Stanford University Press, 2002), p. 17.

[33] Clarkson Centre for Business Ethics, *Principles of Stakeholder Management* (Toronto: Clarkson Centre for Business Ethics, 1999).

[34] Post, Preston, and Sachs, *Redefining the Corporation,* p. 16.

[35] John Argenti, "Stakeholders: The Case Against," *Long Range Planning,* June 1997, p. 444.

[36] Anant K. Sundaram, "Tending to Shareholders," *Financial Times,* May 26, 2006, p. 6.

[37] "R. Edward Freeman, "The Wal-Mart Effect and Business, Ethics, and Society," *Academy of Management Perspectives,* August 2006, p. 40.

corporations have adopted methods and processes to analyze their stakeholders and engage them. This trend is discussed in Chapter 6.

OUR APPROACH TO THE SUBJECT MATTER

Discussion of the business–government–society field could be organized in many ways. The following is an overview of our approach.

Comprehensive Scope

This book is comprehensive. It covers many subjects. We believe that for those new to the field seeing a panorama is helpful. Because there is less depth in the treatment of subjects than can be found in specialized volumes, we suggest additional sources in footnotes.

Interdisciplinary Approach with a Management Focus

The field is exceptionally interdisciplinary. It exists at the confluence of a fairly large number of established academic disciplines, each of which contributes to its study. These disciplines include the traditional business disciplines, particularly management; other professional disciplines, including medicine, law, and theology; the social sciences, including economics, political science, philosophy, history, and sociology; and, from time to time, natural sciences such as chemistry and ecology. Thus, our approach is eclectic; we cross boundaries to find insight.

strategic management Actions taken by managers to adapt a company to changes in its market and sociopolitical environments.

The dominant orientation, however, is the discipline of management and, within it, the study of *strategic management*, or actions that adapt the company to its changing environment. To compete and survive, firms must create missions, purposes, and objectives; the policies and programs to achieve them; and the methods to implement them. We discuss these elements as they relate to corporate social performance, illustrating successes and failures.

Use of Theory, Description, and Case Studies

theory A statement or vision that creates insight by describing patterns or relationships in a diffuse subject matter. A good theory is concise and simplifies complex phenomena.

Theories simplify and organize areas of knowledge by describing patterns or regularities in the subject matter. They are important in every field, but especially in this one, where innumerable details from broad categories of human experience intersect to create a new intellectual universe. Where theory is missing or weak, scholarship must rely more on description and the use of case method.

No underlying theory to integrate the entire field exists. Fortunately, the community of scholars studying BGS relationships is building theory in several areas. The first is theory describing how corporations interact with stakeholders. The second is theory regarding the ethical duties of corporations and managers. And the third is theory explaining corporate social performance and how it can be measured. Theory in this last area focuses on defining exactly what a firm does to be responsible in society and on creating scales and rulers with which to weigh and measure its actions. Scholarship in all three areas shows increasing sophistication and wider agreement on basic ideas.

Despite the lack of a grand theory to unify the field, useful theories abound in related disciplines. For example, there are economic theories about the impact of

TABLE 1.1 Select Multinational Corporations with High Percentages of Sales, Assets, and Employees Outside Home Countries, 2005

Source: United Nations Conference on Trade and Development, *World, Investment Report, 2007* (New York and Geneva: United Nations, 2007), annex A, table A.I.13.

Company	Sales	Assets	Employees
Nokia (Finland)	99%	65%	57%
Nestlé (Switzerland)	98	65	97
Honda (Japan)	80	74	87
ExxonMobil (United States)	69	69	63
McDonald's (United States)	66	65	78
Procter & Gamble (United States)	57	44	51

government regulation, scientific theories regarding industrial pollution, political theories explaining corporate power, and legal theories on subjects such as negligence applied by courts to corporations when, for example, industrial accidents occur. When fitting, we discuss such theories; elsewhere we rely on descriptions of events. We also use case studies at the end of each chapter to raise issues for discussion.

Global Perspective

Today global capitalism animates the planetary stage, creating movements of people, money, goods, and information that, in turn, beget conflicts as some benefit more and others less or not at all. Viewing any nation's economy or businesses in isolation from the rest of the world is myopic. Every government finds its economic and social welfare policies judged by world markets. Every corporation has a home country, but as shown in Table 1.1, many large multinational corporations have more sales, assets, and employees outside its borders than within. For now, global capitalism is ascendant. It brings unprecedented wealth creation and new material comforts. But it also imposes burdens on human rights and the environment, challenges diversity of values, and creates conflict with those who are fed upon in the lively predation or who stand aloof from the free market consensus. A fitting perspective on the BGS relationship must, therefore, be global.

Historical Perspective

history
The study of phenomena moving through time.

History is the study of phenomena moving through time. The BGS relationship is a stream of events, of which only one part exists today. Historical perspective is important for many reasons. It helps us see that today's BGS relationship is not like that of other eras; that current ideas and institutions are not the only alternative; that historical forces are irrepressible; that corporations both cause and adapt to change; that our era is not unique in undergoing rapid change; and that we are shaping the future now. When appropriate, we examine the antecedents of current arrangements.

Chapter Two

The Dynamic Environment

Royal Dutch Shell PLC

Royal Dutch Shell is the world's second largest private energy company, operating in 130 countries. Each year it makes capital investments of between $15 and $19 billion, sums that are larger than the annual revenues of all but a few corporate behemoths.[1] With such large sums and payoffs that come only after years—even decades—risks are also large. Shell exists in an uncertain geopolitical environment stirred by forces it cannot dominate. Even a giant must bend to heedless fortune. Are its investments the right ones for the world of the future?

scenario
A plausible story of the future based on assumptions about how current trends might play out.

To find out, Shell convenes teams of elite scholars and staff that create alternate visions of this future called scenarios.[2] A *scenario* is a plausible story of the future based on assumptions about how current trends might play out. Carefully written scenarios challenge managers to think in original ways. They are mental wind tunnels that shift environmental forces around the form of the company to see how it "flies."

Scenarios were first used in the 1960s by scholars studying the idea of a nuclear war between Russia and the United States. With no historical precedent for an exchange of atomic bombs, they drew up riveting alternatives about how such a battle might advance.[3] In the 1970s, Shell pioneered the use of scenarios in corporate planning and they soon proved helpful. In 1971 its planners created a scenario in which oil-rich countries cut their oil exports to raise prices. Conventional wisdom at the time held this improbable. Nonetheless, thinking about the possibility changed Shell's strategy, and when an oil embargo surprised the world in 1973 it was the only major oil firm ready for the supply interruption. Shell's reward was higher profits than its competitors for years afterward. Shell then continuously used scenarios as a basis for its strategic thinking. In the 1990s, its planners formed a theory of change in the

[1] Royal Dutch Shell plc, Form 20-F (2005), p. 3.

[2] See Peter Cornelius, Alexander Van de Putte, and Mattia Romani, "Three Decades of Scenario Planning in Shell," *California Management Review,* Fall 2005.

[3] For example, Herman Kahn, *On Escalation: Metaphors and Scenarios* (New York: Praeger, 1965).

liberalization An economic policy of lowering tariffs and other barriers to encourage trade.

global business environment caused by three dominant forces: globalization, technological change, and *liberalization* (meaning relaxation of trade restrictions and regulations). According to Shell, these forces made up "a rough, impersonal game, involving stresses and pressures akin to those of the Industrial Revolution."[4]

Until 2001, a series of scenarios created imaginary worlds that adapted differently to the three forces. Then, two occurrences created what Shell planners call "discontinuities," or unforecast events that alter ongoing, predictable trends. First, scandals produced a global wave of public mistrust focused on corporations and markets. These included not only the banner criminality at Enron, Worldcom, Adelphia, and Tyco in the United States, but also cheating at firms such as Parmalat in Italy, Vivendi in France, and Tokyo Electric Power in Japan. Second, terrorism, particularly the September 11 attacks, combined with upheavals in the Middle East to produce a security crisis.

To explore the effect of the twin crises of trust and security to the year 2025, Shell's planners built three new global scenarious.[5]

- In a *Low Trust Globalization* scenario the trend toward globalization continues. Strong economic growth in China, India, and Brazil dramatically raises world energy demand. But anxiety over security and suspicion of markets require Shell to operate in a climate of heavy regulation and public distrust. Coercive and complex government rules force more disclosure and more corporate responsibility. Nations enact new taxes to discourage pollution. Activist groups become more confrontational and litigious. Transnational corporations grow in size because spreading heavy regulatory costs over large operations is economical.
- *Open Doors* is a contrasting world of globalization and strong economic growth. In this scenario, security issues recede and trust in markets is restored. Shell does not face a climate of oppressive laws and regulation. Instead, a vibrant, global civil society emerges and, along with it, global norms of corporate social responsibility. Companies work cooperatively with stakeholders to promote a more just and sustainable world, even cooperating with governments in joint delivery of services such as education and health. Demand for oil grows, but new incentives to develop renewable sources of energy emerge also.
- The last scenario is *Flags*. The term "flags" is a metaphor for the multiple entities in a splintered world of values, causes, nations, religions, and global crusades. Splits within societies and nations deepen. Terrorism continues. Trust is low. Trade barriers rise as nations put security before economic growth. Globalization stalls. World energy demand is flat. Taxes on business rise. In a climate of deep distrust, activists and the media closely watch big firms such as Shell to ferret out wrongdoing. People become very cynical about voluntary corporate social responsibility. Agreement on international norms of corporate behavior is weak, so a patchwork of bridling national regulation grows.

Such story worlds may be more fantasy than prophecy. However, they show the importance that Shell places on understanding its dynamic external environment. In

[4] Shell International Limited, *Global Scenarios 1995–2020*, Public Scenarios PX96-2, 1996, p. 2.

[5] Shell International Limited, *The Shell Global Scenarios to 2025* (London: Shell Center, 2005).

what follows we present a framework for understanding the forces that animate this environment. First, we identify deep historical forces that create change and risk. Then, we identify key dimensions of the global business environment and describe major trends within them.

UNDERLYING HISTORICAL FORCES CHANGING THE BUSINESS ENVIRONMENT

We believe that, in a broad sense, order can be found in the swirling patterns of current events; that there is a deep logic in the passing of history; and that change in the business environment is the result of elemental historical forces moving in roughly predictable directions. Henry Adams defined a *historical force* as "anything that does, or helps to do, work."[6] The work to which Adams refers is the power to cause events. Change in the business environment is the work of nine deep historical forces or streams of related events discussed below.

historical force
An environmental force of unknown origin and mysterious action that provides the energy for events. The discussion divides this force, somewhat artificially, into nine separate but related forces causing distinct chains of events.

industrial revolution
Transforming changes that turn agricultural economies into industrial economies. This transformation occurs in the presence of certain economic, technological, political, and philosophical conditions.

The Industrial Revolution

The first historical force is the industrial revolution, a powerful force that grips the imagination of humanity. The term *industrial revolution* refers to transforming changes that turn simple economies of farmers and artisans into complex industrial economies. In thousands of years before the industrial takeoff of Great Britain in the late eighteenth century, there had been no widespread, sustained economic growth to raise living standards. The vast majority of the world's population was mired in poverty.

Industrial transformation requires specific conditions, including a sufficiency of capital, labor, natural resources, and fuels; ready transportation; strong markets; and ideas and institutions that support the productive blend of these ingredients. Britain came first because it was first to have the right mix of social, political, and economic supports. It was an open society that allowed social mobility and encouraged individual initiative. Its parliament embodied values of political liberty, free speech, and public debate. Perhaps consequently, Britain was the source of scientific advances and inventions such as the steam engine that liberated energy in the nation's massive coal deposits. Its climate supported agriculture and its island geography put it at the hub of sea routes for world trade.[7]

After Britain's takeoff, conditions for sustained economic growth arose in western Europe and the United States during the nineteenth century. Japan and Russia followed in the first half of the twentieth century, and other Asian nations, including Taiwan, South Korea, and China, followed in the second half. Industrialization continues to spread as less developed nations try to create the conditions for it.

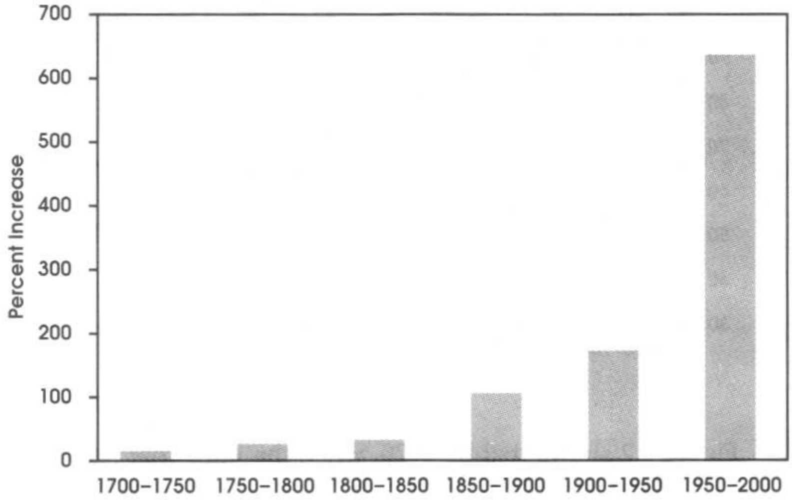
Industrial growth remakes societies. It elevates living standards, alters life experience, and shifts values. Historically, material progress has been associated

[6] In the essay "A Dynamic Theory of History (1904)," in Henry Adams, *The Education of Henry Adams* (New York: Modern Library, 1931), p. 474; originally published in 1908.

[7] See Jeffrey Sachs, *The End of Poverty: Economic Possibilities for Our Time* (New York: Penguin Press, 2005), chapter 2.

FIGURE 2.1
World GDP Growth in 50-Year Intervals

Source: Bradford J. DeLong, "Estimating World GDP, One Million B.C.–Present," available at http://econ161.berkeley.edu.



with moral progress; that is, in the words of one historian, it "fosters greater opportunity, tolerance of diversity, social mobility, commitment to fairness, and dedication to democracy."[8] Since institutions built on older ideas change more slowly than people's lives, industrialization generates huge strains in the social fabric even as it elevates civil life. The size and acceleration of economic growth in the twentieth century were astounding. The total amount of goods and services produced exceeded all that was produced in prior human history. As Figure 2.1 shows, output for just the half century from 1950 to 2000 exceeded all that came before. This growth continues today, generating enormous tensions in both developing and developed societies.

Inequality

From time immemorial, status distinctions, class structures, and gaps between rich and poor have characterized societies. Inequality is ubiquitous, as are its consequences—envy, demands for fair distribution of wealth, and doctrines to justify why some people have more than others. The basic political conflict in every nation, and often between nations, is the antagonism between rich and poor.[9]

Gini index A statistical measure of inequality in which 0 is perfect equality (everyone has the same amount of wealth) and 100 is absolute inequality (a single person has all wealth).

As the industrial revolution accelerated the accumulation of wealth, it worsened the persistent problem of uneven distribution. Explosive economic growth widened the gap between rich and poor around the globe. Global income inequality is measured by the *Gini index,* a statistic in which 0 percent stands for absolute equality, that is, a theoretical situation in which everyone has the same income, and 100 percent represents absolute inequality, where one person has all the income. Using this measure, inequality becomes greater as the percentage figure rises toward 100.

[8] Benjamin M. Friedman, *The Moral Consequences of Economic Growth* (New York: Knopf, 2005), p. 4.
[9] Mortimer J. Adler, *The Great Ideas* (New York: Macmillan, 1992), pp. 578–79.

FIGURE 2.2
World Poverty and Income Inequality since 1820

Sources: François Bourguignon and Christian Morrisson, "Inequality among World Citizens: 1820–1992," *American Economic Review*, September 2002, table 1; UNDP, *Human Development Report 2005*, p. 4; and U.S. Census Bureau, "Total Midyear Population for the World: 1950–2050," April 2004.

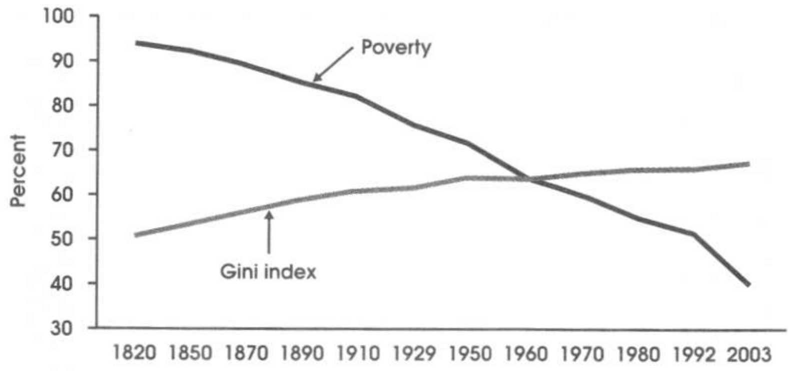


Figure 2.2 shows that by 1820, when the industrial revolution was spreading from England to western Europe, global income inequality was already very high. The Gini index of 50 percent in 1820 climbed to 61 percent in 1910, as economies in industrializing nations rapidly expanded. After that, the rise continued, but more slowly, as populous Asian countries holding the bulk of the world's poor began to industrialize and catch up. The Gini index reached 64 percent in 1950 and continued its decelerating rise to 67 percent in 2003.[10] This represents an extreme level of inequality across the world population, so high that it exceeds the inequality within any single nation. It reflects a situation in which the top 5 percent of people receive about 33 percent of all income and the bottom 5 percent receive 0.2 percent.[11] The cause of this striking gap is the diverging economic fortunes of nations.

Contrary to popular opinion, economic growth itself does not increase income inequality within modernizing nations. During industrialization the incomes of the poorest people rise in proportion to the rise in average income for the country as a whole.[12] The cause of most of the rise in world income inequality is a growing gap between the peoples of rich and poor nations, not a growing separation of rich and poor within nations.

Today about 2.6 billion people live in poverty, defined as an income of less than \$2 a day.[13] This is more poor people than any time in history, an enormous pool of misfortune constituting 40 percent of the world population. Yet in 1820, near the beginning of the industrial revolution, 94 percent of the world's population lived in poverty. A great and steady retreat in the poverty percentage for almost two centuries, in the face of vaulting population growth, is testimony to the wealth-creating power of industrial development. Even as economic growth has widened

[10] Figures are from François Bourguignon and Christian Morrisson, "Inequality among World Citizens: 1820–1992," *American Economic Review*, September 2002, pp. 731–32; and United Nations Development Programme, *Human Development Report 2005* (New York: Oxford University Press, 2005), p. 55.

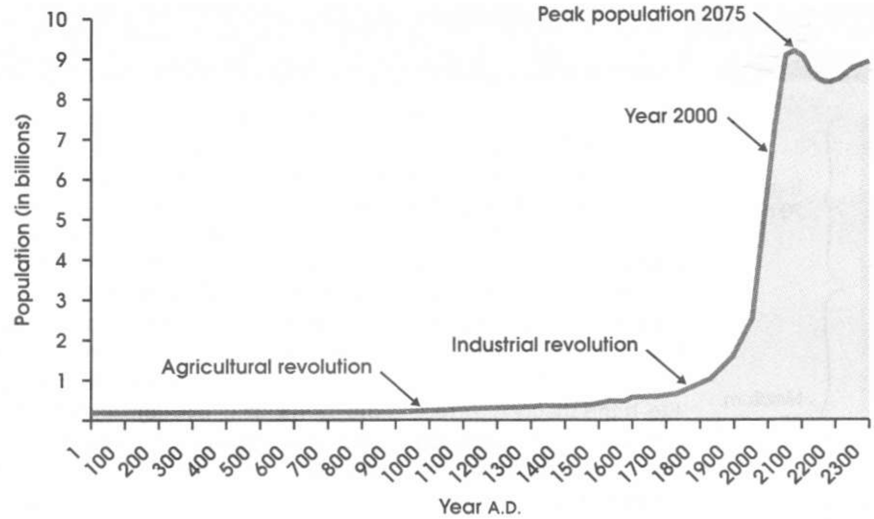
[11] Branko Milanovic, "Global Income Inequality: What It Is and Why It Matters," World Bank Policy Research Working Paper 3865, March 2006, p. 16.

[12] David Dollar and Aart Kraay, "Spreading the Wealth," *Foreign Affairs*, January/February 2002, p. 128.

[13] United Nations Development Programme, *Human Development Report 2007/2008*, p. 25.

FIGURE 2.3 Historical World Population Growth and Projections: 1 A.D. to 2300

Sources: U.S. Bureau of the Census, "Historical Estimates of World Population," available at www.census.gov/ipc/www/worldhis.html; and United Nations, *World Population to 2300*, table A1.



the gap between rich and poor, it has dramatically reduced the proportion of the poor in the total population.

Although the Gini index trend line in Figure 2.2 seems to rise only modestly over the years, it in fact represents a striking confluence of progress and tragedy. If world distribution of income had not become more unequal after 1820, economic growth would have reduced the number of people living in poverty today by an estimated 80 percent.[14] Instead, as the wealth gap between nations widened with each passing year, the distribution of income grew more unequal. Yet even as inequality worsened, the drop in the poverty trend line shows how economic growth has led to a continuous, sharp reduction in privation.

Inequality is resilient and, according to the United Nations, "truly staggering on a global scale."[15] It is perpetuated by social institutions such as caste, marriage, land ownership, law, and market relationships. Arrangements and rules in these institutions are resilient, creating sinkholes of unequal opportunity. The vast majority of the world's 2.6 billion poor people live in nations not yet transformed by industrial growth where entrenched inequities persist over generations. This situation creates expectations that ethical duties of global corporations include helping the poor and equitably distributing the fruits of commerce. The historical lesson of almost two centuries is that if capitalism is harnessed to create economic growth, the poor will benefit.

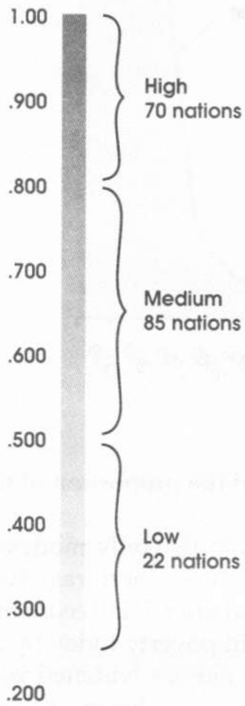
Population Growth

The basic population trend throughout human history is growth. As shown in Figure 2.3, world population inched ahead for centuries, then grew a little faster

[14] Bourguignon and Morrisson, "Inequality among World Citizens," p. 733. The $2-a-day figure represents what could be purchased in the United States for $2, not what could be purchased in local currency.

[15] World Bank, *World Development Report 2006: Equity and Development* (New York: Oxford University Press, 2005), p. 8.

The Human Development Index



The Human Development Index (HDI) is a statistical tool used by the United Nations for measuring the progress of humanity. It is based on the theory that income alone is not an adequate measure of the standard of living, let alone a rich and fulfilling life. If this theory is correct, discussions of inequality based on income differences within and between nations do not give a complete picture of differences in human welfare.

The HDI is a scale running from 0 to 1, with 1 representing the highest human development and 0 the lowest. It measures the development of nations as an average of scores in three equally weighted categories.

- *Longevity,* or life expectancy at birth.
- *Knowledge,* or the adult literacy rate plus the ratio of students enrolled in school as a percentage of the population of official school age.
- *Income,* or gross domestic product per capita (in equivalent U.S. dollars).

Of the 177 nations in the 2005 Human Development Index, 70 have high index values of 0.800 or above, 85 are in the medium range with values of 0.500 to 0.799, and 22 fall in the low range with values below 0.499. Iceland is highest ranked with an index value of 0.968. Sierra Leone is lowest at 0.336. The United States ranks eighth with 0.948.[16]

Historical HDI index values show enormous increases in human welfare since the late nineteenth century, as a consequence mainly of declining mortality and economic growth. In 1870 the United States had an HDI value of 0.467, a score that today is equaled by Tanzania in the low human development category. In 1913 it had an HDI value of 0.730 that would today rank it slightly below Viet Nam deep in the medium human development category.[17]

Since 1950 the absolute gap between the highest- and lowest-rated countries has narrowed substantially, showing that inequality in living standards around the world, as measured by the HDI, is declining even while income inequality, as measured by per capita GDP, is rising. Thus, inequality is greater if measured only by monetary income and less if longevity and education, two traditional measures of a good life, are taken into consideration.

[16] United Nations Development Programme, *Human Development Report 2007/2008* (New York: United Nations Development Programme, 2007), pp. 234–37.

[17] Nicholas Crafts, "Globalization and Growth in the Twentieth Century," IMF working paper, WP/pp/44 (Washington, DC: International Monetary Fund, March 2000), pp. 6–7.

beginning about 1,000 years ago with the inception of large-scale crop cultivation. After eight more centuries, population growth began a rapid new acceleration in the late 1800s that turned into a skyrocketing rise through the twentieth century. It took until 1825 for the world population to reach 1 billion; then each billionth additional person was added faster and faster—first in 100 years, then in 35, then in 15, then in only 12.[18] This astonishing growth had two causes, both related to the industrial revolution. First, advances in water sanitation, hygiene, and scientific medicine reduced deaths from infectious disease, leading to rapid mortality decline. Second, mechanized farming expanded the food supply to feed record numbers.

[18] Clive Ponting, *A Green History of the World* (New York: Penguin Books, 1991), p. 240.

World population reached 6.6 billion in 2007 and it continues to rise, but growth is predicted to slow and, for the first time in recorded history, end. Figure 2.3 shows United Nations projections that the world population will grow to a peak of 9.2 billion in 2075, then decline over a century to 8.3 billion in 2175 before slowly rising back to 9 billion in 2300.[19] This is an intriguing preview of the distant future, but for the near future, in the years 2010 to 2050, rapid though slowing growth will characterize the business environment.

Growth will slow and eventually end as the world undergoes a transition from high to low fertility. In the initial stages of the industrial revolution economic progress encouraged population growth. Now this progress is a brake on fertility because having fewer children frees women to attend school, enter professions, and increase income. The world's total fertility rate, or the number of births per woman, dropped from 5.12 in 1950 to 2.65 in 2005 and is expected to drop as low as 2.05 by 2050.[20] This would be below the *replacement fertility rate* of 2.1 births per woman, calculated as the number of children a woman must have on average to ensure that one daughter survives to reproductive age. In theory, this number is sufficient to maintain a stable population. Fertility is declining on all continents, but the world average of 2.65 disguises wide variation. Fertility is lowest in a group of 44 developed nations averaging 1.56 and highest in a group of 148 less developed nations averaging 2.9. The extremes are captured by Hong Kong's low fertility rate of .94 as opposed to Niger's world high of 7.91.[21]

replacement fertility rate The number of children a woman must have on average to ensure that one daughter survives to reproductive age.

The world population is also aging. Its median age rose from 24 years in 1950 to 28 years now and it will rise faster up to 2050 when it is projected to be 38. Aging will be most rapid in developed nations where mortality rates are lowest. As with fertility, global age averages mask extremes. In Japan, the world's oldest population has a median age of 43 and a life expectancy of 82, far higher than in African nations such as Malawi, where the median age is 16 and life expectancy is only 40 years.[22]

Migration now plays a larger role in population dynamics than in the past. In the 1950s immigration was a negligible factor, leading to net population changes of no more than 5,000 a year in any nation. Today, about 2.6 million people a year migrate to developed countries. For the decade 2000 to 2010, the United States will take in more immigrants than any other nation, about 11.6 million. Mexico and China will lose the most people, 3.8 and 3.7 million, respectively.[23]

Falling fertility, low mortality, and migration will drive future population changes. About 95 percent of all growth to 2050 will occur in developing and less

[19] United Nations, *World Population to 2300* (New York: United Nations Department of Economic and Social Affairs, 2004), p. 2. Figures in this section are based on the medium variant of the 2004 revision of the population database.

[20] United National Department of Economic and Social Affairs, Population Division, *World Population Prospects: The 2004 Revision*, vol. III, *Analytical Report* (New York: United Nations, 2006), tables III.4 and III.9.

[21] Ibid., table III.1, III.2, and III.4.

[22] Ibid., tables II.3 and IV.2.

[23] Ibid., tables V.2.

developed countries, with only 5 percent in the developed world. Fertility will be lowest in Europe and by 2050 its population will fall 10 percent or by 75 million people, reducing it from 11 percent of the world's population to only 7 percent. In North America the population will grow by 32 percent, but due to declining fertility rates in the United States (from 2.04 in 2005 to 1.85 in 2050) this growth will come from immigration. Africa, which contains most of the world's least developed nations, will grow fastest. Despite elevated mortality from the HIV/AIDS epidemic, by 2050 it will add more than 1 billion people, an increase of 114 percent from 2005.[24]

These population trends have many implications. First, although overall world growth is slowing, it will be highest in less industrialized regions, further widening the wealth gap between high- and low-income countries. Second, growth will continue to strain the earth's ecosystems, especially as industrial activity spreads. Third, the West is in demographic decline compared with other peoples. Shrinking, aging populations may lead to lower GDP growth rates and put pressure on national welfare and pension policies.[25] In the future, growing non-Western populations will be stronger economically, militarily, and politically and will push to expand their influence. Although Western market values and business ideology seem ascendant now, they may be less widespread in the future as the numerical basis of Western civilization declines. In such ways will population trends alter the business environment and create new societal expectations for corporate behavior.

Technology

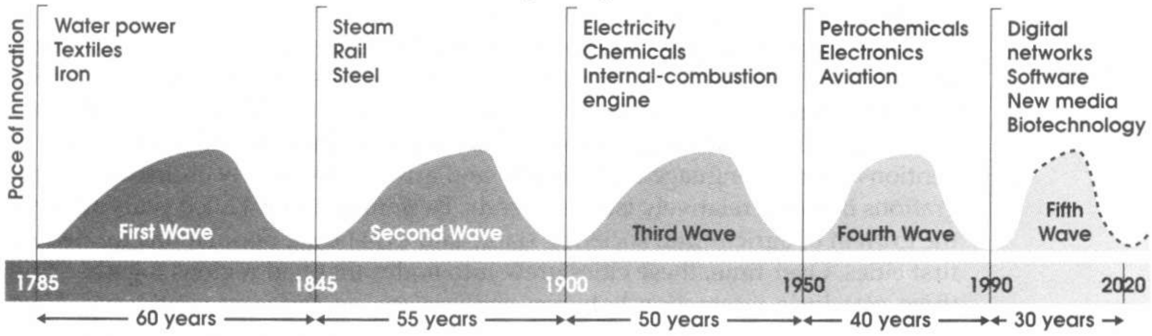
Throughout recorded history new technologies and devices have fueled commerce and reshaped societies. In the 1450s the printing press was an immediate commercial success, but its impact went far beyond the publishing business. Over the next 100 years the affordable, printed word reshaped European culture by creating a free market for ideas that undermined the doctrinal monopoly of the Catholic Church. Printed pamphlets spread Martin Luther's challenge to its scriptural dogma and brought on the Protestant Reformation. Galileo was placed under house arrest in Florence for holding heretical views about astronomy, but his theories prevailed because they were published in Protestant Holland. A Europe opened to the exchange of new ideas based on experience and observation was primed for the scientific revolution.

The invention of the steam engine in the late 1700s and its widespread use beginning in the early 1800s, along with increased use of the waterwheel and new iron-making methods, triggered the industrial revolution. As Figure 2.4 shows, this was the first of five waves of technological revolution. With each wave innovations spread, stimulating economic booms of increased investment, rising productivity, and output growth. The shortening of successive waves reveals faster innovation.

[24] United Nations Department of Economic and Social Affairs, Population Division, *World Population Prospects: The 2004 Revision*, vol. III, *Analytical Report*, table 1.

[25] Nicoletta Batini, Tim Callen, and Warwick McKibbin, "The Global Impact of Demographic Change," IMF Working Paper, WP/06/9, January 2006, pp. 3 and 13.

FIGURE 2.4 **Waves of Innovation since the Beginning of the Industrial Revolution**



Source: "A Survey of Innovation in Industry," *The Economist*, February 20, 1999, p. 8. Copyright © 1999 The Economist Newspaper, Ltd. All rights reserved. Further reproduction prohibited. Reprinted with permission.

New technologies foster the productivity gains that sustain long-term economic progress, and they promote human welfare. However, like the printing press, they also can agitate societies. For example, before the 1860s a transatlantic voyage on a sailing ship took a month, cost a year's wages for a European worker, and was risky. About 5 to 10 percent of passengers died due to sinkings and shipboard transmission of diseases. Then steamship technology cut the cost of passage by 90 percent and reduced travel time to one week, cutting mortality to less than 1 percent. As a result, European immigrants poured into the American east, creating labor gluts that led to wage depressions and fueling political movements against big companies, financiers, and the gold standard.[26] In this way, steamship technology strained American political stability.

During the rise of industrial societies over more than two centuries, technology has altered human civilization by stimulating economic and population growth to sustained rises unimaginable in previous recorded history. New things have created many benefits, including higher living standards and longer life spans, but because technology changes faster than human beliefs and institutions, it also imposes strains.

Globalization

globalization The creation of networks of human interaction that span worldwide distances.

Globalization occurs when networks of economic, political, social, military, scientific, or environmental interdependence grow to span worldwide distances.[27] In the economic realm, globalization occurs when nations open themselves to foreign trade and investment, creating world markets for goods, services, and capital. The current rise of such a system began after World War II, when the victor nations lowered trade barriers and loosened capital controls. Over the next 50 years, international negotiations led more nations to open themselves to global

[26] Robert William Fogel, *The Fourth Great Awakening & The Future of Egalitarianism* (Chicago: University of Chicago Press, 2001), p. 54.

[27] Joseph Nye, Jr., "Globalization's Democratic Deficit," *Foreign Affairs*, July–August 2001, p. 2.

flows of goods, services, and investment until today no national economy of any significance remains isolated from world markets.

Today's economic globalization is the leading edge of a long trend. For thousands of years the human community has, in fits and starts, become more tightly knit. According to historians J. R. McNeill and William H. McNeill, in prehistoric times humans interacted in a loose worldwide web through which genes and inventions such as language and the bow and arrow were slowly exchanged by migrations between relatively isolated bands. Beginning about 12,000 years ago with the growth of agricultural societies, stable and expanding populations formed the first cities. Over time, these cities grew into nodes that tied regions together. Still, there was little interaction between civilizations on different continents. Then, about 500 years ago, China sponsored oceanic voyages to extend its power.[28]

Soon Portugal and Spain followed and over the next 250 years mariners connected even the most remote places to the great centers of civilization. By the late 1700s the world was knit together with the exchange of trade goods, currencies, and ideas. The consequences of this initial globalization are similar to those arising from the current globalization. Economic activity rapidly increased. Mines in Bolivia exported such quantities of silver that nations around the world adopted silver currencies, smoothing international trade. Trade expansion increased inequality among nations. Cultures changed, as when, for example, Spanish conquistadors introduced horses to the Plains Indians. Infectious diseases spread. In little more than a century microbes endemic to Europe killed 50 to 90 percent of the population of the Americas from Cape Horn to the Arctic.

Since this initial tying together of societies in the late 1700s, the trend toward integration has continued. Globalization has been accelerated by new technologies, particularly those based on electricity, but also sometimes slowed by national rivalries and wars.

Transnational corporations, especially a few hundred of the largest headquartered in developed nations, are the central forces of current economic globalization. Their rising levels of investment outside home countries make them the modern equivalents of the intrepid mariners who opened trade routes in the 1400s. Many of these firms have more resources than the governments of smaller nations. However, globalization complicates their management. By operating in many countries they multiply the number and kind of stakeholders to which they must respond. Their actions create strains and anxieties that lead to heightened expectations of responsible behavior. In addition, there is a strong anticorporate movement supported mainly by groups in rich nations that see the growing velocity of trade with alarm because it clashes with their values on the environment, human rights, and demo cracy. These groups seek to restrain and regulate the activities of transnational corporations and they have had some success.

nation-state An international actor having a ruling authority, citizens, and a territory with fixed borders.

Nation-States

In the international arena, the *nation-state* is an actor formed of three elements, a ruling authority, citizens, and a territory with fixed borders. The modern nation-state

[28] *The Human Web* (New York: Norton, 2003), intro. and chap. VI.

system arose in an unplanned way out of the wreckage of the Roman Empire. The institution of the nation-state was well-suited for Western Europe, where boundaries were contiguous with the extent of languages. However, the idea was subsequently transplanted to territories in Eastern Europe, Southwest Asia, and the Middle East, partly by force of colonial empires and partly by mimicry among non-Western political elites for whom the idea had attained high prestige. Where it was transplanted, nations were often irrationally defined and boundary lines split historic areas of culture, ethnicity, religion, and language.

The nation-state is the unit of human organization in which individuals and cultural groups can influence their circumstances and future. This is its paramount function and the reason it has survived over centuries. Today the world is a mosaic of independent countries, and the dynamics of this system are a powerful force in the international business environment. Conflict between nations seeking to aggrandize wealth and power is frequent, though because of economic globalization its nature has changed.

In the past, nations increased their power by seizing territory. With more territory they acquired new natural resources, agriculture, and labor. Hence, in the 1930s Japan colonized South Asian countries to gain access to oil and bauxite. Now, however, the wealth of high-income nations is based on the operation of global corporations that use flows of capital and knowledge to provide goods and services in many nations. Seizing the headquarters or a few manufacturing facilities of one of these corporations would not enable the aggressor nation to take advantage of the value chain in the firm's worldwide operations, particularly where wealth creation was based on brainpower. So nations today increasingly prefer to aggrandize themselves through trade, where they can build wealth more efficiently than through traditional warfare designed to seize land and material resources.[29]

Even as world markets become new sources of national power, they also limit the power of regimes to control their economies. Freewheeling international competition penetrates borders. Nations have a choice. Either close borders to flows of goods, services, and capital, isolating their economies from the world, a move sure to stifle growth, or open borders, allowing free reign to disobedient market forces that quicken growth. No nation can choose isolation and still offer its citizens opportunity and prosperity. So governments are now deeply concerned about how international markets will interpret their domestic actions and policies.

An example is the fate of Mexico after it opened its economy to the North American market in the early 1990s. In 1994, when the government attempted to maintain the peso's value relative to the dollar, world markets rejected the move. Currency speculators attacked the peso and foreign investors pulled great sums of money out of the country. The peso collapsed. Its devaluation halved the life savings of average Mexican citizens and caused bankruptcies, inflation above 50 percent a year, and a 6 percent drop in GDP.[30] Soon similar speculation caused currency

[29] This thesis is elaborated in Richard Rosecrance, *The Rise of the Virtual State* (New York: Basic Books, 1999).
[30] Jeffry A. Frieden, *Global Capitalism: Its Fall and Rise in the Twentieth Century* (New York: Norton, 2006), p. 389.

devaluations and sell-offs in six East Asian countries, prompting the prime minister of Malaysia to say that he was "very scared about foreign capital."[31]

Market forces are just one force that penetrates nation-states and reduces their autonomy. Other forces are epidemics, climate change, terrorism, nuclear weapons, and potent ideas such as international norms of human rights.[32] As intractable global forces, particularly market power, undercut the ability of national governments to protect their citizens, corporations may be called on to assume more of the responsibility.

Dominant Ideologies

ideology
A set of reinforcing beliefs and values that constructs a worldview.

Thought shapes history. An *ideology* is a set of reinforcing beliefs and values that constructs a worldview. The industrial revolution in the West was facilitated by a set of interlocking ideologies, including capitalism, but also constitutional demo cracy, which protected the rights that allowed individualism to flourish; progress, or the idea that humanity was in upward motion toward material betterment; Darwinism, or Charles Darwin's finding that constant improvement characterized the biological world, which reinforced the idea of progress; social Darwinism, or Herbert Spencer's idea that evolutionary competition in human society, as well as the natural world, weeded out the unfit and advanced humanity; and the Protestant ethic, or the belief that sacred authority called for hard work, saving, thrift, and honesty as necessary for salvation.

Ideologies are more than the sum of sensory perception and rational thought. They fulfill the human need for concepts and categories of meaning that explain daily life. Ideologies in accord with experience and current conditions often spread widely. Their belief systems lead adherents to feel a collective identity and to follow common norms that direct social behavior, thereby promoting cooperation and stability. And they give institutions that represent them, such as churches, governments, and corporations, the power to interpret events and resolve human problems.[33]

Ideologies are highly competitive and locked in a constant Darwinian struggle. Vibrant pluralism of belief existed for most of recorded history, but many doctrines have perished with globalization. As ideas diffuse through trade, travel, missionary work, and conquest, they often clash. A centuries-old culling process in the marketplace of ideas has eliminated and marginalized many historical belief systems and favored the ascendancy of a few.[34] Hundreds of local religions, unable to compete with the world salvation religions, have gone extinct. Cultural styles in entertainment, dress, sports, and food now converge in urban societies. In the political sphere monarchy and dictatorship are fighting an end game against democracy. After two

[31] Mahathir Bin Mohamad, "Asian Economies: Challenges and Opportunities," *Vital Speeches of the Day*, October 15, 1997, p. 12.

[32] Philip Bobbitt, "The Market State," in Shell International Limited, *The Shell Global Scenarios to 2025*, p. 160.

[33] Michael Mann, *The Sources of Social Power*, vol. 1 (Cambridge, England: Cambridge University Press), 1986, pp. 20–23.

[34] J. R. McNeill and William H. McNeill, *The Human Web*, pp. 269–76.

centuries of contention, the economic ideology of capitalism has marginalized its rival socialism. This sifting of ideas accelerated in the twentieth century because of rising literacy and innovations that spread information, from magazines and radios in the early part of the century to jet aircraft and computers later.

Great Leadership

Leaders have brought both beneficial and disastrous changes to societies and businesses. Alexander imposed his rule over the ancient Mediterranean world, creating new trade routes on which Greek merchants flourished. Adolf Hitler of Germany and Joseph Stalin in the Soviet Union were strong leaders, but they unleashed evil that retarded industrial growth in their countries.

There are two views about the power of leaders as a historical force. One is that leaders simply ride the wave of history. "Great men," writes Arnold Toynbee, "are precisely the points of intersection of great social forces."[35] When oil was discovered in western Pennsylvania in 1859, John D. Rockefeller was a young man living in nearby Cleveland, where he had accumulated a little money selling produce. He saw an opportunity in the new industry. His remarkable traits enabled him to domineer over a rising industry that reshaped the nation and the world. Yet is there any doubt that the reshaping would have occurred nonetheless had Rockefeller decided to stick with selling lettuce and carrots?

A differing view is that leaders themselves change history rather than being pushed by its tide. "The history of the world," wrote Thomas Carlyle, "is at bottom the History of the Great Men who have worked here."[36] It was John Jacob Astor of the American Fur Company who established a presence in the wild lands of the American continent, exploring them, knitting them together, and thwarting the efforts of other nations to occupy them. The United States map might today be different absent the effects of Astor's singular lust for fur riches. It was James B. Duke of the American Tobacco Company whose solitary marketing genius turned cigarette smoking from a local custom confined largely to the American South into a worldwide health disaster continuing now for more than a century.

Cases and stories in this text provide instances for debate about the role of business leaders in changing the world.

Chance

Scholars are reluctant to use the notion of chance, accident, or random occurrence as a category of analysis. Yet some changes in the business environment may be best explained as the product of unknown and unpredictable causes. No less perceptive a student of history than Niccolò Machiavelli observed that fortune determines about half the course of human events and human beings the other half. We cannot improve on this estimate, but we note it. Its significance is that managers must be prepared for the most unprecedented events and have faith in Machiavelli's counsel that when such episodes arrive those who are ready will prevail, as fortune "directs her bolts

[35] *A Study of History,* vol. XII, *Reconsiderations* (London: Oxford University Press, 1961), p. 125.

[36] In "The Hero as Divinity," reprinted in Carl Niemeyer, ed., *Thomas Carlyle on Heroes, Hero-Worship and the Heroic in History* (Lincoln: University of Nebraska Press, 1966), p. 1. This essay was originally written in 1840.

where there have been no defenses or bulwarks prepared against her."[37] No doubt Machiavelli would think Shell's scenarios are praiseworthy.

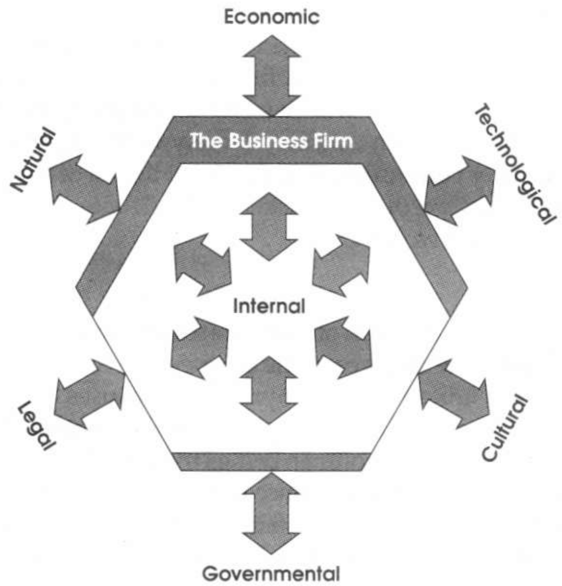
SEVEN KEY ENVIRONMENTS OF BUSINESS

Figure 2.5 shows the seven most important environments affecting business today. In each one powerful forces create change in the relationships between businesses, governments, and societies. These forces are often related and major changes in one area rarely occur in isolation. Here we give thumbnail sketches of each key environment. We will dig more deeply into them throughout the book.

The Economic Environment

The economic environment consists of forces that influence market operations, including overall economic activity, commodity prices, interest rates, currency fluctuations, wages, competitors' actions, technology change, and government policies. Continuing long-term growth in output, consumption, and investment characterizes the global economic environment. World GDP increased 310 percent in the years between 1982 and 2005, rising from \$10.9 trillion to \$44.7 trillion.[38] Growth briefly slowed in 2001 and 2002 because of economic repercussions from the September 11, 2001, terrorist attacks and the sudden acute respiratory syndrome epidemic in Asia. However, after a rough patch of several years the world economy picked up again, led by recovery in the United States and rapid expansion in China

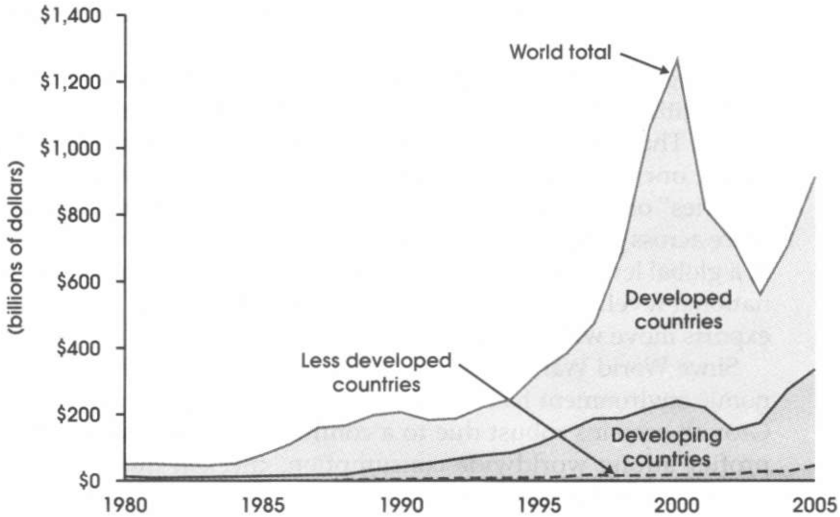
FIGURE 2.5
The Seven Key Environments of Business



[37] Niccolò Machiavelli, *The Prince,* trans. George Bull (New York: Penguin Books, 1961), chap. XXV, p. 73.
[38] United Nations Conference on Trade and Development, (UNCTAD) *World Investment Report 2006* (New York: United Nations, 2006), table I.2.

FIGURE 2.6 Worldwide FDI Inflows: 1980–2005

Source: United Nations Commission on Trade and Development, *World Investment Reports*, various editions, annex table B.1.



and India. Underlying this strong and continuing overall economic growth are two basic subtrends.

The first is rising trade. Three years after the end of World War II, in 1948, the global sum of all merchandise exported was $58 billion. In 2004 it was $10.2 trillion, an increase of 17,586 percent.[39] This spectacular rise has been enabled by a trading system created at the end of World War II. Nations within the system have been encouraged to lower tariffs and other trade barriers because other member nations promised to reciprocate this openness. The system has evolved into an institution called the World Trade Organization (WTO) that embodies an ongoing process of negotiation and *trade liberalization* in which 149 nations now participate. In addition, several hundred regional trade agreements promote freer exchange among countries that are parties to them.

trade liberalization A philosophy in which nations promote trade by easing restrictions, including both tariff and nontariff barriers. This philosophy, sometimes referred to as simply *liberalization*, is the bedrock of economic globalization.

foreign direct investment Capital investment by private firms outside their home countries.

The second subtrend underlying continued economic growth is a major expansion of foreign direct investment (FDI) by transnational corporations. *Foreign direct investment* is capital investment by private firms outside their home countries. Between 1982 and 2005, global FDI inflows (that is, corporate investments moving into foreign countries) rose from $59 billion a year to $916 billion, a 1,553 percent increase.[40] There are about 78,000 multinational corporations and, through FDI, they own or control about 778,000 foreign businesses. Many foreign affiliates are acquired by merger and acquisition and between 1997 and 2002 there was an unprecedented burst of cross-border merger activity both in the number of deals and in their dollar value.[41] Figure 2.6 shows the remarkable rise of FDI, the consequences of the post-2001 slowdown in the world economy and resumption of the

[39] World Trade Organization, *International Trade Statistics 2006* (Geneva: WTO, 2006), table II.2.

[40] UNCTAD, *World Investment Report 2006,* table I.2.

[41] For the six years of 1997 through 2002 there were 633 deals worth $2.4 trillion as compared to the previous six years, including 1991 through 1996, with 134 deals worth $290 billion, see UNCTAD, *World Investment Report 2003* (New York: United Nations, 2003), table I.7.

upward trend in 2003. It also reveals that most investment flows to and from developed nations.

Rising trade and consumer demand have rapidly expanded markets. To remain competitive, corporations have expanded with markets and restructured for efficiency. They invest to enter growing markets or to increase their power in established ones. Many multinational firms have restructured by creating "global factories" or "virtual corporations" in which production of goods or services takes place across geographically dispersed networks. These networks seek to duplicate at a global level the efficiencies of specialization and outsourcing often seen at the national level. They are now so extensive that nearly two-thirds of the world's exports move within them.

Since World War II, and especially since the early 1980s, the international economic environment has been favorable to growth and expansion of corporations. Growth remains robust due to a confluence of factors including high corporate profits, strong worldwide consumption, checked inflation, and low long-term interest rates. However, the International Monetary Fund (IMF) has warned that "surrounding the central scenario of robust growth, risks are weighted on the downside."[42] Years of expansion have created large trade imbalances for some nations, including the United States, and misalignment of currency exchange rates. Protectionist responses that raise trade barriers could limit future international economic integration and lead to stagnation. These are, warns the IMF, "the best of times but they are also the most dangerous of times."[43]

The Technological Environment

nanotechnology
Technology that is developed on the scale of a nanometer, which is one-billionth of a meter.

Today new scientific discoveries create a business environment filled with mind-boggling technology. For example, *nanotechnology* allows manipulation of objects the size of atoms. New materials and tiny machines invisible to the naked eye can be engineered at the molecular level. Semiconductor makers can now make microchips with components the size of one ten-millionth of a meter. When this ability is harnessed to practical manufacturing, it will create chips that operate on an atomic scale comparable to the photosynthesis process in plants. Users with such circuits could store all information in the Library of Congress in the space of a sugar cube.[44] Human genome mapping promises new biogenetic products that will cure intractable diseases. Fuel cells and methods of harnessing renewable energy may dramatically reduce use of fossil fuels.

wiki
A Web site open to collaborative editing by multiple individuals.

Digital telecommunications technology now creates a global network of computers, software, and electronic devices. This network has led to radical innovations such as open sourcing, which allows numbers of individuals to participate in the creation of complex knowledge products. *Wikis*, or Web sites open to collaborative editing by multiple or innumerable parties, have been used to create browsers, encyclopedias, dictionaries, and news sites.

[42] International Monetary Fund, *World Economic Outlook 2006: Globalization and Inflation* (Washington, DC: IMF, 2007), p. xii.

[43] Ibid., p. xii.

[44] Philip Bond, quoted in Ronald Bailey, "The Smaller the Better," *Reason*, December 2003, p. 47.

The wiki principle is an example of how an innovation can be both an opportunity and a threat. It releases an open, Darwinian process in which knowledge emerges from the common pool of humanity and survives the meticulous scrutiny of collective expertise rather than emanating from a single individual or small group to a passive audience. It promotes equality, but undermines hierarchical authority, and attacks old business models of software firms and publishers. In fact, novel technologies are minefields for established firms, which often focus on the immediate commercial possibilities of a technology and miss, or underestimate, its ultimate defiance of their existing business model. An example is Western Union, the dominant communications company of the nineteenth century, which was so confident in the telegraph that it rejected the telephone.

When Alexander Graham Bell invented the telephone in 1876, it had only a three-mile range. Western Union considered hooking telephones into its lines, but decided such a short-range device was just a toy. So Bell formed his own company. When engineers lengthened the range of the phone by using wires made of copper instead of iron, Western Union saw its mistake and rushed into the business with a phone device of its own. The mighty company used "every devious and underhanded method," including political pressure and bribes, to prevent towns and cities from adopting the Bell phone.[45] However, in 1878 it lost a patent infringement suit brought by Bell's company and had to drop the business.

The tiny Bell Telephone Company grew into AT&T, at one time in the twentieth century the world's largest corporation in revenues, a firm so creative that it gave birth to the transistor and the laser, so dominant that the U.S. government broke it up in 1984, so satisfied with success that it repeatedly failed to adapt. Stubbornly, it defined its business as providing voice conversation over wires, thus abiding with indifference as future competitors articulated new digital communication technologies such as wireless and cable networks, computers, and the Internet. Although AT&T is still a large corporation, it now scrambles through mergers and strategies, seeking a formula to restore past glory.

New technologies have unforeseen consequences for society when they are put in wide use for commercial gain. The cigarette-rolling machine was invented before the dangers of smoking were known. Manufacturing that mixed asbestos into hundreds of common materials came long before the morbid effects of asbestos fiber became clear. The World Wide Web is spreading into millions of lives before anyone has a full understanding of its implications for personal privacy. The lesson of the past is that corporations have an ethical duty to weigh carefully not only the strategic impact of technologies on their business models, but also the dangers they may impose on people.

The Cultural Environment

culture
A system of shared knowledge, values, norms, customs, and rituals acquired by social learning.

A *culture* is a system of shared knowledge, values, norms, customs, and rituals acquired by social learning. No universal culture exists, so the environment of a transnational corporation includes a variety of cultures, each with differing peoples, languages, religions, and values.

[45] Page Smith, *The Rise of Industrial America*, vol. 6 (New York: Penguin Books, 1984), p. 115.

On one level, this variation causes conflicts of business custom, and managers in foreign countries must absorb both subtle and striking differences in employee loyalty, group versus individual initiative, the place of women in organizations, ethical values, norms of giving and gratuities, attitudes toward authority, the meaning of time, and clothing worn in business settings. The consequences of cultural differences are often trivial, even humorous. Thus, a consulting firm that helps American managers avoid social blunders in foreign countries counsels them not to force the custom of name tags at business meetings on Europeans, who feel they are being treated as schoolchildren when wearing them.[46] However, consequences can be serious too. In France, the notion is widespread that American fast food causes obesity and, worst of all, is bad tasting and insults the refined French palate. President Jacques Chirac said that national ways of eating should be preserved in the face of an assault by cross-Atlantic invaders; and a minister of agriculture once said that the United States was "home to the world's worst food."[47] For McDonald's, these cultural feelings turned deadly. A mob wrecked one of its restaurants and another was bombed, killing an employee.

On a deeper level, although no uniform world culture exists, there is a fundamental divide between the culture of Western economic development and the rest of the world's cultural groupings. The culture of the advanced West promotes a core ideology of markets, individualism, and democratic government. It is sustained by Western nations that dominate international organizations, contain the most powerful corporations, and have the strongest militaries. However, although developing nations tend to adopt elements of Western culture, some nations and cultures have resisted its spread. Islamic nations and China see spreading Western values as a form of cultural aggression. They have resisted adopting them, particularly participatory forms of government.

Over the last half of the twentieth century, some cultural values in developed nations began to shift, creating changes in the global business environment. In these societies, beginning in the 1960s, traditional values based on historical realities of economic scarcity were transformed. In their place came what are called *postmodern values*, or values based on assumptions of affluence. For example, in older industrializing societies materialism was a dominant value. People sacrificed other values such as leisure time and environmental purity to make money and buy necessities, then luxuries. While consumption is still a powerful value in developed nations, their affluent citizens grow more concerned with quality of life and self-expression.

postmodern values Values based on assumptions of affluence, for example, quality of life and self-expression.

The World Values Surveys, a series of surveys in 75 countries now spanning 25 years, show that the rise of postmodern values has uniformly shifted the social, political, economic, and sexual norms of rich countries. Despite some resistence in non-Western cultures, surveys show the rise of these norms in all modernizing nations. Among the Chinese public, for example, there is "surprisingly high" support

[46] Lalita Khosia, "You Say Tomato," *Forbes*, May 21, 2001, p. 36.

[47] John-Thor Dahlburg, "To Many French, Ugly American Is McDonald's," *Los Angeles Times*, April 22, 2000, p. A10.

for values linked to democracy.[48] And support for democratic ideals in eleven Muslim societies has grown to equal that in Western societies.[49]

Postmodern norms are a strong influence in the operating environments of multinational corporations. To illustrate, there is a powerful global movement to promote fundamental human rights by stamping out racism, sexism, authoritarianism, intolerance, and xenophobia. This movement is energized by West-dominated coalitions of individuals, advocacy groups, governments, and international organizations such as the United Nations. Similar and interrelated movements have risen to promote sustainable development and humanitarian assistance to poor regions. This global tide of morality, based on the postmodern values of developed nations, elevates expectations about the behavior of multinational corporations. Increasingly, they must follow proliferating codes and rules developed by moral reformers and must define their basic purposes as promoting human welfare above narrow profit making.

The Government Environment

Governments have simultaneously stimulated and constrained business. In this regard, two long-term global trends in government are central.

First, government activity has greatly expanded. One way of measuring this is by comparing a government's spending with the size of its economy. Around the world, the percentage of this spending has risen, from single digits in 1900 to an average of 29 percent in 2002.[50] In the United States, in 1913, spending was 8 percent of GDP, but by 2005 it had risen to 35 percent.[51] The percentages have risen highest, up to 40 percent and more, in European welfare states and are lower in developing countries, but broadly the trend is up because governments have taken on new functions. For one, they promote social welfare with a range of transfer payments to their citizens. This role grew in the twentieth century as many nations expanded their electorates. New voters included women and the less privileged, groups that voted to enlarge government assistance programs. Another source of government growth is expanded regulation of industries to protect citizens from abuses. In the United States, for example, there is today practically no aspect of business that governments cannot and will not regulate if the occasion arises and popular support exists. New laws, added to past laws, result in more constraints on business.

The second long-term trend is rising democratization. In 1900 no nation was a full *democracy* with multiparty elections and universal suffrage. The United States and Britain were close, but both lacked female suffrage, and the United States additionally lacked black suffrage in practice. Yet by 1950 there were 22 democracies

democracy
A form of government requiring three elements—popular sovereignty, political liberty, and majority rule.

[48] Ronald Inglehart, "Globalization and Postmodern Values," *Washington Quarterly,* Winter 2000, p. 19.

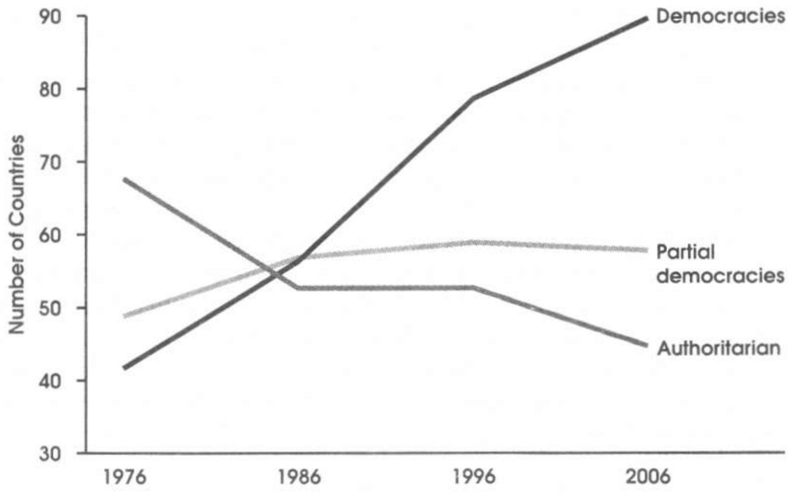
[49] Ronald Inglehart and Pippa Norris, "The True Clash of Civilizations," *Foreign Policy,* March/April 2003, pp. 64–66.

[50] United Nations Economic and Social Council, *Basic Data on Government Expenditure and Taxation* (New York: United Nations, 2004), table 3.

[51] International Monetary Fund, *World Economic Outlook 2000* (Washington, DC: IMF, May 2000), table 5.4; and Bureau of the Census, *Statistical Abstract of the United States, 2007,* 126th ed. (Washington, DC: Bureau of the Census, 2005), tables 419, 458, and 648.

FIGURE 2.7
The Rise of Democratic Regimes

Source: Freedom House. Data is based on combined measures for democracy and civil liberty.



and by 2006 there were 90.[52] Figure 2.7 shows the dramatic rise—from 91 to 148—in the number of democratic and partially democratic regimes since 1975. Much of this rise came in the late 1980s and early 1990s after the breakup of the Soviet Union. When repressive socialist regimes no longer received external support from the Soviet bloc and the United States reduced its support for authoritarian regimes that were anticommunist, a wave of democratization swept Southeast Asia, Latin America, and Africa.

However, a more fundamental cause of expanding democracy is the rise of postmodern values in countries that have undergone socioeconomic growth. These values undermine hierarchical authority and shape expectations for more political participation and autonomy. Authoritarian regimes are now largely confined to nations with lagging economies, where traditional values have not evolved into aspirations for liberty and choice. For business, the consequence of more openness to popular majorities is that governments increasingly respond to public demands for corporate social performance and these demands reflect postmodern values promoting human rights, the environment, aesthetics, and ethics.

The Legal Environment

The legal environment consists of legislation, regulation, and litigation. Five enduring trends in this environment work to constrain business behavior. First, laws and regulations have steadily grown in number and complexity. Second, legal duties to protect the rights of stakeholders, such as employees, consumers, and the public, have expanded. These rights derive from the steady flow of laws and court decisions on, for example, discrimination, sexual harassment, advertising,

[52] Figures are from *Democracy's Century: A Survey of Global Political Change in the 20th Century* (Washington, DC: Freedom House, 2001), p. 2 and Figure 2.7; and Freedom House, *Freedom in the World: 2007* (Washington, DC: Freedom House, 2007), p. 2.

antitrust, the environment, product liability, and intellectual property. Third, globalization has increased the complexity of the legal environment by exposing corporations to international law and laws of foreign nations. In addition, advocacy groups promoting human rights and environmental causes push corporations to adopt so-called *soft law,* or voluntarily adopted codes of conduct that set forth rules for corporate behavior based on emerging international standards of conduct. These rules often exceed requirements in specific laws of nations. Fourth, although the requirements of ethical behavior and corporate social responsibility go beyond legal duty, they are continuously plucked from the voluntary realm and encoded into law. For instance, saving money by firing a long-time employee the week before he or she qualified for a pension was always ignoble. In 1974 the Employee Retirement Income Security Act made it illegal as well.

soft law
Voluntarily adopted codes of conduct setting forth rules about corporate behavior. Guidelines are often derived from emerging international conduct standards.

Finally, the law is constantly evolving. Because of technological change, for example, corporations need to anticipate emerging causes of liability. In this respect, the old *T. J. Hooper* case is still good reading for corporate counsel. On a sunny day in March 1928 the tugboat *T. J. Hooper* hauled a coal barge out to sea. Two days later it hit stormy weather off New Jersey, and the barge sank with its load of coal. The owners of the cargo sued, claiming that the tug was unseaworthy because it had no receiving radio. Lacking a radio, the *T. J. Hooper* missed a weather broadcast that caused other ships to put into harbor before the gale hit. Although no law required a radio and there was no industry custom of installing them, the eminent judge Learned Hand held that "there are precautions so imperative that even their universal disregard will not excuse their omission."[53]

The tug owners were found negligent and paid for the coal cargo because they had not adopted a cutting-edge technology. Moving ahead to the present, a parallel example is the existence of electrically charged table saw blades that can detect contact with a human finger and stop rotation within thousandths of a second.[54] No law or industry standard now requires manufacturers to use this technology, but its availability opens employers who do not use them to charges of negligence by workers who cut off fingers and hands.

The Natural Environment

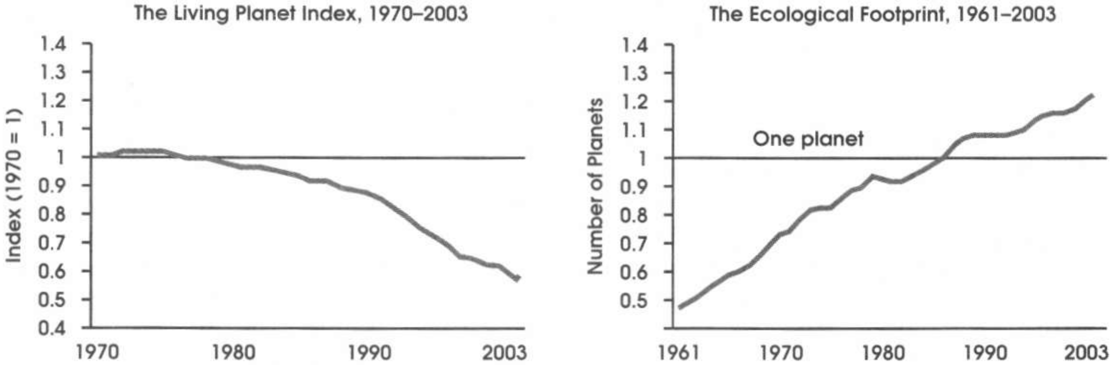
Economic activity is a geophysical force with power to change the natural environment. Just as it has strained the ability of human institutions to adapt, so also has it sometimes overwhelmed the ability of ecosystems to cleanse and regenerate. Spectacular economic growth in the twentieth century came at a high cost to the planet. It depleted mineral resources, reduced forest cover, killed species, released artificial molecules, unbalanced the nitrogen cycle, and altered the chemistry of the earth's atmosphere enough to trigger climate change.

Two measures used by the World Wildlife Fund exhibit global trends for the overall burden of human activity on nature. *The Living Planet Index,* shown in Figure 2.8, combines in one measure thousands of population trends among terrestrial, freshwater, and marine vertebrate species. It fell by about 30 percent between

[53] *In re The* T. J. Hooper *et al.*, 60 F.2d 737 (1932), at 740.

[54] Melba Newsome, "An Edgy New Idea," *Time Inside Business,* May 2006, p. A16.

FIGURE 2.8 Measures of Human Impact on Nature



Source: From *Living Planet Report 2006*, World Wildlife Fund, www.panda.org. Copyright © 2007 WWF. Some rights reserved.

1970 and 2003.[55] This decline of biodiversity reflects deteriorating conditions in the forests, grasslands, deserts, savannahs, and freshwater and marine ecosystems that provide habitat for the world's species. A second indicator, the *Ecological Footprint*, also shown in Figure 2.8, measures human consumption of renewable natural resources. It is calculated as the total land area, in hectares, required to maintain worldwide human consumption of food, wood fiber, energy, and water. In the figure, the vertical axis shows the number of planets required to support ecological footprints of varying size. The horizontal line crosses at one planet, marking the earth's current biological capacity to support life. The trend line shows that the human ecological footprint moved beyond the earth's carrying capacity in the late 1980s and is now unsustainable. The overall human footprint is calculated to be 14.1 billion hectares, whereas the planet's life-carrying capacity is estimated to be only 11.3 billion hectares.[56] The implication is that the extent of natural resource use encouraged by global capitalism is unsustainable.

Attitudes about the relationship of economic activity to nature are now rapidly changing. When the twentieth century began, dominating and consuming nature was justified by a variety of doctrines, not the least being capitalism, which values nature as a production input. At its end, thinking moved toward preservation of nature. Managers must adapt to this changed thinking. With growing frequency environmental criteria enter into judgments of their performance.

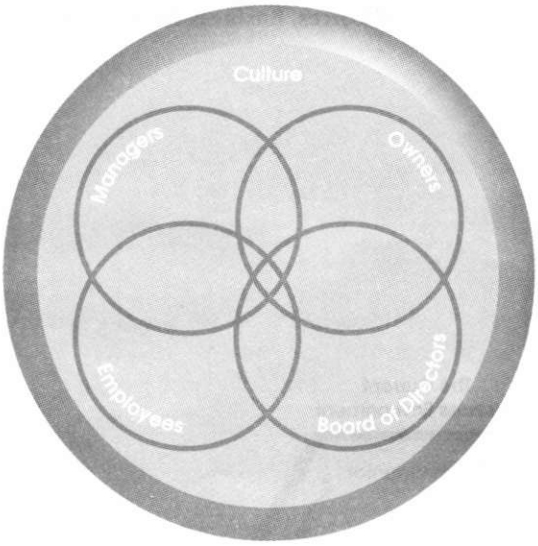
The Internal Environment

In a corporation, the internal environment consists of four groups, as shown in Figure 2.9. Each group has different objectives, beliefs, needs, and functions that managers must coordinate to achieve overall company goals. In this process, a corporate culture that transcends the values of any single internal group is created.

[55] World Wide Fund for Nature, *Living Planet Report 2006* (Gland, Switzerland: WWF International, 2006), pp. 2–3.

[56] A hectare is an area of 10,000 square meters, equivalent to 2.47 acres.

FIGURE 2.9
A Depiction of the Internal Business Environment



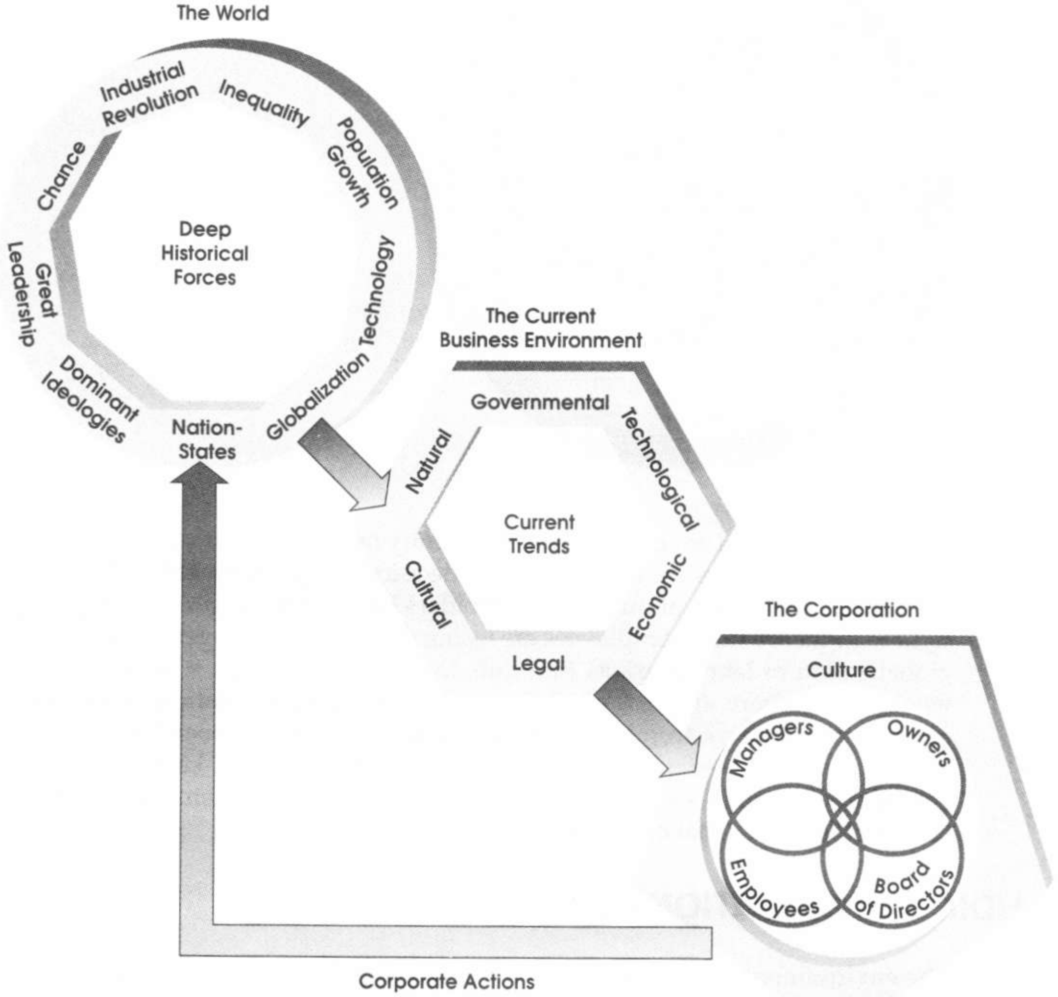
Forces in external environments have recently reduced the power of these internal groups. Managers are limited in their decisions by government and forced to accommodate a range of outside stakeholders having the power or claiming the right to influence them. Employees are losing power over management because of globalization of labor markets that puts them in competition with lower-wage workers elsewhere. In the United States, new financial regulations designed to protect shareholders from dishonest managers have given boards of directors more power and greater independence from top management. However, there is also some erosion of shareholder power by external groups demanding socially responsible actions that conflict with profit maximization.

CONCLUDING OBSERVATIONS

The environments of business have profound implications for managers. Figure 2.10 summarizes the chapter discussion by illustrating the dynamic interconnection of business with historical forces and current environments. The deep historical forces act to shape the seven key environments, while the actions of business constantly influence not only current environments but, in addition, the deeper course of history. As the arrow running from the corporation to the world in Figure 2.10 indicates, business is not simply a passive entity that moves with historical and environmental forces like a billiard ball reacting to impacts. On the contrary, although strongly constrained by its environment, business has a powerful capacity to shape society and change history in ways small and large.

For example, when Eastman Kodak wanted to display the speed of its fast film and Flashmatic shutter in 1940, it ran magazine ads showing pictures of "Kodak Moments" when people blew out candles on their birthday cakes. The ads so

FIGURE 2.10 **The Dynamic Interaction of Historical Forces, Business Environments, and Corporate Actions**



popularized this charming rite that it became universal among Americans.[57] In contrast to such a small cultural change, the story of the automobile illustrates how industries can rearrange whole societies. Perhaps no twentieth century industry created more intentional and unintentional change. It was a prime mover of the American economy and once accounted directly or indirectly for one of every eight jobs. It encouraged an expansive highway system, brought decline to the railroads, depleted oil reserves, created pollution, altered cities, entrenched the idea that status was conferred by ownership of material objects, and changed patterns of courtship and crime.

[57]James B. Twitchell, *Lead Us Not into Temptation* (New York: Columbia University Press, 1999), p. 26.

The American Fur Company

The American Fur Company was a relentless monopoly built in the climactic era of the fur trade. It was created in 1808 by John Jacob Astor, a striving German immigrant, in an environment so favorable that over vast North American territories it had more power than the fledgling American government. In its time, this company shaped the destiny of a young nation. It made Astor the richest American of his day. Yet by the 1830s its situation had so changed that it and the 300-year-old trade in furs collapsed.

ASTOR ARRIVES IN A YOUNG NATION

In 1763 Astor was born to a butcher and his wife in the German village of Waldorf. Young John Jacob found village life dull, so at the age of 15 he left for London, working four years there to save money for an ocean voyage to the New World. In 1783, at the age of 20, with no education, little money, and speaking poor English, he set sail on a merchant ship. During the long voyage, a fur trader taught him how to appraise and handle skins. These lessons gave Astor knowledge he needed for an occupation. He would soon show himself an apt student.

At this time, the fur trade on the North American continent was almost 300 years old. It had begun early in the sixteenth century after Spanish and French explorers made contact with native forest dwellers, and it soon included the British. The Europeans wanted beaver, martin, ermine, mink, otter, bear, deer, muskrat, wolf, racoon, and other animal skins for fashionable hats and clothing. The Native Americans, who had not yet entered the age of metal, were anxious to get even the simplest manufactured goods such as knives, mirrors, ornaments, and buttons. This simple mutual advantage proved durable over time.

Indians were the fur industry's production workers. Fur traders depended on them to trap animals, then negotiated with them to buy pelts in exchange for trinkets. Indian women skinned and prepared the hides. Overhead costs for traders were low. Instead of wages, Indians took trade goods worth a fraction of a fur's ultimate value. Since furs were light, they could be transported economically by mules, barges, and ships to eastern ports and thence to Europe. Profits were enormous.

Fur trading had transforming effects on society because it promoted settlement. Traders worked on the edges of Euro-American habitation. Over time, fur production in these frontier areas always declined. Populations of fur-bearing animals such as beaver, having slow breeding cycles, were steadily depleted. The reliability of Indian trappers fell as their tribal cultures buckled under the strains of new values and diseases. When productivity in an area declined, fur traders pushed over the horizon. In their wake came settlers using fresh maps and trails. Farms and towns sprouted. Indians were killed or dislodged. This unsentimental cycle of the fur trade, repeated over and over, generated waves of migration that settled much of the United States.

ASTOR ENTERS THE FUR BUSINESS

Astor made his way to New York where he got a job selling bakery goods. He invested most of his $2-a-week pay in small trinkets and in his spare time prowled the waterfront for Indians who might have a fur to trade. Within a year he picked up enough skins to take a ship back to London, where he established connections with fur-trading houses. This was a phenomenal achievement for an immigrant lad of 21 who had been nearly penniless on his arrival in America, and it revealed Astor's deadly serious and hard-driving personality.

Astor worked briefly with a fur dealer in New York City during which time he trekked into the forests of upstate New York to bargain for furs. He soon left his employer and by 1787 was working solely for himself. He demonstrated sharp negotiating skills in trading trinkets for furs and soon built up an impressive business. One neighbor said:

> Many times I have seen John Jacob Astor with his coat off, unpacking in a vacant yard near my residence a lot of furs he had bought dog-cheap off the Indians and beating them out, cleaning them and repacking them in

more elegant and salable form to be transported to England and Germany, where they would yield him 1,000 percent on the original costs.[1]

Astor made great profits and expanded his business but, like other Americans, he was blocked from harvesting furs in the forests of the Northwest Territory. The Northwest Territory was the huge unsettled area between the Ohio River and the Mississippi River bounded on the north by the Great Lakes. After the Revolutionary War, Great Britain ceded this area to the United States but continued to maintain forts and troops there because the American government was too weak to enforce its rights. British fur-trading companies exploited the area and incited Indians to attack American traders and settlers who dared enter.

This audacity pushed Congress near to declaring war. To avoid hostilities, England agreed to a treaty in 1794[2] that required removal of British troops and gave both British and Americans trading rights in the Northwest Territory. "Now," said Astor on hearing this news, "I will make my fortune in the fur trade."[3] But he was stunned when President George Washington proposed befriending the Indians by setting up government fur-trading posts to be run with benevolent policies. These posts would compete with Astor and other private traders. Congress approved the plan, which required that trade goods be sold at cost, prohibited the use of liquor, and ordered payment of fair prices for furs.

The government trading posts infuriated Astor, who moved quickly to undercut them. He saturated the territory with his agents, instructing them to buy every fur they could get their hands on before competitors did. He bought trade goods in huge quantities to lower the cost, and his agents paid for furs with these trinkets. And he allowed liquor to flow freely during trade negotiations, creating an advantage the government could not match.

Astor had great success with these tactics. The government lacked his nimbleness and commitment, and he outwitted other rivals. In less than 10 years he was the second-richest man in America (after only Stephen Girard, the shipping magnate and banker). Having accumulated deep resources, the Astor juggernaut turned toward the West.

THE LOUISIANA PURCHASE

In 1803 the territory of the United States more than doubled with the Louisiana Purchase. President Thomas Jefferson agreed to purchase from France for $15 million approximately 800,000 square miles of land between the Mississippi River and the Rocky Mountains and running north from New Orleans to the forty-ninth parallel, which is now the Canada–U.S. boundary. At the time, little was known about the area called the Louisiana Territory. No accurate or complete maps existed; even its exact boundaries were vague. But Louisiana was beautiful in its mystery.

Some geographers thought it was largely an arid desert. Others predicted a lush, fertile land. Rumors of geological wonders, horrific animals, and strange natives circulated, including the story of a tribe of bow-hunting, man-hating female savages in which the archers had their right breasts removed to keep them from interfering with the bowstrings.[4]

Jefferson himself had a clear vision of how to use the new territory. In his 1803 message to Congress, he proposed to relocate into Louisiana eastern tribes getting in the way of American settlers, and over the next 50 years this occurred many times.[5] He also ordered an Expedition of Discovery headed by Meriwether Lewis and William Clark to explore on foot the unknown territory.

A primary purpose of the Lewis and Clark expedition was to determine the suitability of Louisiana for the fur trade. The adventurers set out on a round-trip march between St. Louis and the Pacific Ocean, going where no white American had gone before, and on their return in 1806 reported a wondrous land "richer in beaver and otter than any country on earth."[6] They also reported that most Indian tribes in

[1] A "Gentleman of Schenectady," quoted in John Upton Terrell, *Furs by Astor* (New York: Morrow, 1963), p. 55.

[2] The treaty was negotiated for the United States by John Jay and is known as Jay's Treaty.

[3] Terrell, *Furs by Astor,* p. 93.

[4] Ben Gilbert, *The Trailblazers* (New York: Time-Life Books, 1973), p. 18.

[5] For a list of 24 relocations, see Cardinal Goodwin, *The Trans-Mississippi West (1803–1853)* (New York: Appleton, 1922), plate following p. 88.

[6] Quoted in David J. Wishart, *The Fur Trade of the American West (1807–1840): A Geographical Synthesis* (Lincoln: University of Nebraska Press, 1979), p. 19, citing the original journals of the trip.

the territory were friendly to Americans and the fur trade. These discoveries were not lost on fur traders, among them John Jacob Astor.

THE AMERICAN FUR COMPANY IS BORN

The Lewis and Clark expedition was a catalyst for fur trading in the new territory. Beaver production in the Northwest Territory was already beginning to fall off. The North West Company, Astor's main competitor, began to move down from Canada, intent on harvesting the Louisiana Territory as rapidly as possible.

However, it would reckon with Astor, who wanted the prize himself. In his distant New York City study, Astor pored over maps of the fur-rich areas discovered by Lewis and Clark, hatching a vast and daring plan for a new company that would string trading posts over a 2,000-mile route.

In those days, state legislatures had exclusive power to create a company by issuing a charter that listed the conditions of its existence. So he approached the governor and legislature of New York seeking to charter a company to be known as the American Fur Company.

To sell the idea, he cloaked his mercenary scheme with a veil of patriotism. He argued that most of the furs taken from the Louisiana territory went to Canadians and British, thereby depriving America of trade revenue. His new company would drive the foreigners out. He would join with 10 or 12 other wealthy entrepreneurs to capitalize the new company, which would then issue stock to others. The new company would enhance U.S. security by establishing a strong presence of American citizens over unpopulated areas. And finally, Astor promised that his company would deal honestly with the Indians and drive out smaller, irresponsible traders. The legislators of New York, responding more to Astor's open pocketbook than to the credibility of his arguments, passed a charter setting up the American Fur Company. Soon President Jefferson wrote a letter to Astor giving his blessing to the new company also.

Astor proceeded to take on four partners and establish a board of directors as the charter required. However, he retained 99.9 percent of the stock, elected himself president, and subsequently declared dividends whenever he wanted to compensate himself. The partnership was a fiction; Astor never intended to share either the proceeds of the company or any portion of the fur trade that he could control.

In 1810 he made his first move. His ship, the *Tonquin*, sailed to the mouth of the Columbia River on the Pacific Coast and set up a trading post named Astoria. At this time, Britain and the United States contested the wild area known as Oregon territory, consisting of present-day Oregon and Washington. Astor got diplomatic support for his trading post by arguing that its presence established an American claim to the territory. Secretly, however, he hoped to form a new nation called Astoria and make himself king.

Meanwhile, he would make Astoria one end of a vise that would squeeze competitors out of the new fur areas. Furs taken in the west would come to Astoria and then be shipped to China, which was a major fur market, or to New York. By this time, Astor owned a fleet of ships with which to do this. The other end of the vise would be St. Louis. Furs from Astor's planned string of trading posts on the eastern slopes of the Rocky Mountains would come down the Missouri River system to St. Louis and from there go overland to New York or on to the port of New Orleans to be shipped to Europe. It was a megalomaniac scheme, and no one but Astor had both the nerve and the resources even to attempt it. But it was too grandiose. Only part of it was to work, and the rest worked only until the fur trade fell apart.

THE ROAD TO MONOPOLY

In 1813 Astor's plan suffered a great reversal when he was forced to sell Astoria to the British during the War of 1812. He sold out at a fraction of its value because British soldiers were in a position to seize it as a war prize. Without Astoria as a foothold in the Oregon territory, he was unable to compete with British and Canadian fur companies. And 61 of Astor's employees died pursuing the settlement, along with hundreds of natives they came in conflict with.[7] Unbowed, Astor later commissioned Washington Irving, the best-selling author of the day, to write a book about the intrepid adventurers and himself as the great mind behind them.[8]

[7] Axel Madsen, *John Jacob Astor: America's First Multimillionaire* (New York: Wiley, 2001), p. 163.

[8] *Astoria; or, Enterprise beyond the Rocky Mountains* (New York: The Century Co., 1909); originally published in 1839.

Despite the loss of Astoria, Astor nonetheless predominated. In 1816 his lobbying succeeded in getting Congress to pass a law forbidding foreigners from trading furs in U.S. territories. This prevented Canadian and British companies from operating in the Northwest Territory, and Astor immediately bought out their interests, giving him a monopoly in furs east of the Missouri River. Blocked from the Pacific Coast trade by the British presence, he turned his attention to the upper-Missouri fur trade.

Astor bided his time as other fur companies pioneered trading in the northern Great Plains and then, after discovery of rich valleys of beaver, in the Rocky Mountains. By 1822 Astor had established a presence selling trade goods and buying furs in St. Louis, but he waited as other companies sent expensive expeditions of traders and mountain men up the Missouri, absorbing heavy losses of men and money. Despite losses, these pioneering companies found tremendous reserves of beaver in Rocky Mountain valleys, mapped new routes, and discovered advantageous locations for trading posts.

Then he crushed the competition. In 1826 he merged with Bernard Pratte & Company, an established firm, using it as an agent. He bought out and liquidated another competitor, Stone, Bostwick & Company. In 1827 he broke the Columbia Fur Company by building his own trading posts next to every one of theirs, engaging in cutthroat price competition for furs, and plying Indians liberally with whiskey. His trappers shadowed its trapping parties to learn where the beaver were, then muscled in. Using similar tactics, he bankrupted Menard & Valle. Now, according to Astor's biographer Terrell:

> Competition on the Missouri River was all but nonexistent. What remained was inconsequential, and might have been likened to a terrier yapping at a bear. The bear lumbered on, ignoring the noise until it became aggravating. Then with the sudden swipe of a paw, the yapping was forever stilled.[9]

Astor made astonishing profits. He would buy, for example, a 10-pound keg of gunpowder for $2, or 20 cents a pound, in London and transport it to his trading posts using his ships. He paid himself a 2 percent

Portrait of John Jacob Astor. Source: © Stock Montage/ Getty Image.

commission for buying the trade goods, or $.04 cents on the keg of gunpowder. He paid himself a freight charge for carrying the gunpowder on his ship to New Orleans. From there the keg was transported up the Missouri using the inexpensive labor of his hired trappers and traders. The gunpowder was valued at $4 a pound to the Indians, who were not allowed to pay money for it but got it only by exchanging furs or on credit. In the 1820s Astor charged one 2-pound beaver skin for each pound of gunpowder, getting 10 skins weighing 20 pounds for the keg of gunpowder. These skins were transported back to London, where they were worth $7 a pound or $140. From the $140 Astor deducted a 5 percent commission, or $7, for brokering the sale of the furs. Astor also subtracted 25 percent, or $35 from the $140, for the estimated costs of transportation and wages.

All told, this left a net profit for the American Fur Company of $97.96, or 4,900 percent on the original $2 investment.[10] And Astor owned over 99 percent of the company's shares. This profitable arithmetic was repeated on a wide range of trade goods.

The value of trade goods lay not in their utility, but in Indian beliefs. Indians coveted them so much

[9] Terrell, *Furs by Astor,* p. 391.

[10] These calculations are based on figures in ibid., pp. 397–98.

that they considered whites foolish to exchange even the smallest trinkets for beaver skins that were abundant in the forests. The idea of material acquisition beyond basic needs was foreign to Indian cultures. The Arikaras, for example, believed that a person who had more possessions than needed to survive ought to give the excess to others. Offering money to Indians did not motivate them to trap and process furs; they were indifferent to accumulating currency.

Trade goods such as rifles, knives, clothing, blankets, beads, and trinkets were useful, making them attractive to the Indians, but native-made equivalents were often just as good. Trade goods, however, had mystical significance beyond their utility or monetary value. Their allure lay in magical, spiritual qualities. Indians believed that the future could be seen by looking in a reflection of the self. Because manufactured mirrors gave a clearer reflection than water they were a wondrous advance in prophecy. They thought guns had supernatural properties, because they created thunder, an event associated with the spiritual world. They thought pots and kettles were alive, because they rang or sang out when hit. Thus, Indians found supernatural qualities in trade goods that were lost on Europeans.[11]

Astor encouraged Indians to take trade goods on credit. As a result, some tribes—the Winnebagos, Sacs, Foxes, Cherokees, Chickasaws, and Sioux—were hopelessly mired in debt, owing the American Fur Company as much as $50,000 each. Since trinkets had sky-high markups, Astor could not lose much even if tribal debts grew, but indebtedness forced tribes to trade furs with him rather than with competitors.

His traders and trappers fared no better. He marked up trade goods heavily before selling them to traders. Often, traders were in debt to Astor or had mortgaged their trading posts to him and were forced to mark up goods heavily themselves before selling them to Indians and trappers.

Trappers employed by the American Fur Company were ruthlessly exploited. They worked unlimited hours in hazardous conditions and extreme weather, but when Astor achieved dominance in an area, he cut their salaries from $100 a year to $250 every three years. They had to buy trade goods and staples at markups that were higher than those charged Indians to get furs. Whiskey costing $.30 a gallon in St. Louis was diluted with water and sold to them at $3 a pint. Coffee and sugar costing $.10 a pound was sold for $2 at trading posts up the Missouri. Clothing was marked up 300 to 400 percent.

Astor had contrived a lucrative, pitiless system that amplified his fortune by diminishing those caught in its workings. Though never venturing out West, he was in touch, working long hours, his shrewd mind obsessed with the most minor details and with squeezing out the smallest unnecessary expenses. In 1831 his son William estimated American Fur Company revenues of "not less than $500,000" yearly.[12] Astor was by now the richest man in America. He began to buy real estate in and around New York City.

ASTOR RACES ON

In the early 1830s it seemed nothing could slow Astor. Men who hated the American Fur Company started competing firms, but few lasted. Astor destroyed them by underbidding for furs and debauching the Indians with alcohol.

In 1832 Congress prohibited bringing alcohol into Indian territories, but the law was mostly ignored. Astor never favored using alcohol. It raised costs. However, many competitors saw inebriation as their only hope of seducing Indians with furs away from him. Astor, obsessed with defeating his rivals, let the spirits flow despite sad consequences.

Alcohol was unknown in native cultures; Indians developed a craving for it only after European traders introduced intoxication into fur price negotiations. Some thought that spirits occupied their bodies when they drank. Among Indians who took to whiskey, a new desire was created, a desire that motivated them to produce furs. A few tribes, notably the Pawnee, Crow, and Arikara, never imbibed. Most did, however, and some were so debilitated that their fur production fell and traders moved on.

Astor smuggled liquor as needed past Indian agents. He ordered construction of a still at the confluence of the Yellowstone and Missouri rivers, producing enough spirits to keep tribes in several states in a constant drunken state. Congress could not enforce its will because the federal government had almost no presence

[11] Richard White, "Expansion and Exodus," in Betty Ballantine and Ian Ballantine, eds., *The Native Americans: An Illustrated History* (Atlanta: Turner, 1993), chap. 14.

[12] Gustavus Myers, *History of the Great American Fortunes* (New York: Modern Library, 1936), p. 102; originally published in 1909.

in vast areas of the West. Statutes were meaningless where no authorities stood to enforce them. In Indian country, the only law was the will of leaders of trading companies and brigades of trappers who wore self-designed, military-style uniforms and could rob, cheat, and murder both Indians and whites with impunity. An 1831 report to Lewis Cass, Secretary of War, stated:

> The traders that occupy the largest and most important space in the Indian country are the agents and engagees of the American Fur Trade Company. They entertain, as I know to be the fact, no sort of respect for our citizens, agents, officers of the Government, or its laws or general policy.[13]

Government officials such as Cass were disinclined to thwart Astor in any case since they were frequently in his pay. Cass, who was the federal official in charge of enforcing the prohibition law, was paid $35,000 by the American Fur Company between 1817 and 1834.[14] At one time, Astor even advanced a personal loan of $5,000 to President James Monroe. Over the years, the Astor lobby achieved most of its objectives in Washington, DC, and state capitals, including heavy tariffs on imported furs and abolition of the government fur-trading posts so beloved to Washington and Jefferson. Under these circumstances, it is not surprising that the government failed to regulate the fur trade.

In 1831 Astor introduced a new technological innovation, the steamboat *Yellowstone,* which could travel 50 to 100 miles a day up the Missouri, transporting supplies to his posts. Keelboats used by competitors made only twenty miles upriver on a good day and exposed men pulling them with ropes from the bank to hostile Indian fire. Upriver Indians were awestruck by the *Yellowstone* and traveled hundreds of miles to see the spirit that walked on water. Some tribes refused to trade with the Hudson Bay Company any longer, believing that because of the *Yellowstone* it could no longer compete with the American Fur Company.

THE ENVIRONMENT OF THE FUR TRADE CHANGES

Although the American Fur Company was ascendant, unfavorable trends were building that would bring it down. Demand for beaver was falling as the fashion trends that made every European and American gentleman want a beaver hat waned. Silk hats became the new rage. Also, new ways of felting hats without using fibrous underhair from beaver pelts had developed, and nutria pelts from South America were entering the market.

These were not the only problems. In 1832 trade came to a near standstill during a worldwide cholera epidemic because many people thought the disease was spread on transported furs. Beaver populations were depleted by overtrapping. The fur companies made no conservation efforts; the incentive was rather to trap all beaver in an area, leaving none for competitors. In the 1820s the Hudson Bay Company tried to prevent Astor from moving into Oregon territory by exterminating beaver along a band of terrain to create a "fur desert" that would be unprofitable for Astor's trappers to cross.

Losses of human life rose as mountain men entered the shrinking areas where beaver were still abundant, leaving behind somewhat friendly Indians such as the Snake and Crow to encounter more hostile tribes such as the Blackfeet, who poisoned their arrows with rattlesnake venom and conducted open war against trappers.[15] One study of 446 mountain men actively trapping between 1805 and 1845 found that 182, or 41 percent, were killed in the occupation.[16]

Astor knew that the fur industry was doomed. Beaver pelts that had fetched $6 a pound in 1830 brought only $3.50 a pound by 1833. In that year he liquidated all his fur-trading interests. He spent the rest of his life accumulating more money in New York real estate. For a time, the American Fur Company carried on under new owners, but the industry environment continued to worsen. In 1837 the firm's steamboat *St. Peters* carried smallpox up the Missouri, killing more than 17,000 natives, and an agent observed that "our most profitable Indians have died."[17] By 1840 the firm had withdrawn from the Rocky Mountains and focused on buffalo robes, which remained profitable for some time.

[13] Report of Andrew S. Hughes, quoted in ibid., p. 99.

[14] Myers, *History of the Great American Fortunes,* p. 103.

[15] Trappers also attacked Blackfeet without provocation. See Osborne Russell, *Journal of a Trapper* (Lincoln: University of Nebraska Press, 1955), pp. 52, 86.

[16] William H. Goetzmann, "The Mountain Man as Jacksonian Man," *American Quarterly,* Fall 1963, p. 409.

[17] Jacob Halsey, a clerk at Fort Pierre, quoted in Wishart, *The Fur Trade of the American West,* p. 68.

ASTOR'S LAST YEARS

Astor lived on in New York, wringing immense profits from rents and leases as the city grew around his real estate holdings. By 1847 he had built a fortune of $20 million that towered above any other of that day. In 1998 this sum was estimated to be the equivalent of $78 billion, at the time more than the wealth of Microsoft's Bill Gates.[18] In his last years he was weak and frail and exercised by having attendants toss him up and down in a blanket. Yet despite his physical deterioration, he remained focused on getting every last penny from his tenants, poring over the rents for long hours behind the barred windows of his office.

Astor gave little to charity, and social critics attacked him for his stinginess. When he died in 1848, his major gift to society was $460,000 in his will for building an Astor Library. In addition, he left $50,000 to the town of Waldorf, Germany, his birthplace; $30,000 for the German Society of New York; and $30,000 to the Home for Aged Ladies in New York City. This totaled, in the words of one commentator, less than "the proceeds of one year's pillage of the Indians."[19] The rest of his wealth went to his heirs. As to how America felt about him, one obituary minced no words.

> No doubt he had many fine, noble qualities, but avarice seemed to hold an all-conquering sway. . . . [W]hat a vast amount of good he might have rendered the world! But how reverse is the case—he dies and no one mourns! His soul was eaten up with avarice. Charity and benevolence found not a congenial home in his cold and frigid bosom![20]

THE LEGACY OF THE FUR TRADE

For 300 years the fur trade shaped the economic, political, and cultural life of both native and European inhabitants of the raw North American continent. Its climactic era has often been depicted as a progressive and romantic period when trading posts represented "civilization which was slowly mastering the opposition of nature and barbarism."[21] According to historian Dan Elbert Clark:

> The fur traders, with all their faults and shortcomings, were the pathfinders of civilization. They marked the trails that were followed by settlers. They built trading posts where later appeared thriving towns and cities. They knew the Indians better than any other class of white men who came among them.[22]

The American Fur Company and its competitors greatly advanced geographical knowledge and blazed trails. The fur industry reinforced central American values such as rugged individualism, the frontier spirit, and optimism about the inevitability of progress. Yet there is also a dark side to the story. Traders undermined Indian cultures by introducing new economic motivations. Tribal societies were destroyed by alcohol, smallpox, and venereal disease. "The fur trade," according to Professor David J. Wishart of the University of Nebraska, "was the vanguard of a massive wave of Euro-American colonisation which brought into contact two sets of cultures with disparate and irreconcilable ways of life."[23]

The industry also left extensive ecological damage in its wake. It slaughtered animal populations and denuded riverside forest areas to get steamboat fuel. Astor's mentality of pillage set a destructive standard. Argues Wishart: "The attitude of rapacious, short-term exploitation which was imprinted during the fur trade persisted after 1840 as the focus shifted from furs to minerals, timber, land, and water."[24]

The American Fur Company, now largely forgotten, was the main actor in a global industry with enormous geopolitical power. The firm's operation was like a test-tube experiment on the social consequences of raw, unrestrained capitalism. It would be many years before the American nation gave thought to the lessons.

[18] This is the estimate of Michael Klepper and Robert Gunther in "The American Heritage 40," *American Heritage*, October 1998, p. 56.

[19] Myers, *History of the Great American Fortunes*, p. 149.

[20] "John Jacob Astor," *Appleton's Journal of Literature, Science and Art*, June 1, 1848, p. 116.

[21] Arthur D. Howden Smith, *John Jacob Astor: Landlord of New York* (Philadelphia: Lippincott, 1929), p. 131.

[22] Dan Elbert Clark, *The West in American History* (New York: Thomas Y. Crowell, 1937), p. 441.

[23] Wishart, *The Fur Trade of the American West*, p. 215.

[24] Ibid., p. 212.

Questions

1. How would you evaluate Astor in terms of his motive, his managerial ability, and his ethics? What lesson does his career teach about the relationship between virtue and success?
2. How did the environment of the American Fur Company change in the 1830s? What deep historical forces are implicated in these changes?
3. What were the impacts of the fur trade on society in major dimensions of the business environment, that is, economic, cultural, technological, natural, governmental, legal, and internal?
4. Who were the most important stakeholders of the nineteenth-century fur industry? Were they treated responsibly by the standards of the day? By the standards of today?
5. On balance, is the legacy of the American Fur Company and of the fur trade itself a positive legacy? Or is the impact predominantly negative?
6. Does the story of the American Fur Company hint at how and why capitalism has changed and has been changed over the years?
7. Do one or more models of the business–government–society relationship discussed in Chapter 1 apply to the historical era set forth in this case? Which model or models have explanatory power and why?

Chapter Three

Business Power

James B. Duke and the American Tobacco Company

On December 23, 1856, cries of new life swelled from a North Carolina farmhouse, their source a baby boy named James Buchanan Duke. The lad would have far more impact on the world than the failed president his name was intended to honor.

Soon, the Civil War displaced the Duke family from its land. On returning home in 1865 little James's father built a small factory to manufacture a brand of chewing tobacco named Pro Bono Publico (a Latin phrase meaning "for the public good"). James helped. He was a precocious, energetic boy who became the driving force behind the business.

By his late teens, James had visions of grandeur for the little factory. But the presence of a rival firm, the Bull Durham Co., thwarted them. Its chewing tobacco was so dominant that head-on competition was hopeless. Taking a major gamble, he committed the company to a then-novel product—the cigarette. This was a venturesome move, because at the time few people smoked them. Most tobacco users were rural men who associated cigarettes with degenerate dudes and dandies in big cities.

Nonetheless, in 1881 Duke brought 10 Russian immigrant cigarette rollers to his North Carolina factory and set them to work. Each made about 2,000 per day. At first there was no demand. Tobacco shops refused to order his Duke of Durham brand since customers never asked for them. But Duke was a merchandising genius. In Atlanta, he took out a full-page newspaper ad of a famous actress holding Duke cigarettes in her outstretched hand. This use of a woman to advertise cigarettes created a sensation and, along with it, demand. In St. Louis, Duke confronted extreme prejudice against cigarettes. Tobacco shop proprietors simply would not place orders. He had his agents hire a young, redheaded widow to call on the tobacconists, and she got 19 orders on her first day.

By this time a Virginia engineer, James Bonsack, had invented a machine capable of rolling 200 cigarettes per minute. He offered it first to the largest tobacco companies, but they turned him down, believing that smokers would reject newfangled, machine-rolled cigarettes. Duke saw the significance of the technology and jumped at it.[1] In 1883 he negotiated an exclusive agreement to operate the device and his competitors

[1] Patrick G. Porter, "Origins of the American Tobacco Company," *Business History Review*, Spring 1969, pp. 68–69.

Duke lured men to try his new cigarette brands by putting picture cards in packs. The first cards were stage actresses in poses that were provocative for that day. Later card series included Indian chiefs, perilous occupations, ocean and river steamers, coins, musical instruments, flags, fish, ships, and prize fighters. Source: Courtesy Emergence of Advertising in America, Special Collections Library, Duke University.

never recovered. With the new Bonsack machines, Duke simultaneously cut manufacturing costs from $.80 per thousand to $.30 and multiplied factory production by many times. [2]

To find new markets for this swollen output, Duke next went to New York City, where he rented a loft and set up a small cigarette factory. Then he moved to create demand. He was tireless, working twelve hours a day in the factory, then making the rounds of tobacco shops at night. He gave secret rebates and cash payments to friendly dealers. He hired people to visit tobacco shops and demand his new machine-rolled Cameo and Cross Cut brands. Immigrants were welcomed with free samples as they emerged from the New York Immigration Station to set foot in America for the first time. Ingeniously, he put numbered cards with glamour photos of actresses in his cigarette packs, encouraging men to complete a collection. Late at night he haunted the streets, picking up crumpled cigarette packs from sidewalks and trash cans, creating a crude sales count.

Overseas, Duke's minions were also at work. One great conquest was China. At the time a few Chinese, mostly older men, smoked a bitter native tobacco in pipes. Cigarettes were unknown. Duke sent experts to Shantung Province with bright leaf

[2] John K. Winkler, *Tobacco Tycoon: The Story of James Buchanan Duke* (New York: Random House, 1942), p. 56.

from North Carolina to cultivate a milder tobacco. His sales force hired "teachers" to walk village streets showing curious Chinese how to light and hold cigarettes. He installed Bonsak machines in four new manufacturing plants that soon ran 24 hours a day. And he unleashed on the Chinese a full range of promotional activities. At one time his cigarette packs contained pictures of seminude American actresses, which were a big hit with Chinese men. In this way, Duke turned China into a nation of smokers.

Back home his tactics wore down competitors. He carefully observed John D. Rockefeller's conquest of the oil industry and saw that Rockefeller's methods could be applied to the tobacco industry. In 1884, at the age of 26, he engineered a combination of his firm and other large firms into a holding company known as the American Tobacco trust. As president, Duke built the trust into a monopoly that controlled 98 percent of the domestic cigarette market by 1892, a year in which 2.9 billion cigarettes were sold.[3] Not content with domination alone, he worked tirelessly to expand the tobacco market. By 1903, more than 10 billion cigarettes were sold in the United States.[4] Over two decades his combination ruthlessly swallowed or bankrupted 250 firms until it dominated the cigar, snuff, and smoking tobacco markets too.

Duke used a simple method to strangle competitors. Instead of selling its output at wholesale prices, Duke's company "consigned" its products to dealers. The dealers had to pay full retail price for tobacco goods sent to them "on consignment" and do so within ten days of receipt. Three months later, the company paid the dealer a "commission," which was the dealer's profit. Dealers who sold competitors' brands were not eligible to receive this "commission," so they could not make a profit on the brands that the vast majority of their customers wanted. Duke used detectives to spy on dealers and enforce the scheme. Many dealers disliked this arrogant, coercive system, but they had to play along or wither away.

Duke's monopoly lasted until 1911, when the Supreme Court ordered it broken up.[5] Duke himself figured out how to divide the giant firm into four independent companies: Ligget & Myers, P. Lorillard, R. J. Reynolds, and a new American Tobacco Company. After the breakup he retired from the tobacco industry to start an electric utility, Duke Power & Light. He also gave money to a small North Carolina college, which became Duke University. He died of complications from pernicious anemia in 1925.

Duke's career illustrates the power of commerce to shape society. He made the cigarette an acceptable consumer product and spread it around the world. His monopoly destroyed rivals and defined the structure of the tobacco industry. Its influence checked the early efforts of antitobacco leagues to publicize health hazards. His bribes to legislators blocked antismoking laws. And, owing largely to Duke's ingenuity, growing tobacco trade revived the crippled post–Civil War southern economy. Eventually, he ran into a hard check on power when the Supreme Court dismantled his colossus, but his work endures in the roll call of smokers across 120 years.

[3] "Iron Heel of Monopoly," *New York Times,* December 28, 1892, p. 10.

[4] "The Caesar of Tobacco," *The Wall Street Journal,* June 27, 1903, p. 6.

[5] *United States v. American Tobacco Company,* 221 U.S. 106 (1911).

THE NATURE OF BUSINESS POWER

Business has tremendous power to change society, and the extent of this power is underappreciated. In past eras, companies in ascending industries changed societies by altering all three of their primary elements—ideas, institutions, and material things. This effect is visible in the stories of dominant companies such as the American Tobacco Company, the American Fur Company, and the Standard Oil Trust. The cumulative power of all business is a massive, irrepressible shaping force. In this chapter we explain the underlying dynamics of this power to change society. We then discuss its limits.

WHAT IS POWER?

power The force or strength to act or to compel another entity to act.

Power is the force or strength to act or to compel another entity to act. In human society it is used to organize and control people and materials in order to achieve individual or collective goals. It exists on a wide spectrum ranging from coercion at one extreme to weak influence at the other. Its use in human society creates change. Although power is sometimes exerted to prevent change, such resistance is itself a force that alters history. There are many sources of power, including wealth, position, knowledge, law, arms, status, and charisma. Power is unevenly distributed, and all societies have mechanisms to control and channel it for wide or narrow benefit. These mechanisms, which are imperfect, include governments, laws, police, cultural values, and public opinion. Also, multiple, competing formations of power may check and balance each other.

business power The force behind an act by a company, industry, or sector.

Business power is the force behind an act by a company, industry, or sector. The greater this force, the more the action creates change or influences the actions of other entities in society. Its basic origin is a grant of authority from society to convert resources efficiently into needed goods and services. In return for doing this, society gives corporations the authority to take necessary actions and permits a profit. This agreement derives from the social contract.

legitimacy The rightful use of power. Its opposite is tyranny, or the exercise of power beyond right.

The social contract legitimizes business power by giving it a moral basis. *Legitimacy* is the rightful use of power. The power of giant corporations is legitimate when it is exercised in keeping with the agreed-upon contract.[6] The philosopher John Locke wrote that for governments the opposite of legitimacy is tyranny, defined as "the exercise of power beyond right."[7] Corporations breach the social contract, exercising "power beyond right," when they violate social values, endanger the public, or act illegally.

Business power is legitimate when it is used for the common good. The grounds of legitimacy vary between societies and over time. Child labor, once widespread in the United States, is no longer permitted, but it exists in other nations. As we will

[6] For an effort to stipulate social contract norms that should guide business behavior, see Thomas Donaldson and Thomas W. Dunfee, *Ties That Bind: A Social Contracts Approach to Business Ethics* (Boston: Harvard Business School Press, 1999).

[7] John Locke, *The Second Treatise of Government* (New York: Bobbs-Merrill, 1952), p. 112; originally published in 1690.

see in subsequent chapters, the definition of the common good that business must serve has expanded throughout American history and is now expanding globally.

LEVELS AND SPHERES OF CORPORATE POWER

Corporate actions have an impact on society at two levels, and on each level they create change. On the *surface level,* business power is the direct cause of visible, immediate changes, both great and small. Corporations expand and contract, hire and fire; they make and sell products.

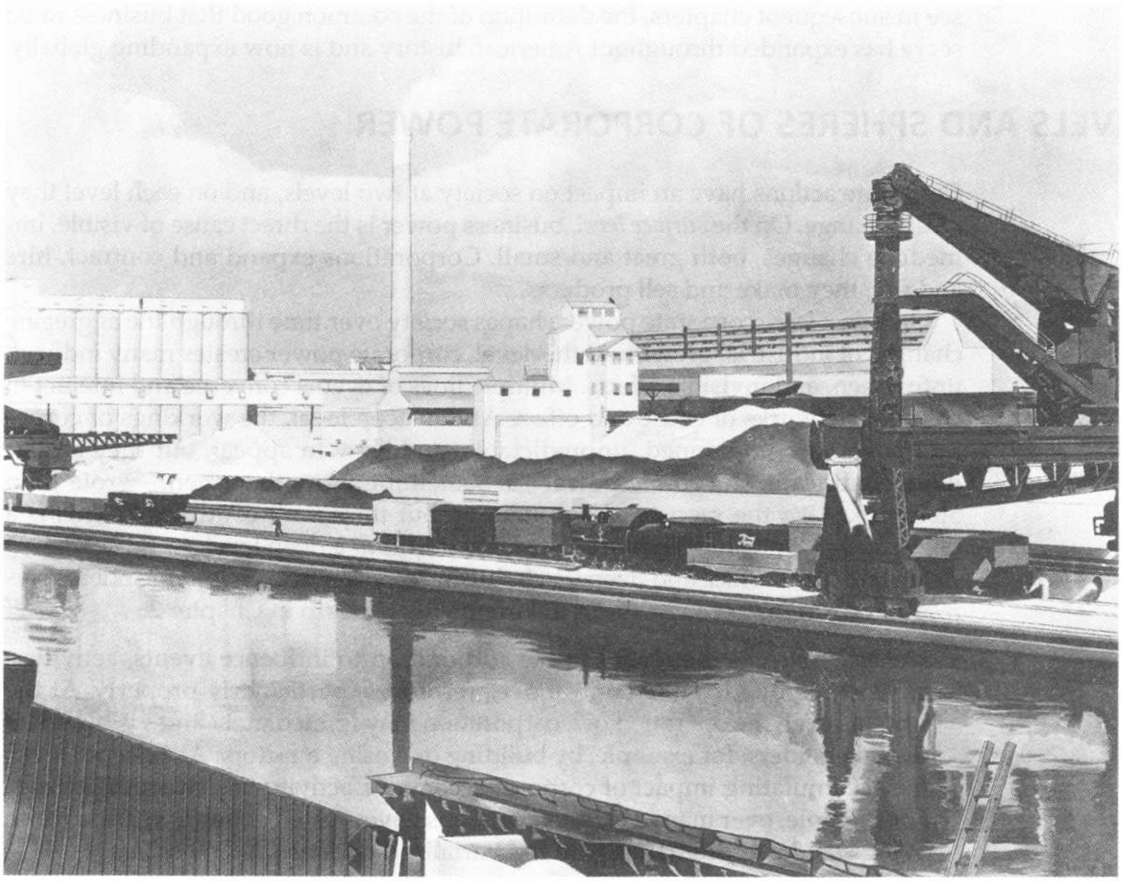
On a *deep level,* corporate power shapes society over time through the aggregate changes of industrial growth. At this level, corporate power creates many indirect, unforeseen, and invisible effects. Multiple lines of events converge and interact in complex networks of cause and effect. At this deep level, the workings of corporate power are unplanned, unpredictable, and slow to appear, but they are far more significant. Corporate power "is something more than men," wrote John Steinbeck. "It's the monster. Men made it, but they can't control it."[8] This is a poetic but accurate description of business power at a deep level.

On both the surface and deep levels, business power is exercised in spheres corresponding to the seven business environments set forth in Chapter 2.

- *Economic power* is the ability of the corporation to influence events, activities, and people by virtue of control over resources, particularly property. At the surface level, the operation of a corporation may immediately and visibly affect its stakeholders, for example, by building or closing a factory. At a deeper level, the accumulating impact of corporate economic activity has sweeping effects. For example, over many years corporations have created enough wealth to raise living standards dramatically in industrialized nations.
- *Technological power* is the ability to influence the direction, rate, characteristics, and consequences of physical innovations as they develop. On a surface level, in 1914, assembly lines run by new electric motors allowed Henry Ford to introduce transportation based on the internal combustion engine. Using this method, he turned an expensive luxury of the rich into a mass consumer product. But at a deeper level, as the auto took hold in American society it created unanticipated consequences. One juvenile court judge in the 1920s called the automobile a "house of prostitution on wheels," something that the puritanical Henry Ford doubtless never intended to create.[9]
- *Political power* is the ability to influence governments. On the surface, corporations give money to candidates and lobby legislatures. On a deeper level, around the world industrialization engenders values that radiate freedom and erode authoritarian regimes.
- *Legal power* is the ability to shape the laws of society. On the surface, big corporations have formidable legal resources that intimidate opponents. On a

[8] *The Grapes of Wrath* (New York: Viking Press, 1939), p. 45.

[9] Frederick Lewis Allen, *Only Yesterday: An Informal History of the 1920s* (New York: Harper & Brothers, 1931), p. 100.



American Landscape, a 1930 oil painting, depicts Ford Motor Company's mighty River Rouge plant, which took in raw materials such as sand and iron ore at one end and turned out finished autos at the other. In its day, the plant was regarded as a wonder and people traveled from around the world to see it. Here artist Charles Sheeler evokes the power of business to change and shape society. On the surface, this vista seems to beautify and ennoble the architecture of production, making it seem almost pastoral. Yet on a deeper level the painting provokes anxiety. Factory buildings run nature off the scene, dominating a landscape that is now, but for the sky, entirely artificial. A tiny human figure in the middle ground is overwhelmed and marginalized by the massive complex; its movement limited and regimented by the surrounding industrial structure. Here, then, art reveals emotions and insights about business power. Other Sheeler paintings and photographs are open to the same interpretation. He never revealed his intentions, leaving art critics to debate whether he was, in fact, sanguine or dispirited about how business power was shaping the "American landscape." Source: Digital Image © The Museum of Modern Art/Licensed by SCALA/Art Resource, NY.

deeper level, the laws of the United States—including constitutional, civil, and criminal laws—have been shaped by the consequences of industrial activity.

- *Cultural power* is the ability to influence cultural values, habits, and institutions such as the family. John Wanamaker, founder of a department store chain and a master of advertising, started Mother's Day in the early 1900s. He ran full-page ads in the *Philadelphia Inquirer* about a woman mourning for her mother, creating the sentiment that gratitude for mothers should be expressed by a gift on a special day.[10] At a deeper level, the cumulative impact of ads has altered American society by reinforcing values selectively, for example, materialism over asceticism, individualism over community, or personal appearance over inner character.

- *Environmental power* is the impact of a company on nature. On the surface, a power plant may pollute the air; on a deeper level, since the seventeenth century, emission of gases in the burning of wood, coal, and oil to power industry has altered the chemistry of earth's atmosphere. One study found that since 1882 the Standard Oil Trust and its successor companies have contributed between 4.7 and 5.2 percent of worldwide carbon dioxide emissions.[11]
- *Power over individuals* is exercised over employees, managers, stockholders, consumers, and citizens. On the surface, a corporation may determine the work life and buying habits of individuals. At a deeper level, industrialism sets the pattern of daily life. People are regimented, living by clocks, moving in routes fixed by the model of an industrial city with its streets and sidewalks. Their occupation determines their status and fortune.

Activity in the economic sphere is the primary force for change. From this, change radiates into other spheres. The story of the railroad industry in the United States illustrates how an expanding industry with a radical new technology can change its environments.

THE STORY OF THE RAILROADS

When small railroads sprang up in the 1820s, most passengers and freight moved by horse and over canals. The railroad was a vastly superior conveyance and was bound to revolutionize transportation. Tracks cost less to build than canals and did not freeze in winter. Routes could be more direct. For the first time in history, people and cargo traveled overland faster than the speed of a horse. The trip from New York to Chicago was reduced from three weeks to just three days. And the cost of moving goods and passengers was less; in a day a train could go back and forth many times over the distance that a canal boat or wagon could traverse once.

The initial boom in railroading came at mid-century. In 1850 trains ran on only 9,021 miles of track, but by 1860 30,626 miles had been laid down. During that decade, 30 railroad companies completed route systems, which had significant consequences for the financial system. Tracks were expensive, and each of these enterprises was a giant for its day. Many needed $10 to $35 million in capital, and the smallest at least $2 million. Companies in other industries did not approach this size; only a handful of textile mills and steel plants required capitalization of more than $1 million.[12]

[10] Richard Wolkomir and Joyce Wolkomir, "You Are What You Buy," *Smithsonian,* May 2000, p. 107.

[11] Friends of the Earth International, *Exxon's Climate Footprint* (London: FOEI, January 2004), p. 5. See also Richard Heede, *Exxon Mobil Corporation Emissions Inventory: 1882–2002* (London: Friends of the Earth Trust Ltd., December 17, 2003).

[12] Alfred D. Chandler, Jr., *The Visible Hand: The Managerial Revolution in American Business* (Cambridge, MA: Belknap Press, 1977), pp. 83, 86, and 90.

The call for this much money transformed capital markets. The only place such huge sums could be raised was in large northeastern cities. Since interest rates were a little higher in Boston at the time, New York became the center of financial activity and has remained so to this day. Railroads sold bonds and offered stocks to raise capital, and a new investment banking industry was created. The New York Stock Exchange went from a sleepy place, where only a few hundred shares of stock might change hands each week, to a roaring market. Speculative techniques such as margin trading, short-selling, and options trading appeared for the first time. Later, the financial mechanisms inspired by railroad construction were in place when other industries needed more capital to grow. This changed American history by accelerating the industrial transformation of the late 1800s. It also put New York bankers such as J. P. Morgan in a position to control access to capital.

At first the railroads ran between existing trade centers, but as time passed and track mileage increased, they linked ever more points. The 30,626 miles of track in 1860 increased to 93,267 miles by 1880 and 167,191 miles by 1890.[13] This required enormous amounts of wood, and led to extensive clear-cuts where forests were harvested to make ties and stoke fires in early steam locomotives. A deeper consequence of extending the tracks was a society transformed.

Before tracks radiated everywhere, the United States was a nation of farmers and small towns held together by the traditional institutions of family, church, and local government. Since long-distance travel was time-consuming and arduous, these towns often were isolated. Populations were stable. People identified more with local areas than with the nation as a whole. Into this world came the train, a destabilizing technology powered by aggressive market capitalism.

Trains took away young people who might have stayed in rural society but for the lure of wealth in distant cities. In their place came a stream of outsiders who were less under the control of community values. Small-town intimacy declined, and a new phenomenon appeared in American life—the impersonal crowd of strangers. Trains violated established customs. Sunday was a day of rest and worship, so many churchgoers were angered when huffing and whistling trains intruded on services. But new capital accounting methods used by railroad companies dictated using equipment an extra day each week to increase return on investment. This imperative trumped devoutness. In early America, localities set their own time according to the sun's overhead transit, but this resulted in a patchwork of time zones that made scheduling difficult. An editorial in *Railroad Age* argued, "Local time must go."[14] For the convenience of the railroads, a General Time Convention met in 1882 and standardized the time of day, though not without resistence from holdouts who felt that "[s]urely the world ran by higher priorities than railroad scheduling."[15]

[13] Bureau of the Census, *Statistical Abstract of the United States,* 77th ed. (Washington, DC: Government Printing Office, 1956), table 683.

[14] Bill Kauffman, "Why Spring Ahead," *The American Enterprise,* April–May 2001, p. 50.

[15] Ibid., p. 50, quoting Michael O'Malley, *Keeping Watch: A History of American Time* (Washington, DC: Smithsonian Institution Press, 1996).

As the railroads grew, they spread impersonality and an ethic of commerce. Towns reoriented themselves around their train stations. Shops and restaurants sprang up nearby so that strangers would spend money before moving on. The railroads gave more frequent service to cities with commercial possibilities and bypassed small towns or let them wither from less frequent service. This speeded urbanization and the centralization of corporate power in cities. Rural areas were redefined. Once the cultural heartland, they now were seen as backward and rustic—places best used for vacations from urban stress.

The railroads also changed American politics. On the surface, their lobbyists could dominate legislatures. On a deeper level, the changes were more profound. Congress had always selected nominees before presidential elections, but now trains brought delegates to national party nominating conventions, changing the way candidates were picked. Trains enabled all sorts of associations to have national meetings, and the rails spread issues that might in an earlier era have remained local. The movement to give women the vote, for example, succeeded after Susan B. Anthony took trains to all parts of the country, spreading her rhetoric and unifying the cause.[16]

At first government encouraged and subsidized railroads. All told, federal and state governments gave them land grants of 164 million acres, an area equal to the size of California and Nevada combined.[17] But later the challenge was to control them. When Congress passed the Interstate Commerce Act in 1887 to regulate railroads, the approach of the statute, with all its strengths and weaknesses, set the example for regulating other industries later.

Many other changes in American society are traceable to the railroads. They were the first businesses to require modern management structures. The need for precise coordination of speeding trains over vast reaches caused railroads to pioneer professional management teams, division structures, and modern cost accounting—all innovations later adopted in other industries.[18] Railroads lay behind Indian wars. For the plains Indians, tracks that divided old hunting grounds were the main barrier to peace.[19] Thousands of laborers came from China to lay rail, and their descendants live on in communities along the lines. Railroads changed the language. The word *diner,* meaning a place to eat, appeared after the introduction of the Pullman Palace Car Company's first dining car in 1868. The expression "hell on wheels" originally described the raucous body of prostitutes, gambling cars, and saloons that rolled along with construction crews as tracks spread west. The phrase "off again, on again" derives from discussions about train derailments.[20] And social values changed. Big-city commercial values rumbled down the tracks, jolting traditions along rural byways.

16 These and other social and political changes are treated at length in Sarah H. Gordon, *Passage to Union* (Chicago: Ivan R. Dees, 1996).

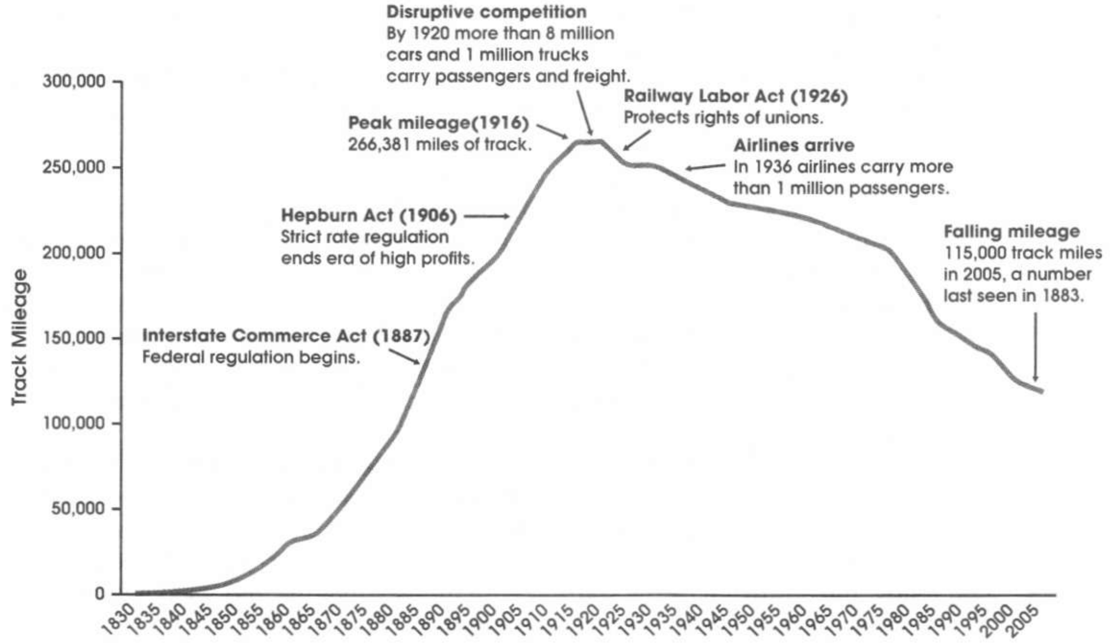
17 Page Smith, *The Rise of Industrial America,* vol. 6 (New York: Viking Penguin, 1984), p. 99.

18 Chandler, *The Visible Hand,* chap. 3.

19 Smith, *The Rise of Industrial America,* p. 89.

20 Rudolph Daniels, *Trains across the Continent: North American Railroad History,* 2d ed. (Bloomington: Indiana University Press, 2000), pp. 53 and 78.

FIGURE 3.1 **Railroad Track Miles in Operation 1830–2005**
The rise and decline of a powerful industry is reflected in the miles of track that trains have run on over the years.



Source of data: *Statistical Abstract of the United States*, various editions 1878–2006.

As the track system swelled so did the power of railroads to shape the sociopolitical as well as the physical landscape. Figure 3.1 shows how track mileage fell after 1916, reflecting a decline in the fortunes of the industry. Government regulation matured, making rate hikes more difficult and strengthening the hand of unions. In addition, railroads came into competition with new transportation technologies, first autos, buses, and trucks, then aircraft. As the importance of rails receded, these emerging technologies gathered power to shape American life.

TWO PERSPECTIVES ON BUSINESS POWER

There is agreement that business has great power. There is considerable disagreement about whether its power is adequately checked and balanced for the public good. Views about business power cover a wide spectrum, but there are two basic and opposing positions.

On one side is the *dominance theory*, which holds that business is preeminent in American society, primarily because of its control of wealth, and that its power is both excessive and inadequately checked. Corporations can alter their environments in self-interested ways that harm the general welfare. This was the thesis of Karl Marx, who wrote that a ruling capitalist class exploited workers and dominated

dominance theory The view that business is the most powerful institution in society, because of its control of wealth. This power is inadequately checked and, therefore, excessive.

pluralist theory The view that business power is exercised in a society where other institutions also have great power. It is counterbalanced and restricted and, therefore, not excessive.

other classes. The dominance theory is the basis of the dominance model of the business–government–society relationship set forth in Chapter 1.

On the other side the *pluralist theory* holds that business power is exercised in a society in which other institutions such as markets, government, labor unions, advocacy groups, and public opinion also have great power. Business power is counterbalanced, restricted, controlled, and subject to defeat. Adam Smith was convinced that largely through market forces, business power could be disciplined to benefit society. The pluralist theory is the basis of the countervailing forces model in Chapter 1.

The Dominance Theory

In industrializing societies, business organizations grow in size and concentrate wealth. According to the dominance theory, business abuses the power its size and wealth confer in a number of ways. The rise of huge corporations creates a business elite that exercises inordinate power over public policy. Asset concentration creates monopoly or oligopoly in markets that reduces competition and harms consumers. Corporations wield financial and organizational resources unmatched by opposing interests. For example, they use campaign contributions to corrupt politicians, hire lobbyists to undermine the independence of elected officials, employ accountants and lawyers to avoid taxes, and run public relations campaigns that shape opinion in their favor.

Moreover, large corporations achieve such importance in a nation's economy that elected officials are forced to adopt probusiness measures or face public wrath. "If enterprises falter for lack of inducement to invest, hire, and produce," writes one advocate of the dominance theory, "members of the political elite are more likely than those of the entrepreneurial elite to lose their positions."[21] We will discuss further the growth in size and wealth of corporations and the presence of elites.

Corporate Asset Concentration

The idea that concentration of economic power results in abuse arose, in part, as an intellectual reaction to the awesome economic growth of the late nineteenth century. Until then, the United States had been primarily an agricultural economy. But between 1860 and 1890, industrial progress transformed the country. Statistics illustrating this are striking. During these 30 years, the number of manufacturing plants more than doubled, growing from 140,433 to 355,415; the value of what they made rose more than 400 percent, from \$1.8 billion to \$9.3 billion; and the capital invested in them grew 650 percent, from \$1 billion to \$6.5 billion.[22]

This growth did more than create wealth; it also concentrated it. At the end of the century, between 1895 and 1904, an unprecedented merger wave assembled dominant firms in industry after industry. Since then, there have been other great

[21] Charles E. Lindblom, *The Market System: What It Is, How It Works, and What to Make of It* (New Haven: Yale University Press, 2001), p. 247.

[22] Figures in this paragraph are from Arthur M. Schlesinger, *Political and Social Growth of the United States: 1852–1933* (New York: Macmillan, 1935), pp. 132–44.

merger waves, but this was the first. It made a definitive impression on the American mind, and its legacy is an enduring fear of big companies.

Merger waves are caused by changes in the economic environment that create incentives to combine. The main stimulus for the 1895–1904 wave was the growth of the transcontinental railroads, which reduced transportation costs, thereby creating new national markets. Companies rushed to transform themselves from regional operations to national ones. Combinations such as James Duke's American Tobacco Company gorged themselves, swallowing competitors. They crowded into formerly isolated markets, wiping out small family businesses. The story was repeated in roughly 300 commodities, including oil, copper, cattle, smelting, and such items as playing cards and tombstones. A 1904 study of the 92 largest firms found that 78 controlled 50 percent of their market, 57 controlled 60 percent or more, and 26 controlled 80 percent or more.[23]

At the time, the public failed to see the growth of huge firms as a natural, inevitable, or desirable response to the new economic incentives. Instead, it saw them as colossal monuments to greed. Companies of this size were something new. They inspired a mixture of awe and fear. In 1904, when the United States Steel Corporation became the first company with more than $1 billion in assets, people were astounded. Previously, such numbers applied in the realm of astronomy, not business.

In the twentieth century, corporations continued to grow in size, but the marked rise in asset concentration slowed and leveled off. By 1929 the 200 largest nonfinancial corporations in the United States (less than 0.7 percent of all nonfinancials) controlled nearly 50 percent of all corporate wealth. But by 1947 the nation's top 200 corporations had only 46 percent of corporate wealth, and this was reduced to 36 percent in 1996.[24] Although no continuing data series exists to provide a current figure, a recent study reveals that asset concentration in the top 200 firms on the Fortune 500 declined by 8 percent between 1995 and 2004.[25]

Because of the trend toward global production today the number of transnational firms and the scale of their activity has grown. There are approximately 78,000 transnationals, up from only about 34,000 as recently as 1990. Assets and sales of the largest of these firms are rising. Between 1990 and 2005, assets of the 100 biggest transnationals increased by 271 percent and sales by 213 percent.[26] However, despite

[23] John Moody, *The Truth about Trusts: A Description and Analysis of the American Trust Movement* (New York: Greenwood Press, 1968), p. 487; originally published in 1904.

[24] J. Fred Weston, Kwang S. Chung, and Juan A. Siu, *Takeovers, Restructuring, and Corporate Governance*, 2d ed. (Upper Saddle River, NJ: Prentice Hall, 1998), p. 116. These figures allow rotation of new firms into the top 200 firms. If the same 200 firms had been followed over the years, asset concentration would have fallen even faster.

[25] Edward Nissan, "Structure of American Business: Goods versus Services," *Southwestern Economic Review* (online), Spring 2006, table 1.

[26] United Nations Conference on Trade and Development (UNCTAD), *World Investment Report 2007* (New York: United Nations, July 2007), table I.10; and UNCTAD, *World Investment Report 1993* (New York: United Nations, July 1993), table I.11.

heightened global merger activity, the largest global firms do not show signs of concentrating international assets the way that large American firms have concentrated domestic assets. In fact, the foreign assets of the largest 100 transnationals fell from 13 percent of estimated global assets in 1999 to 11 percent in 2004.[27] And these 100 firms are still only a small part of world economic activity. For the decade 1990–2000, their economic activity as a share of world GDP grew from 3.5 percent to only 4.3 percent.[28]

Despite this, adherents of the dominance theory believe that the increasing size and financial power of global corporations will be converted into the same old abuses. But the link between market power and abuse remains to be seen. Larger transnational firms in many industries do not necessarily even have increased market power because they face formidable competitors, emerging competition from new industries, enlarged market boundaries, and more aggressive antitrust enforcement. In the sociopolitical dimension, these firms face growing global pressures to act responsibly.

Also, no corporation, no matter how large, is assured of prospering. Over time, poor management, competition, and technological change have continuously revised the roster of America's biggest companies. Of the 100 largest corporations in 1909, only 36 remained on the list until 1948. Between 1948 and 1958, only 65 of the top 100 held their place. Only 116 company names remained on the Fortune 500 list of industrial corporations from its inception in 1955 to 1994. By 2003 only 71 of the original 500 were still there.[29] Many firms dropped from the list were, of course, acquired by other firms. Among the 100 largest transnational corporations there were 28 American firms in 1990, but that number had declined to 25 by 2004.[30] The lesson is that, with a very few exceptions, the power of uncontrollable competitive forces exceeds the power of even the largest corporations to maintain their dominance.

Elite Dominance

Another argument that supports the dominance theory is that there exist a small number of individuals who, by virtue of wealth and position, control the nation. The members of this elite are alleged to act in concert and in undemocratic ways. There is a long history of belief in an economic elite dominating American society. In the debates preceding adoption of the Constitution in 1789, some opponents charged that the delegates were wealthy aristocrats designing a government favorable to their businesses. Later, farmers suspected the hand of an economic elite in

[27] Figures are from UNCTAD, *World Investment Report 2000* (New York: United Nations, 2000), p. 71; and UNCTAD, *World Investment Report 2006* (New York: United Nations, July 2006), p. 30.

[28] UNCTAD, *World Investment Report 2002*, box table IV.1.2. These figures are based on a value-added calculation (the sum of salaries, pretax profits, and depreciation and amortization) for TNCs.

[29] Figures in this paragraph are from Neil H. Jacoby, *Corporate Power and Social Responsibility* (New York: Macmillan, 1973), p. 32; John Paul Newport, Jr., "A New Era of Rapid Rise and Ruin," *Fortune*, April 24, 1989, p. 77; Carol J. Loomis, "Forty Years of the 500," *Fortune*, May 15, 1995, p. 182; and Julie Schlosser and Ellen Florian, "Fifty Years of Amazing Facts!" *Fortune*, April 5, 2004, p. 159.

[30] UNCTAD, *World Investment Report 2006*, p. 31.

The Rise and Decline of Powerful Corporations

In 1896 journalist Charles H. Dow created a list of 12 companies as an index of stock market performance. Each firm was a leader in an important industry and represented its fortunes. As America's industrial structure changed over the years, companies came and went; and the list, today called the Dow Jones Industrial Average Index, grew from 12 to 30. The most recent additions and deletions were made in 2008.

The leading firms in 1896 reflect a different world. Farming was much more important in the American economy, and four firms dealt in agricultural products. They included James B. Duke's American Tobacco Company, cotton and sugar producers, and a company that made livestock feed. Other firms represented the prominence of industrial technologies based on iron, lead, and coal. U.S. Leather made a product in the shadow of imminent obsolescence, leather belts used for power transmission in factories. General Electric, which made electric motors, was the technology company of that era. Chicago Gas and Laclede Gas Light Co. of St. Louis were utilities supplying natural gas for new gas streetlamps in cities. North American Co. ran streetcars.

1896	2008	
American Cotton Oil	Alcoa	Home Depot
American Sugar Refining	American Express	IBM
American Tobacco	American International Group	Intel
Chicago Gas	AT&T	J. P. Morgan Chase
Distilling & Cattle Feeding	Bank of America	Johnson & Johnson
General Electric	Boeing	McDonald's
Laclede Gas Light	Caterpillar	Merck
National Lead	Chevron	Microsoft
North American	Coca-Cola	3M
Tennessee Coal & Iron	Citigroup	Pfizer
U.S. Leather	DuPont	Procter & Gamble
U.S. Rubber	ExxonMobil	United Technologies
	General Electric	Verizon Communications
	General Motors	Wal-Mart Stores
	Hewlett-Packard	Walt Disney

The 2008 list registers the rise of new technologies and sectors of the economy providing services and consumer products. General Electric is the only company that was on the 1896 list, and it was removed for nine years between 1898 and 1907. Of the other 11 original firms, 2 (American Tobacco and North American) were broken up by antitrust action, 1 (U.S. Leather) was dissolved, and 8 continue to operate as less important companies or as parts of other firms that acquired their assets.

As a biography of American industry, the index dramatizes the rise and fall of powerful companies and industries. Over more than a century, 100 different firms have been listed. The index teaches that dominance of even the largest firms is transient.

the probusiness policies of Alexander Hamilton, George Washington's secretary of the treasury, who had many ties to wealth and commercial power. Since the colonial era, charges of elitism have surfaced repeatedly in popular movements opposed to big business.

The modern impetus for the theory of elite dominance comes from the sociologist C. Wright Mills, who wrote a scholarly book in 1956 describing a "power elite" in American society. "Insofar as national events are decided," wrote Mills, "the power elite are those who decide them."[31] Mills saw American society as a pyramid of power and status. At the top was a tiny elite in command of the economic, political, and military domains. Mills was never specific about its numbers, but said it was small. Just below was a group of lieutenants who carried out the elite's policies. They included professional managers of corporations, politicians beholden to the elite for their election, and bureaucrats appointed by the politicians. The large base of the pyramid was composed of a mass of powerless citizens, including feeble groups and associations with little policy impact. This image of a pyramid corresponds to the dominance model in Chapter 1.

power elite A small group of individuals in control of the economy, government, and military. The theory of its existence is associated with the American sociologist C. Wright Mills.

Mills did not see America as a democracy and thought that the elite simply used government "as an umbrella under whose authority they do their work."[32] Although he never stated that the economic segment of the elite was dominant over the political and military, he noted that "the key organizations, perhaps, are the major corporations."[33]

The Power Elite is a book in which there is more speculation than substantiation. It is based on cursory evidence. There is none of the statistical research that would be required to support such sweeping generalizations in a similar work of sociology today. Yet it contained a powerful new explanation of economic power and came out just as many American leftists were becoming disenchanted with Marxism. Mills's vision of a small ruling elite caught on and has been popular with the anticorporate left ever since. Mills would have been pleased. In correspondence, he once expressed indignation about the power of "the sons of bitches who run American Big Business."[34]

Scholars inspired by Mills have pressed the study of elites and are less reluctant to suggest business dominance. One is G. William Domhoff, who has for more than 30 years argued that an upper class dominates America through its control of corporations. He writes of "a general leadership group for the corporate community and the upper class, called the *power elite*," that consists of "members of the upper class who have taken on leadership roles in the *corporate community*."[35]

> [T]he owners and top-level managers in large companies work together to maintain themselves as the core of the dominant power group. Their corporations, banks, and

[31] C. Wright Mills, *The Power Elite* (New York: Oxford University Press, 1956), p. 18.

[32] Ibid., p. 287.

[33] Ibid., p. 283.

[34] In a letter to his parents quoted by John B. Judis, "The Spiritual Wobbly," *New York Times Book Review*, July 9, 2000, p. 9.

[35] G. William Domhoff, *Who Rules America: Power, Politics, & Social Change*, 5th ed. (New York: McGraw-Hill, 2006), pp. xiii and 103 (emphasis in the original).

agribusinesses form a corporate community that shapes the federal government on the policy issues of interest to it . . . [t]he power elite consists of those people who serve as directors or trustees in profit and nonprofit institutions controlled by the corporate community through stock ownership, financial support, or involvement on the board of directors.[36]

In an effort extending over 25 years political scientist Thomas R. Dye has tried to identify precisely which individuals constitute an American elite. Believing that power comes from leadership roles in corporations, government, and other large organizations, he defines a "national institutional elite" composed of

individuals who occupy the top positions in *the institutional structure of American society.* These are the individuals who possess the formal authority to formulate, direct, and manage programs, policies, and activities of the major corporate, governmental, legal, educational, civic, and cultural institutions in the nation. . . . For purposes of analysis we have divided American society into ten sectors: (1) industrial (nonfinancial) corporations, (2) banking, (3) insurance, (4) investments, (5) mass media, (6) law, (7) education, (8) foundations, (9) civic and cultural organizations, and (10) government.[37]

Applying this method, Dye identified 7,314 elite positions and found that they were held by 5,778 individuals (because some persons held more than one position). This is a much larger elite than that suggested by Mills, but it is still only about three-thousandths of 1 percent of the population.

Elites formed from some combination of wealth, ability, position, and social status are inevitable. Their existence is a challenge to the validity of democratic governance in that it divides citizens into a small number who rule and a vast majority who are ruled. But elites are not necessarily sinister, oppressive, or conspiratorial. They can be sources of talent and expert leadership. The American business elite comes from the ranks of top corporate executives and directors, and those who hold these positions do so based overwhelmingly on ability. Turnover is frequent. However, those selected at these rarified levels come from a narrow range of backgrounds. Every study of them finds that disproportionately they are male, white, and Christian; that they come from upper-class families; and that they graduate from a few prestigious universities. Evidence suggests that inclusion of blacks, Latinos, and women is based on their similarity in background and thinking to the existing elite.[38] In conclusion, the presence of an American elite, one perhaps dominated by business interests, troubles a nation with such a deep commitment to equality. Yet some argue that its actions are adequately checked and balanced. This view is taken up in the next section.

Pluralist Theory

pluralistic society
A society with multiple groups and institutions through which power is diffused.

A *pluralistic society* is one having multiple groups and institutions through which power is diffused. Within such a society no entity or interest has overriding power, and each may check and balance others. The countervailing forces model

[36] Ibid., pp. xi and 103.

[37] Thomas R. Dye, *Who's Running America? The Bush Restoration,* 7th ed. (Upper Saddle River, NJ: Prentice Hall, 2002), p. 8; emphasis in the original.

[38] Richard L. Zweigenhaft and G. William Domhoff, *Diversity in the Power Elite: Have Women and Minorities Reached the Top?* (New Haven: Yale University Press, 1998).

J. P. Morgan and the Panic of 1907

In the first decade of the twentieth century, J. P. Morgan (1837–1913), head of J. P. Morgan & Co. in New York, was often called the most powerful man in the country. He specialized in buying competing companies in the same industry and merging them into a single, monopolistic firm. He joined separate railroads into large systems. He combined smaller electrical concerns into General Electric in 1892 and then pulled a collection of manufacturers into the International Harvester Company, which started with 85 percent of the farm machinery market. In 1901 he created the first billion-dollar company when he merged 785 separate firms to form the United States Steel Company with capitalization of $1.4 billion.

Morgan and two of his close associates together held 341 corporate directorships. His power was very independent of government controls since at the time antitrust laws were little enforced, there was no national bank to regulate the money supply, and existing securities and banking laws were rudimentary. One awestruck biographer said that Morgan "was a God" who "ruled for a generation the pitiless, predatory world of cash."[39] His critics were less kind. Senator Robert W. La Follette once called him "a beefy, red-faced, thick-necked financial bully, drunk with wealth and power."[40]

In October 1907 panic swept Wall Street and stocks plummeted as frantic investors sold shares. Soon banks suffered runs of withdrawals and were on the verge of failure. Liquidity, or the free flow of money, was fast vanishing from financial markets, and the nation's banking system teetered on the verge of collapse. So influential was Morgan that he commanded the New York Stock Exchange to stay open all day on October 24 to maintain investor confidence. To support it, he raised $25 million of credit.

[39] John K. Winkler, *Morgan the Magnificent* (New York: Doubleday, 1950), p. 3; originally published in 1930.
[40] Jean Strouse, *Morgan: American Financier* (New York: Random House, 2000), p. x.

The federal government could do little to ease the crisis. President Theodore Roosevelt was off hunting bears in Louisiana, an ironic pursuit in light of the crashing stock market. Without a national bank, the government had no capacity to increase the money supply and restore liquidity. Powerless, Secretary of the Treasury George B. Cortelyou traveled to New York to get Morgan's advice.

On the evening of October 24, Morgan gathered members of the New York banking elite at his private library. He played solitaire while in another room the assembled bankers discussed methods for resolving the crisis. Periodically, someone came to him with a proposal, several of which he rejected. Finally, a plan was hatched in which $33 million would be raised to support the stock exchange and failing banks. Where would this money come from? The secretary of the treasury was to supply $10 million in government funds, John D. Rockefeller contributed $10 million, and Morgan the remaining $13 million.

This action stabilized the economy. Perhaps it demonstrates that elite power may be exercised in the common good. It should be noted, however, that the panic of 1907—and other panics of that era—came after Morgan and other titans of finance repeatedly choked the stock exchange with the colossal stock offerings needed to finance their new combinations.

Morgan was widely criticized for his role in ending the panic of 1907. Conspiracy theorists, suspicious of so much power resident in one man, attacked him. Upton Sinclair, for example, accused him of inciting the panic for self-gain, a wildly erroneous accusation. In 1912 Morgan was the focus of congressional hearings which concluded that he led a "money trust" that controlled the nation's finances and that this was bad for the nation. Death claimed him in 1913 just before Congress passed the Federal Reserve Act to set up a central bank and ensure that no private banker would ever again be sole caretaker of the money supply.

in Chapter 1 illustrates how, in such a society, business must interact with constraining forces in its environment. It may have considerable influence over some of them; but over most it has limited influence, and over a few none at all. Several features of American society support this thesis of pluralism.

First, it is infused with democratic values. Unlike many nations, America has no history of feudal or authoritarian rule, so there is no entrenched deference to an aristocracy of wealth. In colonial days, Americans adopted the then-revolutionary doctrine of natural rights, which held that all persons were created equal and entitled to the same opportunities and protections. The French aristocrat Alexis de Tocqueville, who toured America and wrote an insightful book about American customs in the 1830s, was forcibly struck by the "prodigious influence" of the notion of equality. Belief in equality, he wrote, ran through American society, directing public opinion, informing the law, and defining politics. It was, he wrote, "the fundamental fact from which all others seem to be derived." [41] Thus, in America laws apply equally to all. All interests have the right to be heard. To be legitimate, power must be exercised for the common good.

Second, America encompasses a large population spread over a wide geography and engaged in diverse occupations. It has a great mixture of interests, more than some other countries. Economic interests, including labor, banking, manufacturing, agriculture, and consumers, are a permanent fixture. A rainbow of voluntary associations (whose size, longevity, and influence vary) compete in governments at all levels.

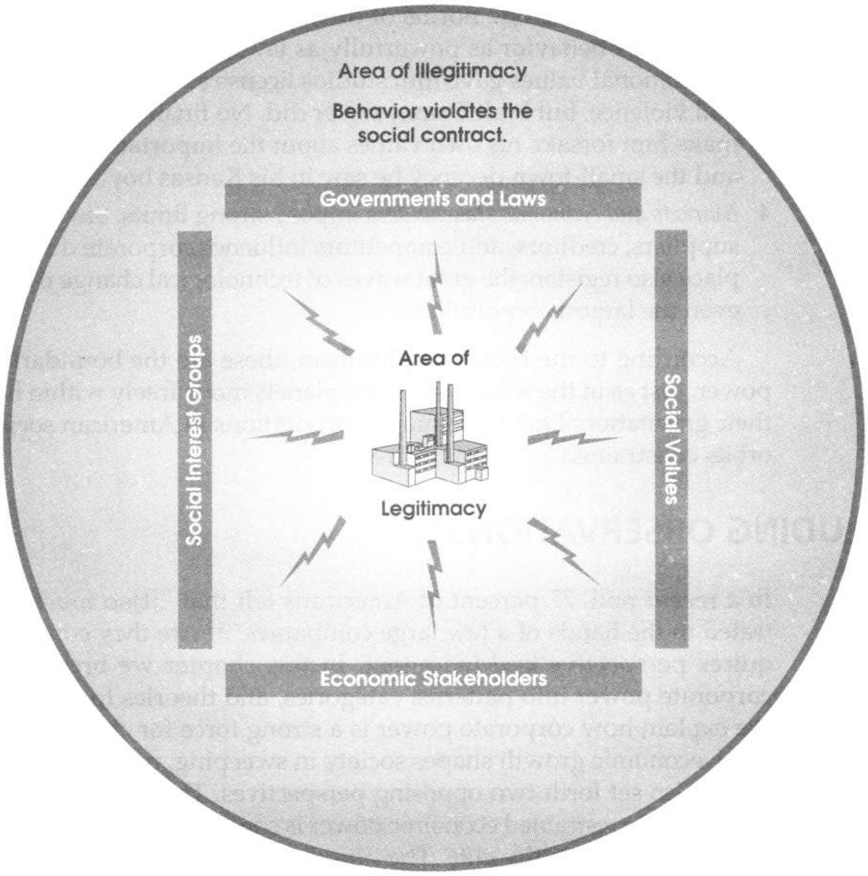
Third, the Constitution encourages pluralism. Its guarantees of rights protect the freedom of individuals to form associations and freely to express and pursue interests. Thus, business is challenged by human rights, environmental, and other groups. The Constitution diffuses political power through the three branches of the federal government and between the federal and state governments and to the people. This creates a remarkably open political system.

In addition, business is exposed to constraining market pressures that force a stream of resource allocation decisions centered on cost reduction and consumer satisfaction, forces that can fell even the mighty. Henry J. Kaiser seemed unerring in business. The son of German immigrants, he worked his way up from store clerk to owner of 32 companies, including seven shipyards that launched one finished ship a day during most of World War II. When he started an auto company in 1945, nobody thought he could fail. Eager customers put down thousands of deposits before a single car was built.[42] But his cars, the Kaiser and the Frazier, were underpowered and overpriced, and the market eventually rejected them. The venture failed. Kaiser never got costs under control; he had to negotiate the prices of many parts with competing auto companies that made them. Toward the end, he built a model that was sold at Sears as the Allstate. This was a terrible mistake because it gave the car a low-quality image with consumers.

[41] Alexis de Tocqueville, *Democracy in America* (New York: New American Library, 1956), p. 26; originally published as two volumes in 1835 and 1850.

[42] Robert Sobel, "The $150 Million Lemon," *Audacity,* Winter 1997, p. 11.

FIGURE 3.2
Boundaries of Managerial Power



In sum, predictable and strong forces in a pluralistic, free market society limit business power. Wise managers anticipate that, despite having considerable influence on governments, markets, and public opinion, their power can be restricted, challenged, or shared by others. Overall, as illustrated in Figure 3.2, there are four major boundaries on managerial power.

1. *Governments and laws* in all countries regulate business activity. Governments are the ultimate arbiters of legitimate behavior and can act forcefully to blunt the exercise of corporate power that harms the public. Laws channel and restrict operations.
2. *Social interest groups* represent every segment of society and use many methods to restrain business, including product boycotts, lawsuits, picket lines, media campaigns, and lobbying for more regulation. Historically, labor has been the great antagonist and counterweight to business power, but also prominent in recent years are environmental, human rights, religious, consumer, and public interest groups.
3. *Social values* are transmitted across generations, reflected in public opinion, and embedded in the law. Managers internalize them in schools and churches.

Social values include norms of duty, justice, truth, and piety that can direct a manager's behavior as powerfully as laws. For example, in the 1960s shifting generational values gave film studios license to experiment with brazen nudity and violence, but Walt Disney never did. No financial incentive was enough to make him forsake his own values about the importance of morality, family life, and the small-town decency he saw in his Kansas boyhood.[43]

4. *Markets and economic stakeholders* impose strong limits. Stockholders, employees, suppliers, creditors, and competitors influence corporate decisions. The marketplace also registers the great waves of technological change that can sweep away even the largest corporations.

According to the theory of pluralism, these are the boundaries of managerial power. Just as in the solar system the planets move freely within but cannot escape their gravitational fields, so major corporations in American society move within orbits constrained by plural interests.

CONCLUDING OBSERVATIONS

In a recent poll, 77 percent of Americans felt that "[t]oo much power is concentrated in the hands of a few large companies."[44] Are they correct? The answer requires perspective and judgment. In this chapter we break down the idea of corporate power into patterns, categories, and theories to allow critical thinking. We explain how corporate power is a strong force for change and how, at a deep level, economic growth shapes society in sweeping, unplanned ways.

We also set forth two opposing perspectives. The dominance theory holds that inadequately restrained economic power is concentrated in large corporations and in the hands of a wealthy elite. The pluralist theory holds that many restraints in an open society control corporate power. These theories are locked in perpetual conflict. Both are molds into which varieties of evidence must be fitted. Both contain insights, but neither has a lock on accuracy. And both attract adherents based on inner judgments about whether market capitalism moves society in the right direction.

If corporate power remains generally accountable to democratic controls, society will accord it legitimacy. If rule by law and a just economy exist, corporate power will broadly and ultimately be directed toward the public welfare, this despite the habitual breakouts of deviltry that inflame critics.

[43] Richard Schickel, *The Disney Version*, 3d ed. (Chicago: Ivan R. Dee, 1997), p. 39.

[44] Princeton Survey Research Associates International, national adult survey, question ID USPSRA.051005A, R11M, May 10, 2005.

John D. Rockefeller and the Standard Oil Trust

This is the story of John D. Rockefeller, founder of the Standard Oil Company. It is the story of a somber, small-town boy who dominated the oil industry with organizational genius, audacity, and ruthless, methodical execution. He became the richest man in America and, for a time, the most hated.

Rockefeller's life spanned 98 years. At his birth Martin Van Buren was president and settlers drove covered wagons over the Oregon Trail. He lived to see Franklin Roosevelt's New Deal, watch the rise of the Nazi party in Germany, and hear Frank Sinatra and *The Lone Ranger* on radio.

The historical backdrop of this lifetime is an economy gripped by the fever of industrial progress. Rockefeller built his fortune in an era that lacked many of today's ethical norms and commercial laws, an era in which the power of a corporation and its founder could be exercised with fewer restraints.

THE FORMATIVE YEARS

John Davison Rockefeller was born on July 8, 1839, in a small village in southern New York. He was the second of six children and the oldest boy. His father, William Rockefeller, was an itinerant quack doctor who sold worthless elixirs and engaged in a wide variety of businesses. He was jovial, slick, and cunning and made enough money to keep the family in handsome style until he had to flee and live away from home to avoid arrest on a charge of raping a local woman. After that, he visited only in the dark of night. But he taught young John D. and his brothers lessons of business conduct, especially that sentimentality should not influence business transactions. "I cheat my boys every chance I get," he once said. "I want to make 'em sharp."[1]

John D.'s mother was a somber, religious woman who gave the children a strict upbringing, emphasizing manners, church attendance, and the work ethic. She preached homilies such as "Willful waste makes woeful want." And she taught charity to the children; from an early age John D. made regular contributions to worthy causes.

Young John D. was not precocious in school. In high school he was an uninspired student, little interested in books and ideas, but willing to work hard. He grew into a somber, intense lad nicknamed "the Deacon" by his classmates because he faithfully attended a Baptist church and memorized hymns. In the summer of 1855 he attended a three-month course at a business college in Cleveland, Ohio, and then set out looking for a job. In addition to his formal schooling, he carried the contradictory temperaments of his parents—the wily, self-assured boldness of his father and the exacting, pietistic character of his mother. He internalized both, and the combination was to prove formidable. Here was a man with the precision of an accountant and the cunning of Cesare Borgia.

EARLY BUSINESS CAREER

Rockefeller's first job was as a bookkeeper at a Cleveland firm where he meticulously examined each bill submitted and pounced on errors. He also recorded every cent he earned and spent in a personal ledger. Its pages show that he was parsimonious and saved most of his $25-a-month salary but that he still gave generously to the Baptist church and the poor.

In 1859 he formed a successful partnership with two others in the produce business in Cleveland and proved himself an intense negotiator, described by an acquaintance as a person "who can walk right up on a man's shirt bosom and sit down."[2] The business boomed from supplying food to the Union army during the Civil War. Although in his early 20s at the time, the steady, unemotional lad was never touched by patriotic fervor. In those days, the law permitted any man of means to pay someone else to serve in his place, and this he did.

BEGINNINGS OF THE OIL BUSINESS

Profits from the produce business were high, and John D. looked around for a promising new investment. He soon found one—a Cleveland petroleum refinery in which he invested $4,000 in 1863. At the time, petroleum production and refining was an infant industry. A new drilling technology had led to an 1859 oil strike in nearby Pennsylvania, followed by a frenzied boom in drilling and refining.

Soon Rockefeller devoted himself full time to the oil business, and he began to apply his principles of parsimony. One basic principle was to avoid paying a profit to anyone. For example, instead of buying barrels and paying the cooper $2.50 each, Rockefeller set up his own barrel-making factory and made them for $.96. He purchased a forest to make staves from his own trees. Another basic principle was methodical

[1] David Freeman Hawke, *John D.: The Founding Father of the Rockefellers* (New York: Harper & Row, 1980), p. 13.

[2] Jules Abels, *The Rockefeller Billions* (New York: Macmillan, 1965), p. 35.

cost cutting. Lumber for barrel staves was kiln-dried before shipment to the cooperage plant. Water evaporated from the wood, making it lighter and lowering transportation costs.

Though obsessed with details and small economies, Rockefeller also proved aggressive in larger plans. He borrowed heavily from banks to expand the refinery. The risk scared his partners, so he bought them out. In 1865 he borrowed more to build a second refinery. Soon he incorporated an export sales company in New York, making the world his market.

DYNAMICS OF THE OIL INDUSTRY

During this early period, the new industry was in a chaotic state. A basic cause was overproduction in the Pennsylvania oil regions, which were the only source of crude oil. The price of crude fluctuated wildly, but was in long-term decline. Each drop in the price of crude oil encouraged construction of new refineries and by the late 1860s refining capacity was three times greater than oil production. This caused vicious price wars. Some refiners tried to stay in business by selling products at a loss to raise cash for continued debt payments. In doing so, they dragged down profit margins for all refiners.

Rockefeller had the insight to invest in large-scale refineries and, because he cut costs relentlessly, his refineries made money. Yet despite disciplined cost control, the market forces of a sick industry ate away at his net earnings. He believed it was time to "rationalize" the entire industry and stop destructive competition.[3] His method for doing this would be monopoly, his tactics hard-nosed.

ROCKEFELLER'S COMPETITIVE STRATEGIES

Rockefeller used a range of competitive strategies. He was a low-cost, high-volume producer. He used debt financing to expand. He attempted to make his refined petroleum products of high and consistent quality, since fly-by-night refiners turned out inferior distillates. Cheap kerosene with a low ignition point had burned many a home down after exploding in a wick lamp. When he incorporated the Standard Oil Company of Ohio in 1870, the name suggested a "standard oil" of uniformly good quality. He engaged in vertical integration by making wooden barrels. As time when on, he also bought pipelines, storage tanks, and railroad tank cars.

Critical to his success, however, was the art of strong-arming the railroads. In this, Rockefeller was the master. Transportation costs paid to railroads were important to refiners, who shipped in crude oil and then shipped out products such as kerosene or lubricating oil. In the 1860s railroads were highly competitive and often altered shipping rates to attract business. No law prohibited this and published rates were only the starting point of negotiations.

Railroads often granted *rebates* to shippers; that is, they returned part of the freight charge after shipment. These rebates were usually secret and given in return for the guarantee of future business. Large volume shippers, including oil refineries, got the biggest rebates. Standard Oil was no exception.

At this time, Rockefeller has been described by biographers as a prepossessing man with penetrating eyes who drove a hard bargain. He would take the measure of a person with a withering stare, and few were his match. He was formidable in negotiations because he was invariably informed in detail about the other's business. And he was still a pious churchgoer who read the Bible nightly before retiring.

Late in 1870 Rockefeller hatched a brazen plan for stabilizing the oil industry at the refining level. In clandestine meetings, he worked out a rebate scheme between a few major refiners and the three railroads going into the Pennsylvania oil regions. They gave this scheme an innocent-sounding name, the South Improvement Plan. In it, the railroads agreed to increase published rates for hauling oil. Then Rockefeller's Cleveland refineries and a few others would get large rebates on each barrel shipped. For example, the regular rate between the oil regions and Cleveland would be $.80 a barrel and between Cleveland and New York $2.00 a barrel. It would cost a total of $2.80 per barrel for any other refinery in Cleveland to bring in a barrel of crude oil and ship a barrel of refined oil to New York for sale or export. Rockefeller and his accomplices, on the other hand, would be charged $2.80 but then get a rebate of $.90.

In addition, the refineries participating in the South Improvement Plan received *drawbacks*, or payments made on the shipment of oil by competitors! Thus,

[3] Ron Chernow, *Titan: The Life of John D. Rockefeller, Sr.* (New York: Random House, 1998), pp. 130 and 149–52.

Rockefeller would be paid \$.40 on every barrel of crude oil his competitors shipped into Cleveland and \$.50 on every barrel of refined oil shipped to New York. Under this venal scheme, the more a competitor shipped, the more Rockefeller's transportation costs were lowered. While competitors were charged \$2.80 on the critical route (Pennsylvania oil regions–Cleveland–New York), Rockefeller paid only \$1.00. Moreover, the railroads agreed to give the conspirators waybills detailing competitors' shipments; a better espionage system would be hard to find.

Why did the railroads agree to this plot? There were several reasons. First, it removed the uncertainty of cutthroat competition. Oil traffic was guaranteed in large volume. Second, the refiners provided services to the railroads including tank cars, loading facilities, and insurance. And third, railroad executives received stock in the participating refineries, giving them a stake in their success.

The consequences of the South Improvement Plan were predictable. Nonparticipating refiners faced bloated transportation costs and would be uncompetitive. They had two choices. Either they could sell to Rockefeller and his allies, or they could stand on principle and go bankrupt. When they sold, as they must, the flaw in industry structure would be corrected. Rockefeller intended to acquire them, then close them or limit their capacity. This would give him market power to stabilize the price of both crude oil and refined products. And the rebates would be a formidable barrier to new entrants.

THE CONSPIRACY PLAYS OUT

In February of 1872 the new freight rates were announced. Quickly, the full design was revealed, causing widespread, explosive rage in the oil regions. Although it broke no laws, it overstepped prevailing norms. People believed that since railroads got their right-of-ways from the public they had a duty to serve shippers fairly. Volume discounts might be justified, but this shakedown was extortionate. Producers and refiners in the oil regions boycotted the conspirators and the railroads.

Rockefeller, seen as the prime mover behind the South Improvement Plan, was vilified in the industry and the press. His wife feared for his life. Yet he never wavered. "It was right," he said of the plan. "I knew it as a matter of conscience. It was right between me and my God."[4] As journalist Ida Tarbell noted, Rockefeller was not squeamish about such business affairs.

> Mr. Rockefeller was "good." There was no more faithful Baptist in Cleveland than he. Every enterprise of that church he had supported liberally from his youth. He gave to its poor. He visited its sick. He wept with its suffering. Moreover, he gave unostentatiously to many outside charities. . . . Yet he was willing to strain every nerve to obtain himself special and unjust privileges from the railroads which were bound to ruin every man in the oil business not sharing them with him.[5]

Within a month, the weight of negative public opinion and loss of revenue caused the railroads to cave in. They rescinded the discriminatory rate structure. All appearances were of a Rockefeller defeat, but appearances deceived. Rockefeller had moved quickly, meeting one by one with rival refiners, explaining the rebate scheme and its salutary effect on the industry, and asking to buy them out. He offered the exact value of the business in cash or, preferably, in Standard Oil Company stock.

By the time the railroads reset their rates, Rockefeller had bought out 21 of his 26 Cleveland competitors. Some acquisitions were simply dismantled to reduce surplus capacity. He now dominated Cleveland, the country's major refining center, and controlled more than a quarter of U.S. capacity. In secrecy, he negotiated a new rebate agreement with the Erie Railroad. Of these actions, Ida Tarbell noted sardonically: "He had a mind which, stopped by a wall, burrows under or creeps around."[6] Regardless of methods, he had, indeed, corrected structural flaws in the oil industry. It would attract more capital. If any circumstance cast a shadow over this striking victory, it was that public opinion had turned against him. From then on, he was reviled as an unfair competitor, hatred of him growing apace with his burgeoning wealth. He never understood why.

[4] Peter Collier and David Horowitz, *The Rockefellers: An American Dynasty* (New York: New American Library, 1976), p. 11.

[5] Ida M. Tarbell, *The History of the Standard Oil Company,* vol. 1 (Gloucester, MA: Peter Smith, 1963), p. 43.

[6] Ibid., p. 99.

ONWARD THE COURSE OF EMPIRE

Rockefeller, now 33, was wealthy. Yet he drove on, compelled to finish a grand design, to spread his pattern over the industry landscape, to conform it to his vision.

He continued the strategy of horizontal integration at the refinery level by absorbing more and more of his competitors. As the size of Standard Oil increased, Rockefeller gained added leverage over the railroads. Like an orchestra conductor he played them against each other, granting shares of the oil traffic in return for rebates that gave him a decisive advantage.

Some competitors stubbornly clung to their businesses, partly out of hatred for Rockefeller. He made them "sweat" and "feel sick" until they sold.[7] The fleets of tank cars that he leased to railroads were often "unavailable" to ship feedstock and distillates to and from such refiners. Rockefeller concealed many of his acquisitions, disguising the full sweep of his drive to monopoly. These companies were the Trojan horses in his war against rival refiners. They seemed independent but secretly helped to undermine Standard's competitors. Often they were at the center of elaborate pricing conspiracies involving code words in telegrams such as "doubters" for refiners and "mixer" for railroad drawbacks. The phantoms bought some refiners who refused in principle to sell out to Standard Oil. Their existence confronted independents with a dark, mysterious force that could not be brought into the light and fought.

THE STANDARD OIL TRUST

By 1882 Rockefeller's company was capitalized at $70 million and produced 90 percent of the nation's refining output. Its main product, illuminating oil, was changing the way people lived. Before the sale of affordable illuminating oil of good quality, most Americans went to bed with darkness. They could not afford expensive candles or whale oil and feared using the unstable kerosene made by early, small refiners. With the rise of Rockefeller's colossus, they had reliable, inexpensive light and stayed up. Their lives, and the life of the nation, changed.

Rockefeller reorganized Standard Oil as a trust.[8] His purpose was to make state regulation more difficult. Soon other large companies followed his lead, adopting the trust form to avoid government restrictions. Inside Standard Oil, Rockefeller's organizing skills were extraordinary. Working with a loyal inner circle of managers, he directed his far-flung empire from headquarters at 26 Broadway in New York City. As he absorbed his competitors, so had he co-opted the best minds in the industry and much of Standard's success is attributable to this stellar supporting cast. Though dominant, Rockefeller delegated great responsibility to his managers. High-level committees controlled business operations. He circulated monthly cost statements for each refinery, causing fierce internal competition among their managers that led to high performance. He set up a network of informants around the globe. Critics called them spies, but they functioned as a well-organized information system. A perfectionist, he insisted on having a statement of the exact net worth of Standard Oil on his desk every morning. Oil prices always were calculated to three decimals. He was so dogged about efficiency and recycling that his Standard Oil plants might win environmental awards were they operating today. At night he prowled the headquarters turning down wicks in oil lamps.

His management style was one of formal politeness. He never spoke harshly to any employee. Once, when a manager leaked information to the press, Rockefeller said to his secretary: "Suggest to Mr. Blank that he would do admirably as a newspaper man, and that we shall not need his services after the close of this month."[9] Compared with other moguls of that era, he lived simply. He had two large estates, in Cleveland and New York, but neither was too ostentatious. He read the Bible daily, continued regular attendance at a Baptist church, and gave generously to charities.

Rockefeller's organizing skills were critical to his success. Discussions often focus on his ethics, but the

[7] Abels, *The Rockefeller Billions*, p. 35.

[8] A trust is a method of controlling a number of companies in which the voting stock of each company is transferred to a board of trustees. The trustees then have the power to coordinate the operations of all companies in the group. This organizing form is no longer legal in the United States.

[9] Quoted in "A Great Monopoly's Work: An Inner View of the Standard Oil Company," *New York Times*, February 27, 1883, p. 1.

key to Standard Oil's long-term domination lay elsewhere. The company was an immense, organized force opposed only by smaller, less united adversaries. Its success came from centralized, coordinated effort. Compromising methods, to the extent they were used, were of far less importance. [10]

EXTENDING DOMINATION

By the 1880s Standard Oil had overwhelming market power. Its embrace of refining activity was virtually complete, and it had moved into drilling, pipelines, storage tanks, transportation, and marketing of finished products. By now the entire world was addicted to kerosene and other petroleum products, and Standard's international sales grew.

Rockefeller's dominating competitive philosophy prevailed. His marketing agents were ordered to destroy independent suppliers. To suppress competition, his employees pioneered fanatical customer service. The intelligence-gathering network paid competitors' employees to pass information to Standard Oil. Railroad agents were bribed to misroute shipments. Standard workers climbed on competitors' tank cars and measured the contents. Price warfare was relentless. A stubborn competitor often found Standard selling kerosene to its customers at a price substantially below production cost.

Rockefeller himself was never proved to be directly involved in flagrant misconduct. He blamed criminal and unethical actions on overzealous subordinates. His critics thought the strategy of suffocating small rivals and policies such as that requiring regular written intelligence reports encouraged degenerative ethics among his minions.

Rockefeller saw Standard Oil as a stabilizing force in the industry and as a righteous crusade to illuminate the world. How, as a good Christian devoted to the moral injunctions of the Bible, was Rockefeller able to suborn such vicious behavior in commerce? One biographer, Allan Nevins, gives this explanation:

> From a chaotic industry he was building an efficient industrial empire for what seemed to him the good not only of its heads but of the general public. If he relaxed his general methods of warfare . . . a multitude of small competitors would smash his empire and plunge the oil business back to chaos. He always believed in what William McKinley called "benevolent assimilation"; he preferred to buy out rivals on decent terms, and to employ the ablest competitors as helpers. It was when his terms were refused that he ruthlessly crushed the "outsiders." . . . It seemed to him better that a limited number of small businesses should die than that the whole industry should go through a constant process of half-dying, reviving, and again half-dying.[11]

THE STANDARD OIL TRUST UNDER ATTACK

Standard Oil continued to grow, doubling in size before the turn of the century and doubling again by 1905.[12] Eventually its very size brought a flood of criticism that complicated operations. Predatory monopoly was at odds with prevailing beliefs about individual rights and free competition. The states tried to regulate Standard Oil and filed antitrust suits against it. Overwrought muckrakers lashed out at Rockefeller. Because of him, wrote one, "hundreds and thousands of men have been ruined."[13] Rockefeller was the personification of greed in political cartoons. Politicians not suborned by his bribery lambasted him.

Rockefeller, by now the richest American, was shaken by public hatred. He hired bodyguards and slept with a revolver. Pinkerton detectives were present at church on Sundays to handle the gawkers and shouters who appeared. He developed a digestive ailment so severe that he could eat only a few bland foods, and upon his doctor's advice he stopped daily office work. By 1896 he appeared only rarely at 26 Broadway. Soon he was afflicted with a nervous disorder and lost all his hair.

As attacks on Rockefeller grew, the vise of government regulation tightened on his company. A swarm of lawsuits and legislative hearings hung about it. Finally, in 1911, the Supreme Court ordered its breakup under the Sherman Antitrust Act, holding that its monopoly position was an "undue" restraint on trade

[10] David M. Chalmers, ed., "Introductory Essay," in Ida M. Tarbell, *The History of the Standard Oil Company, Briefer Version* (Mineola, NY: Dover, 2003), pp. xvii–xviii.

[11] Allan Nevins, *Study in Power: John D. Rockefeller,* vol. 2 (New York: Scribner, 1953), p. 433.

[12] Ibid., app. 3, p. 478.

[13] Henry Demarest Lloyd, "Story of a Great Monopoly," *The Atlantic,* March 1881, p. 320.

that violated the "standard of reason."[14] The company was given six months to separate into 39 independent firms. The breakup consisted mainly of moving the desks of managers at 26 Broadway and was a financial windfall for Rockefeller, who received shares of stock in all the companies, the prices of which were driven up by frenzied public buying. Before the breakup kerosene sales had buoyed the company. However, just as electric light bulbs were replacing oil lamps, the automobile jolted demand for another petroleum distillate—gasoline. Rockefeller, who was 71 at the time of the breakup and would live another 26 years, earned new fortunes simply by maintaining his equity in the separate companies.

Rockefeller remained a source of fascination for the American public. As *The Wall Street Journal* noted, "[t]he richest man in a world where money is power is necessarily a fascinating object of study."[15] This being so, it was his enduring misfortune that muckraking journalist Ida Tarbell turned her gaze on him.

Tarbell wrote two unflattering character studies and a detailed, two-volume biography of Rockefeller, all serialized in the widely read *McClure's Magazine* between 1902 and 1905. Her unsentimental words were no less ruthless than the actions of the old man himself. Although admitting that Rockefeller and Standard Oil had some measure of "legitimate greatness," she was obsessed with his flaws. In one essay she found "something indefinably repulsive" in his appearance, writing that his mouth was "the cruelest feature of his face," and that his nose "rose like a thorn."[16] Such ad hominem attacks lacked merit but, in addition, Tarbell delved deeply into Rockefeller's career, producing narratives of exquisite detail. The thesis she conveyed to the public was that by his singular example, Rockefeller was responsible for debasing the moral tone of American business. She believed his story incited legions of the ambitious to use cold-blooded methods, teaching them that success justifies itself. Like the master, the junior scoundrels often cited biblical verse to support their actions.

Few public figures have a nemesis such as Ida Tarbell. Her relentless pen, along with others, deprived him of some public adulation he may have craved and her scholarship permanently defined him. Her intricate period research cannot be duplicated and subsequent biographers, even more friendly ones, must go to it for insight. Rockefeller may or may not have deserved such a definitive hand. He called her a "poisonous woman." [17]

THE GREAT ALMONER

Since childhood Rockefeller had made charitable donations and, as his fortune accumulated, he increased them. After 1884 the total was never less than $100,000 a year, and after 1892 it was usually over $1 million and sometimes far more. In his mind, these benefactions were linked to his duty as a good Christian to uplift humanity. To a reporter he once said:

> I believe the power to make money is a gift from God—just as are the instincts for art, music, literature, the doctor's talent, yours—to be developed and used to the best of our ability for the good of mankind. Having been endowed with the gift I possess, I believe it is my duty to make money and still more money and to use the money I make for the good of my fellow-man according to the dictates of my conscience.[18]

Over his lifetime, Rockefeller gave gifts of approximately $550 million. He gave, for example, $8.2 million for the construction of Peking Union Medical College in response to the need to educate doctors in China. He gave $50 million to the University of Chicago. He created charitable trusts and endowed them with millions. One such trust was the General Education Board, set up in 1902, which started 1,600 new high schools. Another, the Rockefeller Sanitary Commission, succeeded in eradicating hookworm in the South. The largest was the Rockefeller Foundation, established in 1913 and endowed with $200 million. Its purpose was "to promote the well-being of mankind throughout the world." Rockefeller always said, however, that the greatest philanthropy of all was developing the earth's natural resources and employing people. Critics greeted his gifts with skepticism, thinking them atonement for years of plundering American society.

In his later years, Rockefeller lived a secluded, placid existence on his great Pocantico estate in

[14] *Standard Oil Company of New Jersey v. United States,* 31 U.S. 221. It was an 8–1 decision.

[15] "Incarnate Business," *The Wall Street Journal,* June 26, 1905, p. 1.

[16] Ida Tarbell, "John D. Rockefeller: A Character Study," *McClure's,* August 1905, p. 386.

[17] Chernow, *Titan: The Life of John D. Rockefeller, Sr.,* p. xxii.

[18] Quoted in Abels, *The Rockefeller Billions,* p. 280.

John D. Rockefeller at age 65. This photograph was taken shortly after a disease, generalized alopecia, caused him to lose his hair. Source: Library of Congress, Prints and Photographs Collection, LC-USZ62-123825.

New York, which had 75 buildings and 70 miles of roads. As years passed, the public grew increasingly fond of him. Memories of his early business career dimmed, and a new generation viewed him in the glow of his huge charitable contributions. For many years, he carried shiny nickels and dimes in his pockets to give to children and well-wishers. On his 86th birthday he wrote the following verse.

> I was early taught to work as well as play,
> My life has been one long, happy holiday;
> Full of work and full of play—
> I dropped the worry on the way—
> And God was good to me every day.

He died in 1937 at the age of 97. His estate was valued at $26,410,837. He had given the rest away.

Questions

1. With reference to the levels and spheres of corporate power discussed in the chapter, how did the power of Standard Oil change society? Was this power exercised in keeping with the social contract of Rockefeller's era?
2. How does the story of Standard Oil illustrate the limits of business power? Does it better illustrate the dominance theory or the pluralist theory discussed in the chapter?
3. Did Rockefeller himself ever act unethically? By the standards of his day? By those of today? How could he simultaneously be a devout Christian and a ruthless monopolist? Is there any contradiction between his personal and business ethics?
4. In the utilitarian sense of accomplishing the greatest good for the greatest number in society, was the Standard Oil Company a net plus or a minus? On balance, did the company meet its responsibilities to society?
5. Did strategies of Standard Oil encourage unethical behavior? Could Rockefeller's vision have been fulfilled using "nicer" tactics?

Chapter Four

Critics of Business

Mary "Mother" Jones

In the early years of the twentieth century Mary Jones (1837–1930), known as Mother Jones, was one of the most notable women in America. Emerging from personal tragedy, she created a singular persona and hurled herself against big corporations and the capitalist system that sustained them. Hers was an era of great change, dissent, and conflict. It was the ideal stage for a defiant performance.

She was born in 1837 as Mary Harris in Cork, Ireland. When she was eight years old, a fungus blighted the nation's potato crop, causing a terrible famine. She emigrated with her family to Toronto and there grew up, graduated from a convent school, and became a schoolteacher. Eventually she moved to Memphis and married an iron molder named George Jones. Between 1862 and 1867 they had four children. She devoted herself to cooking, cleaning, and sewing for the family. Then yellow fever struck.

The deadly epidemic came in the fall of 1867. As mortality rose, rich families left town, leaving those who could not afford travel to become victims. The sounds of death carts taking bodies away filled neighborhoods. Mary Jones describes what happened to her.

> All about my house I could hear weeping and the cries of delirium. One by one, my four little children sickened and died. I washed their little bodies and got them ready for burial. My husband caught the fever and died. I sat alone through nights of grief. No one came to me. No one could.[1]

She nursed the sick until the plague ended, then returned to Chicago to set up a dressmaking business. She often worked for wealthy society matrons.

> I had ample opportunity to observe the luxury and extravagance of their lives. Often while sewing for the lords and barons who lived in magnificence on the Lake Shore Drive, I would look out of the plate glass windows and see the poor, shivering wretches, jobless and hungry, walking along the frozen lake front. The contrast of their condition with that of the tropical comfort of the people for whom I sewed was painful to me. My employers seemed neither to notice nor to care.[2]

[1] Mary Field Parton, ed., *The Autobiography of Mother Jones* (Chicago: C. H. Kerr, 1925), p. 12.
[2] Ibid., chap. 1, p. 13.

Several years passed, then in 1871 the Great Chicago Fire burned her business and left her destitute. After the fire she attended evening meetings of the Knights of Labor, an early union, and became engrossed in the fight of industrial workers for better wages and conditions. The perspective of class war began to dominate her view of society. She felt that workers were enslaved by corporate employers and by the corrupt politicians and judges who did their bidding. She believed that only by overthrowing capitalism could the laboring class end its bondage and usher in a new day of socialism, so she joined a small socialist political party.

For almost two decades Mary Jones worked in obscurity for labor causes and during this time she created the persona that would make her powerful and famous. Mary Jones became Mother Jones. The loss of her own family had freed her to take on another, to adopt the downtrodden. In an era when women had no vote, held no leadership positions, and received no encouragement to speak up, she would use this metaphor of motherhood to give her power.

She rose to prominence as an organizer for the United Mine Workers. Horrible working conditions prevailed in coal mines. Miners worked 10- and 12-hour days in damp, dusty, cramped, dangerous tunnels. Wages were so low that to get by mining families put their children to work. Boys as young as eight years old toiled six or seven days a week, some spending so many hours in cramped shafts that their bones grew irregularly and they could not stand straight as adults. Textile mills were built near mining towns to employ the miners' wives and daughters. The United Mine Workers wanted to unionize the miners, but the coal companies viciously resisted. Organizers were followed and observed. Miners who shook an organizer's hand were fired. Hired thugs beat up troublemakers. Companies had friendly judges convene lunacy hearings and commit prounion employees to asylums. The miners wanted unions, but they were intimidated.

In the late 1890s Mother Jones arrived in Pennsylvania coal country. At 60 years old she looked like a grandmother. She stood five feet tall with silver hair and sharp blue eyes. With great energy she worked the coal towns. She was an explosive orator with a vocal range from shrill cries to a forceful, low pitch that mesmerized listeners. She knew the miners' language and spoke in colorful terms, calling mine owners "a crew of pirates," "a gang of thieves," and "cowards." She called the men her "boys" and as their "mother" told them to stand up to the companies.

During a bitter strike in 1900 when some miners were losing their nerve she organized marches of the miners' wives. The women paraded to work sites wearing aprons, waving mops, and banging pans. Laughing company guards saw no danger from the comical processions and let them through, not realizing how Mother Jones had cleverly dramatized the role of aggrieved wives and mothers fighting for the welfare of their families. She scolded the men, telling them they were shamed if their wives stood up to the companies and they did not.

Mother Jones used ironic wit to puncture establishment pretensions. In 1902 she was arrested in West Virginia after the coal companies got an injunction against union organizing. In court, the judge suspended her sentence, but advised her that because she was a woman it would be "better far for her to follow the lines and paths which the Allwise Being intended her sex should pursue." She appreciated the advice, she said, adding that it was no surprise he was taking the company's side, since

Mary "Mother" Jones. Source: Library of Congress, Prints and Photographs Collection, LC-USZ62-7678.

experience had taught her that "robbers tend to like each other."[3] When asked by a Princeton professor to address his class, she brought with her a stooped and pale 10-year-old boy. "Here's a textbook on economics," she said. "He gets three dollars a week . . . [working] in a carpet factory ten hours a day while the children of the rich are getting higher education."[4] She had a favorite story for audiences: "I asked a man in prison once how he happened to get there. He had stolen a pair of shoes. I told him that if he had stolen a railroad he could be a United States Senator."[5]

Eventually, Mother Jones fell out with the United Mine Workers because she was more militant than its leadership. She became a lecturer for the Socialist Party, but in time she renounced socialism. She was a doer, not an ideologue, and she lacked patience with hairsplitting doctrinal debates among intellectuals who led comfortable lives. However, in 1905 she helped launch the International Workers of the World (IWW), a radical union dedicated to overthrowing American capitalism. By 1911 she had returned to the front lines in mining regions. Later, she marched with striking

[3] Gene R. Nichol, Jr., "Fighting Poverty with Virtue," *Michigan Law Review,* May 2002, p. 1661.

[4] Quoted in Marilyn Jurich, "The Female Trickster—Known as Trickstar—As Exemplified by Two American Legendary Women, 'Billy' Tipton and Mother Jones," *Journal of American Culture,* Spring 1999, p. 69.

[5] "Mother Jones Speaks to Coney Island Crowd," *New York Times,* July 27, 1903.

garment and streetcar workers in New York City. In 1916 she started a riot by two hundred wives of streetcar workers with an inflammatory speech, telling them: "You ought to be out raising hell."[6]

By the 1920s Mother Jones had grown disillusioned with unions. She quit the IWW saying it was more interested in symbolic displays than in concrete victories. Other unions had grown comfortable with the corporate establishment. She had contempt for union leaders motivated by their own status and importance in society and called John L. Lewis, president of the United Mine Workers, a "pie counter hunter."[7] She retired from public life, speaking out now and then, and died in 1930 at the age of 92.

Today Mother Jones is little remembered. Her time passed and the specific labor abuses that enraged her are mostly ended. Perhaps her invective is unmatched today. She defined "monster capitalism," as a "robber system" supported by the "national gang of burglars of Wall Street." The corporations she attacked had "snake brains" and were run by "idiots" and "commercial pirates." But her ideas live on. Although her life was unique in its tragedy and drama, her attacks were based on enduring values that recycle through time. We may forget Mother Jones, but we hear her in today's business critics. In this chapter we explore the birth and life of these values.

ORIGINS OF CRITICAL ATTITUDES TOWARD BUSINESS

There are two underlying sources of criticism of business, one ancient and the other modern. The first is the belief that people in business place profit before more worthy values such as honesty, truth, justice, love, piety, aesthetics, tranquillity, and respect for nature. The second is the strain placed on societies by economic development. During industrialization and later, when market economies grow large and complex, business has a range of problematic impacts on societies. We will discuss both fundamental sources of criticism. We begin in the ancient Mediterranean world.

The Greeks and Romans

agrarian society
A society with a largely agricultural economy.

The earliest societies were agrarian in nature. An *agrarian society* is a preindustrial society in which economic, political, and cultural values are based on agricultural experience. In these societies, most people worked the land for subsistence. No industrial centers or mass markets existed, so business activity beyond barter and exchange was a tiny part of the economy. The activities of merchants were often thought unprincipled because their sharp trading practices clashed with the traditional, more altruistic values of family and clan relations among farmers. Merchants typically had lower class status than officials, farmers, soldiers, artisans, and teachers.

The extraordinary civilizations of ancient Greece and Rome were based on subsistence agriculture. Economic activity by merchants, bankers, and manufacturers was limited. The largest factory in Athens, for example, employed 120 workers

[6] "Car Riot Started by 'Mother' Jones," *New York Times*, October 6, 1916, p. 1.

[7] Quoted in Elliot J. Gorn, Mother Jones: *The Most Dangerous Woman in America* (New York: Hill and Wang, 2001), p. 249.

making shields.[8] Commercial activity was greater in Rome, but it was still mainly an agrarian society. Perhaps because industry was so limited in both societies, inaccurate economic doctrines arose to explain commercial activity.[9] For example, the desire for riches was suspect due to the popular belief that the amount of wealth was fixed. If so, an individual accumulated wealth only by subtracting from the share of others. This is believable logic in an agrarian society because the land on which the economy is based is fixed in amount.

Philosophers moved into this realm of intellectual error, reasoning that profit seeking was an inferior motive and that commercial activity led to excess, corruption, and misery. Their views are of lasting significance because, as with many topics of discourse in Western civilization, they first defined the terms of debate over the ranking of profit relative to other values. In particular, both Plato and Aristotle articulated the fundamental indictment that casts an everlasting shadow over business.

Plato believed that insatiable appetites existed in every person. These could be controlled only by inner virtues painstakingly acquired through character development. The pursuit of money was one such appetite, and Plato thought that when people engaged in trade they inevitably succumbed to the temptation of excess and became grasping. In a society, as with an individual, wealth spawned evils, including inequality, envy, class conflict, and war. "Virtue and wealth," he argued, "are balanced against one another in the scales."[10] Rulers of the utopian society he conceived in *The Republic* were prohibited from owning possessions for fear they would be corrupted and turn into tyrants. So troubled was he about this that they were forbidden even to touch gold or silver.

Aristotle believed there was a benign form of acquisition that consisted of getting the things needed for subsistence. This kind of acquisition was natural and moderate. However, after trading and monetary systems arose, the art of acquisition was no longer practiced this simple way. Instead, merchants studied the techniques of commerce, figuring out how to make the greatest profit, seeking not the necessities, but unlimited pools of money. Aristotle thought this was a lower form of acquisition because it was activity that did not contribute to inner virtue.

For Aristotle, happiness is the ultimate goal of life. It comes to those who develop character virtues such as courage, temperance, justice, and wisdom. He called these virtues "goods of the soul" and held them superior to "external goods," which he defined as possessions and money. Aristotle believed that the amount of happiness a person gained in life was equal to the amount of virtue accumulated in the soul. Since material possessions beyond those needed for subsistence added nothing to the store of virtue in the soul, it followed that they contributed nothing to happiness; thus, it was a waste or "perversion" of any virtue to apply it toward the acquisition of excess. "The proper function of courage, for example, is not to produce money but to give confidence," he wrote.[11]

[8] Will Durant, *The Life of Greece* (New York: Simon & Schuster, 1939), p. 272.

[9] John Kenneth Galbraith, *Economics in Perspective* (Boston: Houghton Mifflin, 1987), pp. 9–10.

[10] *The Republic,* trans. F. M. Cornford (New York: Oxford University Press, 1945), p. 274.

[11] In *Politics,* trans. Ernest Barker (New York: Oxford University Press, 1962), book I, chap. X, § 17. See also book VII, chap. 1, §§ 1–10.

Thus, both Plato and Aristotle relegated the profit motive to the sphere of lower or base impulses, a place from which it would not escape for centuries and then only partially. Soon, Roman law would forbid the senatorial class from making business investments (and the law would be widely circumvented). Likewise, the Stoic philosophers of Rome, including Epictetus and Marcus Aurelius, taught that the truly rich person possessed inner peace rather than capital or property. "Asked, 'Who is the rich man?' Epictetus replied, 'He who is content.'"[12] These sages looked down on merchants of their day as materialists who, in pursuit of wealth, sacrificed character development. Of course, this did not deter the merchants from accumulating fortunes and neglecting the study of ideals. The scornful ethos of the philosophers, though potent enough to endure and to beget perennial hostility, has never had enough power to suppress the tide of commerce.

The Medieval World

During the Middle Ages, the prevailing theology of the Roman Catholic Church was intolerant of profit seeking. As the Christian religion arose, its early practitioners had been persecuted by the wealthy and corrupt ruling class of Rome. The Church, then, rejected a focus on wealth and sought special status for the poor. Saint Augustine, the towering figure of early Church doctrine, accepted the idea that material wealth was fixed in supply. To become rich, a person necessarily sinned by accumulation that violated the natural equality of Creation. Moreover, the love of material things was a snare that pulled the soul away from God.[13]

just price
A price giving a moderate profit; one inspired by fairness, not greed.

market price
A price determined by the interaction of supply and demand.

usury
The lending of money for interest.

Protestant ethic
The belief that hard work and adherence to a set of virtues such as thrift, saving, and sobriety would bring wealth and God's approval.

The Church's most definitive theologian, St. Thomas Aquinas, was greatly influenced by the ideas of Aristotle when he set forth Church canon about the ethics of profit making and lending money. Merchants were exhorted to charge a *just price* for their wares, a price that incorporated a modest profit just adequate to maintain them in the social station to which they were born. The just price stands in contrast to the modern idea of a *market price* determined by supply and demand without any moral dimension. Today we hear echoes of medieval theology when consumers complain that high prices for a scarce product are unjust. Catholicism also condemned *usury*, or the lending of money for interest. By the twelfth and thirteenth centuries, however, the money supply and economic activity had greatly expanded and interest-bearing loans were commonplace. "Commercial activity," notes historian Will Durant, "proved stronger than fear of prison or hell."[14] In time, the Church backed away from the dogma of just price and usury. It was a slow process. Church teaching making lending money for interest a sin was not officially renounced until 1917.

The Modern World

As business activity accelerated during the Renaissance, new theories arose to justify previously condemned practices. Two are of great importance. First, is the rise of the *Protestant ethic* in the sixteenth century. The Protestant reformers Martin

[12] *The Golden Sayings of Epictetus*, trans. Hastings Crossley, in Charles W. Eliot, ed., *Plato, Epictetus, Marcus Aurelius* (Danbury, CT: Grolier, 1980), p. 179.

[13] Saint Augustine, *The City of God*, trans. Gerald G. Walsh et al. (New York: Image Books, 1958), book XIX, chap. 17. This work was completed in A.D. 426.

[14] *The Age of Faith* (New York: Simon & Schuster, 1950), p. 631.

Luther and John Calvin believed that work was a means of serving God and that if a person earned great wealth through hard work it was a sign of God's approval. This confronted the Church's antagonism toward commerce with a new doctrine that removed moral suspicion of wealth. It contradicted the belief that pursuit of money corrupted the soul. Second, in 1776 Adam Smith published his theory of capitalism, writing that free markets harnessed greed for the public good and protected consumers from abuse. This defied the Church's insistence on the idea of a just price. Moreover, visible wealth creation in expanding economies forcefully countered the notion that only a more or less fixed amount of wealth existed in a society. These developments ended the domination of doctrines that made business activity seem faintly criminal and released new energies into commerce. But the broom of doctrinal reform failed to make a clean sweep, and many business critics clung to the old approbations of the Greek philosophers and of the Church.

In addition, just when old strictures were loosening, the industrial revolution created new tensions that reinforced critical attitudes about business. These new tensions arose as inventions and industries transformed agrarian societies and challenged traditional values with modern alternatives. During industrialization, rural, slow-paced, stable societies are swiftly and dramatically altered. They become urban and fast-paced. More emphasis is placed on material things and people's values shift. Wealth creation overwhelms self-restraint. Consumption supplants thrift and saving. Conquest of nature replaces awe of nature.

THE AMERICAN CRITIQUE OF BUSINESS

As societies modernize, the antiquarian values of Greece live on in the charges of critics who are troubled by these changes. Always, the fundamental critique is altered to fit current circumstances. We will see how this happened in the United States.

The Colonial Era

The American nation was colonized by corporations. The colonists who landed at Jamestown, Virginia, in 1606 were sponsored by investors in the London Company, who hoped to make a fortune by discovering gold in the New World. Instead, the colonists found a mild strain of native tobacco that caused a sensation in England (and became the basis for the plantation economy that would rise in the South). The Pilgrims who came in the *Mayflower* to Cape Cod, Massachusetts, in 1620 had fled persecution to set up a religious colony. But their voyage was financed by the Plymouth Company, whose backers sought to make a profit. To repay their debt and to buy manufactured goods they exported furs and forest products such as timber, tar, and turpentine. In this way the early colonists became lively traders.

As international trade in coastal regions expanded, settlers moved inland, creating a broad agrarian base for the economy. These frontier farms seethed with profit-oriented activity. Unlike European peasants, American farmers owned their land and this turned them into little capitalists. Most tried to make money by raising crops for market. Some were land speculators. Others built and ran grain mills and in other ways employed their capital like the traders and merchants in towns.

The popular theoretician of the rising capitalist spirit was Benjamin Franklin (1706–1790). Franklin began a business career at the age of 22 by opening a printing shop. He then bought several newspapers and retired rich at the age of 42. During travels in Europe he became acquainted with Adam Smith, who shared parts of the manuscript for *Wealth of Nations* with him. Franklin came to accept Smith's then-radical views on the superiority of laissez-faire markets. Writing prolifically, Franklin gave form to a new American business ethos.

In 1732 he published the first annual *Poor Richard's Almanack*, an eclectic book of facts, information, and self-help advice. Over many years the *Almanack* carried aphorisms and maxims about the road to success in business, a road open to all who practiced virtues such as hard work, thrift, and frugality. "The sleeping Fox catches no Poultry." "Lost Time is never found again." "Diligence is the Mother of Good Luck." "The Art of getting Riches consists very much in Thrift."[15]

Unlike the Old World theologians who taught that commercial success was slightly sinful, Franklin taught that God would approve the pursuit of self-interest and wealth. "God gives all things to Industry."[16] He made business activity synonymous with traditional virtues and released it from moral suspicion. His teaching resonated with the American condition and he became the prophet of a vibrant economy. Not surprisingly, his *Almanacks* were best sellers.

The Young Nation

The amalgam of a new land, a new people, and new thinking generated an early emphasis on business activity and material progress. Yet not everyone felt this was either inevitable or proper and dissent soon emerged. After independence in 1783 business interests were important in the new nation but not to the extent that they would be in time. There were few large companies. The economy was 90 percent agricultural, so the interests of farmers and planters dominated those of infant industry. A major debate arose over the direction of the economy, one that would define subsequent debate between business and its critics in America. It was played out in a bitter rivalry between two members of President George Washington's cabinet who differed both in temperament and ideas.

Alexander Hamilton (1755–1804), the first secretary of the treasury, was young, ambitious, brilliant, and inclined to action. He believed that industrial growth would increase national power and designed a grand scheme to promote manufacturing and finance. He was an arrogant, aloof leader who mistrusted the wisdom of common citizens. Having once said that "the people is a great beast," he favored rule by an economic elite.[17] Hamilton got Congress to approve his plans for taxation, debt financing, tariffs to protect infant industry, and creation of a national bank, setting a policy of industrialization in motion.

[15] Quotations are in *Poor Richard's Almanack*, 1749, and "The Way to Wealth," Preface to *Poor Richard Improved*, 1758, in Nathan G. Goodman, ed., *The Autobiography of Benjamin Franklin and Selections from his other Writings* (New York: Carlton House, 1932), pp. 198, 206, 207.

[16] Ibid., "The Way to Wealth," p. 207.

[17] Quoted in Vernon Louis Parrington, *Main Currents in American Thought*, vol. 1 (New York: Harcourt, Brace, 1958), p. 300; originally published in 1927.

He was opposed by Secretary of State Thomas Jefferson (1743–1826), one of America's most original and philosophical minds. Jefferson was a shy man who avoided conflict. His thinking achieved great depth, but he was less a man of action than Hamilton. His weakness as a manager is summed up in a revealing statement. "We can only be answerable for the orders we give, and not for their execution."[18] He had grown up in sparsely populated frontier areas of Virginia, never having seen a village of more than 20 houses until he was 18 years old. Awed by the common sense and resourcefulness of the settlers he knew, he formed the opinion that an agrarian economy of landowning farmers was the ideal social order.

Reading books as much as 15 hours a day, he gathered arguments to reinforce his convictions. According to Jefferson, America should aspire to spread farming over its immense, unsettled territory. He wrote that God placed "genuine virtue" in farmers, His chosen people. Manufacturing as an occupation "suffocates the germ of virtue," leads to venality, and corrupts the "manners and principles" of those who work at it.[19] He believed that an agrarian economy would prevent the rise of subservience to the wealthy and bring a state of equality, basic justice, and concern for the common good. Jefferson was well-read in Greek philosophy and it was no coincidence that he echoed the admonitions against commerce found in Plato and Aristotle. Even as he restated the Greeks, he laid the ground for more than two centuries of American business critics to follow.

Jefferson did not prevail. His agrarian ideal was fated to exist in the shadows of industrial growth. His theory of a nation of small farmers was somewhat nebulous and idealistic. As a policy it was no match for the more concrete design that Hamilton sold to Congress with great energy, a design that was surely more in tune with economic forces afoot in the young nation. With the support of business leaders, Hamilton carried out a bold, visionary program to stimulate the growth of manufacturing. His actions prepared the ground for the unexampled industrial growth that roared through the next century. He so angered Jefferson that the two rarely spoke even as they served together in George Washington's cabinet. Each had many followers and the conflict between their positions created not only the basis for subsequent criticism of business, but the basic cleavage that has prevailed in the American two-party system to the present.

1800–1865

The first half of the nineteenth century saw steady industrial growth. This aroused critics who clung to the values and life of the agrarian society that was fading before their eyes. Early in the century banking and manufacturing expanded. Markets were opened by tens of thousands of miles of new turnpikes. Completion of the 350-mile-long Erie Canal in 1825 inspired another 4,400 miles of canals to transport goods over water.[20] Railroads started to run in the 1830s. Immigrants arrived and cities grew. Business boomed.

[18] Letter to Baron F. W. von Stueben, March 10, 1781, quoted in Stanley Elkins and Eric McKitrick, *The Age of Federalism* (New York: Oxford University Press, 1993), p. 206.

[19] Quotes are from *Notes on Virginia*, in Adrienne Koch and William Peden, *The Life and Selected Writings of Thomas Jefferson* (New York: Random House, 1944), p. 280; first published in 1784.

[20] James Oliver Robertson, *America's Business* (New York: Hill and Wang, 1985), p. 81.

As the force of events put capitalism in control, agrarian romantics were pushed to the side, having only the power to object as cherished values were eroded. "Commerce," complained Ralph Waldo Emerson in 1839, "threatens to upset the balance of man and establish a new, universal Monarchy more tyrannical than Babylon or Rome."[21] Later, his friend Henry David Thoreau wrote to belittle a society in which this commerce smothered the poetry and grace of everyday life.

> This world is a place of business. What an infinite bustle! I am awakened almost every night by the panting of the locomotive. It interrupts my dreams. There is no sabbath. It would be glorious to see mankind at leisure for once. It is nothing but work, work, work. I cannot easily buy a blank-book to write thoughts in; they are commonly ruled for dollars and cents. . . . I think that there is nothing, not even crime, more opposed to poetry, to philosophy, ay, to life itself, than this incessant business.[22]

Among those who rejected capitalism, some tried to create alternative worlds. Beginning in the 1820s there was a frenzy of utopia building. Small bands of people who disdained the values prized in industrial society—materialism, competition, individualism, and tireless labor—built model communities intended to act as beacons for a better way. The largest was New Harmony, Indiana, founded in 1825 by Robert Owen (1771–1858), an English industrialist. Owen ran a large cotton mill in Scotland that had become a model for fair treatment of workers. Yet he believed that human values were corrupted by factory work and life in capitalist societies. He aspired to show that a society based on principles of equality, charity, cooperation, and moderation could flourish. At New Harmony money was abolished and the residents shared the fruits of communal labor.

Owen called his creation a "socialist" system and in the 1820s the term "socialism" first came into widespread use as a reference to Owen's philosophy. He started several other socialist communities and his ventures inspired others to form utopias based on socialist principles. More than 100 such communities appeared between 1820 and 1850.[23] A few were successful. The Oneida Community in New York lasted thirty-one years from 1848 to 1879. But most floundered, on average in less than two years.[24]

New Harmony emptied after only four years. Like other utopias it required businesslike activities for subsistence, but it attracted more loafers than skilled farmers and artisans who, in any case, could command higher material rewards in the outside world. After their initial zeal wore off, the sojourners tired of spartan living, regimentation, and rules to enforce cooperation. Most communes had programs to infuse socialist values into human natures tainted by capitalist schooling. Rarely did this work. One indication is that pilfering of supplies from common storehouses was common.

[21] Quoted from Emerson's *Journals,* vol. V, pp. 284–86, in Parrington, *Main Currents in American Thought,* vol. I, p. 386.

[22] "Life without Principle," *The Atlantic Monthly,* October 1863, pp. 484–85.

[23] W. Fitzhugh Brundage, *A Socialist Utopia in the New South* (Urbana: University of Illinois Press, 1996), p. 6.

[24] Joshua Muravchik, *Heaven on Earth: The Rise and Fall of Socialism* (San Francisco: Encounter Books, 2002), p. 51.

The agrarian and socialist communes failed utterly as alternatives to the bustling capitalism beyond their margins. Although a few new ones appeared as late as the 1890s, by the 1850s the idea had run its course. It failed in practice because it was based on romantic thinking, not on sustaining social forces. A series of withered utopias and a growing consensus on capitalist values adjourned the experiments. Socialism would return, but it awaited a new day and new ideas.

Populists and Progressives

At the end of the Civil War in 1865, America was still a predominantly rural, agrarian society of small, local businesses. But explosive industrial growth rapidly reshaped it, creating severe social problems in the process. Cities grew as farmers left the land and immigrants swelled slum populations. Corrupt political machines ran cities but failed to improve parlous conditions. Companies merged into huge national monopolies. These changes were the raw material of two movements critical of big business.

populist movement A political reform movement that arose among farmers in the late 1800s. Populists blamed social problems on industry and sought radical reforms such as government ownership of railroads.

The first was the *populist movement,* a farmers' protest movement that began in the 1870s and led to formation of a national political party, the Populist Party, which assailed business interests until its decisive defeat in the presidential election of 1896. The movement arose soon after the Civil War, when farmers experienced falling crop prices. The declines were due mainly to overproduction by mechanized farm machinery and to competition from foreign farmers exploiting new transport technologies. Farmers overlooked these factors and blamed their distress on railroad companies, the largest businesses of the day, which frequently overcharged for crop hauling, and on "plutocrats" such as J. P. Morgan and other eastern bankers who controlled the loan companies that foreclosed on their farms.

In a typical tirade, Mary Lease, a populist orator who whipped up crowds of farmers at picnics and fairs, explained:

> Wall Street owns the country. It is no longer a government of the people, by the people and for the people, but a government of Wall Street and for Wall Street. The great common people of this country are slaves, and monopoly is the master. The West and South are bound and prostrate before the manufacturing East.[25]

To solve agrarian ills, the populists advocated government ownership of railroad, telegraph, and telephone companies and banks, a policy dagger that revealed their fundamental rejection of capitalism. They demanded direct election of U.S. senators, who at the time were picked by state legislatures corrupted with money from big business. And to ease credit they sought to abandon the gold standard and expand the money supply.

Historian Louis Galambos believes that despite the populist critique, there existed a great reservoir of respect for and confidence in business until the late 1880s.[26] After that, analysis of newspaper and magazine editorials shows mounting

[25] In John D. Hicks, *The Populist Revolt* (Minneapolis: University of Minnesota Press, 1931), p. 160.

[26] Louis Galambos, *The Public Image of Big Business in America, 1880–1940* (Baltimore: Johns Hopkins University Press, 1975), chap. 3. Galambos examined 8,976 items related to big business that were printed in newspapers and journals between 1879 and 1940, using content analysis to reconstruct rough measures of opinion among certain influential groups.

Was President McKinley the Wizard of Oz?

The Wonderful Wizard of Oz is one of the all-time best-selling children's books.[27] It was written by Lyman Frank Baum (1856–1919), an actor, salesclerk, and small-town newspaper editor who loved creating stories for children. On the surface, the book is a magical adventure in a fairyland where children are as wise as adults. However, the book has a deeper dimension. It is a parable of populism.[28]

The Wonderful Wizard of Oz satirizes the evils of an industrial society run by a moneyed elite of bankers and industrialists. "Oz" is the abbreviation for ounce, a measure of gold. It and the Yellow Brick Road allude to the hated gold standard. The main characters represent groups in society. Dorothy is the common person. The Scarecrow is the farmer. The Tin Woodsman is industrial labor. His rusted condition symbolizes factory closings in the depression years of the 1890s, and his lack of a heart hints that factories dehumanize workers. The Cowardly Lion is William Jennings Bryan, the defeated Populist Party candidate, whom Baum regarded as lacking sufficient courage. The Wicked Witch of the East is a parody of the capitalist elite. She kept the munchkins, or "little people," in servitude. At the end of the Yellow Brick Road lay the Emerald City, or Washington, DC, where on arrival the group was met by the Wizard, representing the president of the United States. At the time Baum wrote the book, William McKinley was president, having defeated Bryan in 1896. Populists reviled McKinley because he had the backing of big trusts and he supported the hated gold standard.

At the conclusion, Dorothy melted the Wicked Witch of the East, the Wizard flew off in a balloon, the Scarecrow became the ruler of Oz, and the Tin Woodsman took charge of the East. This ending is the unrealized populist dream.

Baum's first motive was to be a child's storyteller, not to write political satire for adults. He never stated that the book contained populist themes, leading to debate over whether finding such symbolism is fair. Yet Baum lived in South Dakota while populism was emerging and he marched in Populist Party rallies. *The Wonderful Wizard of Oz* was written in 1898, at the height of ardor for reform. Therefore, it seems reasonable to think that Baum's tale was inspired by the politics of the day.

[27] L. Frank Baum (Chicago: Reilly & Britten, 1915), first published in 1900.
[28] The classic interpretation of symbolism is by Henry W. Littlefield, "The Wizard of Oz: Parable on Populism," *American Quarterly*, Spring 1964.

hostility toward large trusts. Soon the populists succeeded in electing many state and local officials, who enacted laws to regulate the railroads and provided the political groundswell behind creation of the Interstate Commerce Commission in 1887 to regulate railroads.

The populist movement was a diverse, unstable coalition of interests, including farmers, labor, prohibitionists, antimonopolists, silverites, and suffragists. These groups were held together for a time by a common, deep-seated hostility toward big companies. Ultimately, the populists failed to forge an effective political coalition and the movement was moribund after 1900 when William Jennings Bryan, the Populist Party's presidential candidate, was decisively defeated for a second time.

However, the populists refined a logic and lexicon for attacking business. They blamed adverse consequences of industrialization on monopoly, trusts, Wall Street, "silk-hatted Easterners," the soulless "loan sharks" and shameless "bloodhounds of money" who foreclosed on farms, and on corrupt politicians who worked as errand boys for the "moneybags" in a system of "plutocracy" (or rule by the wealthy).

Their criticisms were harsh and colorful. "The James Brothers and the Daltons were limited in their methods," thundered Mary Lease to a cheering crowd. "If they had operated on as large a scale as the millionaires of the country they could have built universities like Rockefeller. . . . "[29] In an essay on the virtues of farming as an occupation, Bryan wrote that for farmers "even the dumb animals are more wholesome companions than the bulls and bears of Wall Street."[30] Thomas Jefferson would likely have applauded.

It was, of course, too late for America to be a nation of farmers. This did not diminish the appeal of the populist message to large segments of the population. On the contrary, continued industrial growth has caused this message to resurface time and again up to the present, each time its vocabulary recycled and its content refined to fit current circumstances.

progressive movement A turn-of-the-century political movement that associated moderate social reform with progress. Progressivism was less radical than populism and had wider appeal.

The second critical movement was the *progressive movement*, a broader reform effort lasting from about 1900 until the end of World War I in 1918. Fueled by wide moral indignation about social problems caused by industry, it had strong support from the urban middle class and professionals. Although a short-lived Progressive Party was formed and unsuccessfully ran Theodore Roosevelt for president in 1912, both the Democratic and Republican parties had powerful progressive wings. Unlike populism, progressivism was a mainstream political doctrine. Like populism, it was at root an effort to cure social ills by using government to control perceived abuses of big business.

Because of broad popular support, progressives were far more effective than populists in their reform efforts, and during their era a cleansing tide washed over business. "Turn the waters of pure public spirit into the corrupt pools of private interests," wrote Ernest Crosby, editor of *Cosmopolitan* magazine, "and wash the offensive accumulations away."[31] Progressives broke up trusts and monopolies, outlawed campaign contributions by corporations, restricted child labor, passed a corporate income tax, and regulated food and drug companies and public utilities. With the Seventeenth Amendment in 1913 requiring direct election of senators they completed part of the Populist agenda.

Socialists

socialism The doctrine of a classless society in which property is collectively owned and income from labor is equally divided among members. It rejects the values of capitalism.

The full story of the Progressive movement's success lies in the counterpoint it provided to the socialist movement of that era. *Socialism* is a classless social system in which property is collectively owned and income from labor is equally and indiscriminately divided among members. When wealth is shared, want and conflict are eliminated. Socialism poses a revolutionary challenge to capitalist society because it requires a change in property relationships that destroys bedrock arrangements.

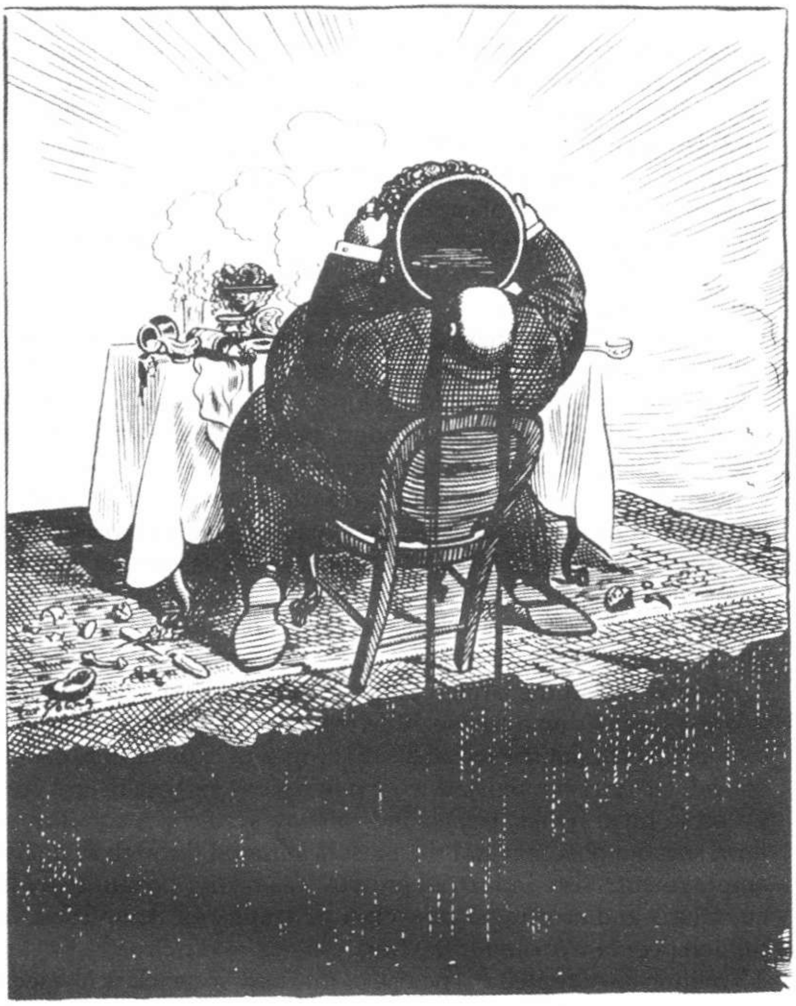
Although elements of socialist thinking are ageless, the originator of modern socialist doctrine is Francois-Noël Babeuf (1764–1797), a minor French official and writer who wanted to fulfill the promise of equality for all made during the French

[29] Quoted in "Furor over Mary Lease," *New York Times*, August 11, 1896, p. 3.

[30] "Farming as an Occupation," *Cosmopolitan*, January 1904, p. 371.

[31] "The Man with the Hose," August 1906, p. 341.

Art Young, a radical cartoonist of the Progressive era, had an impish ability to highlight the excesses of the industrial age. This cartoon, typical of many then drawn by Young and others, first appeared in 1912.



CAPITALISM

Revolution of 1789. He advocated seizing the possessions of the wealthy and giving them to the masses. Following this seizure, Babeuf envisioned a new communal economy. Private property would be abolished. Citizens would be required to work based on their trade or skill. The government would receive their output and distribute to everyone the basic material necessities of life. To eliminate individual desire for wealth and power, schools would teach egalitarian principles. Babeuf pushed for a violent overthrow of the French regime to achieve his vision and for this he was imprisoned, then beheaded in 1797. But his ideas took hold and circulated throughout Europe. One convert was Robert Owen, who was inspired to set up his tiny utopia in Indiana.

For a half century after Babeuf, socialist thought was splintered and muddied in a ferment of competing schools. Then, in 1848, Karl Marx (1818–1883) and his lifetime collaborator, Friedrich Engels (1820–1895), published *The Communist Manifesto* and put socialism on a new foundation.[32] Marx and Engels argued that the basis for socialism was an inevitable process of class struggle underlying and explaining the history of human society. Under capitalism the working class is exploited by the owners of capital, who pay low wages for dehumanizing work and then usurp for themselves the value of what workers toil to create. Marx often used metaphors in which capitalists became vampires and werewolves, sucking the lifeblood from labor.

Like Babeuf and others, Marx and Engels envisioned an equalitarian society that abolished private ownership of capital and instituted wealth-sharing among all members. Workers would no longer be alienated by miserable, meaningless labor. With class distinctions ended, people would live in harmony, their basic needs fulfilled. While Marx and Engels repeated many of the timeless criticisms of capitalism as characterized by barbaric competition, corruption of values by money, and meaningless work, they made socialism more compelling when they discovered a theory of history to explain it. Class warfare was the underlying dynamic that changed society. Workers in all nations had the duty to rise and overthrow the capitalist class. The last sentence of the *Manifesto* reads: "WORKINGMEN OF ALL COUNTRIES UNITE!"[33]

Meanwhile, in the United States of 1850 to 1900, rapid industrial growth was taking place within a coarse, little-regulated capitalist system that in many ways seemed to bear out the socialist's nightmare of exploitation. Child labor was widespread; factories injured and wore down workers; wealth and power were concentrated in great banks, trusts, and railway systems; inequality between rich and poor seemed obscene; and the masses suffered through financial panics and unemployment. Also, industrial growth was taking people away from agrarian occupations and creating a new class of employed Americans. In 1860 about 1.3 million people worked for the trusts, mines, and railroads, but by 1890 there were 4.3 million so occupied.[34] The rise of this new social class formed the soil in which labor unions could grow, and given widespread labor abuses, these unions might be attracted to socialism. As it turned out, this attraction would be limited.

As unions sprang up employers fought them. Most early unions were tied to single companies or locations. A few were radical and avowedly socialist, especially those with many European immigrants who brought Marxist thinking with them. The first big national union was the Knights of Labor, set up in 1869. Its constitution recognized exploitation of labor by owners of capital, but it called for

[32] According to Paul Sweezy, Marx chose to use the word "communist" rather than "socialist" because the meaning of the word "socialist" had become muddled. The term communist, in use for centuries to denote pooled property, more clearly conveyed his theory. See *Socialism* (New York: McGraw-Hill, 1949), pp. 8–9.

[33] Karl Marx and Friedrich Engels, *Manifesto of the Communist Party*, in Lewis S. Feuer, ed., *Marx & Engels: Basic Writings on Politics & Philosophy* (New York: Anchor Books, 1959), p. 41.

[34] Arthur M. Schlesinger, *Political and Social Growth of the United States: 1852–1933* (New York: MacMillan, 1935), p. 203.

reforms to protect labor rather than for overthrow of the capitalists. However, the union movement soon struck fear in the capitalist heart.

In the summer of 1877 a wave of violent strikes hit the railroads, then rolled on to other industries as it spread across the nation. Fighting and killing between strikers and the hired armies of employers was widespread. President Rutherford B. Hayes called his cabinet into a continuous session. He was so terrified that the country would fall to a workers' revolution that, rather than using federal troops to restore order in major cities, he gathered them in Washington, DC, to protect the government. The strikes eventually ran their course, and although there was never again such a violent cluster, from this time until the end of the century the number, size, and violence of strikes only increased.

In this climate of unrest, the socialist movement was surprisingly slow to blossom. The largest union, the American Federation of Labor, formed in 1886, disdained Marxism and elected to work with employers for higher wages and better working conditions. As time passed and the union movement grew, many workers still wanted radical change. They eventually found a home when the Industrial Workers of the World (IWW) was formed in 1905. The IWW proposed to represent all workers of both sexes and all races and in every industry in the fight to overthrow the capitalist system. Its platform was clear.

> We are here to confederate the workers of this country into a working-class movement that shall have for its purpose the emancipation of the working-class from the slave bondage of capitalism. . . . The aims and objects of this organization shall be to put the working-class in possession of the economic power, the means of life, in control of the machinery of production and distribution, without regard to the capitalist masters.[35]

Although the IWW was not as large as other unions, its unmitigated rejection of the system scared mainstream America and it was severely repressed. Laws were passed to prevent IWW members from speaking or assembling and it defied them, sometimes violently.

Working alongside the IWW was a young Socialist Party with growing power. It had been formed in 1901 with the avowed purpose of overthrowing capitalism. At the peak of its popularity in 1912 it had 118,000 members and its presidential candidate, Eugene V. Debs, got 6 percent of the popular vote. More than 1,000 socialists had been elected to state and local office.[36] This moment was the high mark of socialism in the United States. From then on, its appeal rapidly declined and it never recovered meaningful power.

There were four immediate reasons. First, because of its electoral successes the Socialist Party chose to make itself less radical to appeal to more voters. This breached socialist unity by alienating firebrand IWW leaders. Second, moderate reforms of the Progressive movement stole much of the socialists' thunder. Arguably, these reforms came only because the threat of growing socialist popularity put

[35] Quoted in Howard Zinn, *A People's History of the United States: 1492–Present,* rev. ed. (New York: HarperCollins, 2003), p. 330.

[36] Irving Howe, *Socialism and America* (New York: Harcourt, Brace, Jovanovich, 1985), p. 3.

pressure on the capitalist elite. Third, socialist unions made a huge tactical mistake (though not a doctrinal error) when they labeled World War I (1914–1918) an imperialist war and said that labor would refuse to shed its blood for wealthy capitalists. In 1917 the government put 101 leaders of the IWW on trial for violating sedition laws and all were convicted. Almost half of them got prison sentences of from 10 to 20 years. Others got shorter terms. This decapitated the IWW and crippled the socialist labor movement going forward. Fourth, as time passed the lot of most workers simply improved. Between 1897 and 1914 real wages rose 37 percent and the average sixty-hour workweek declined to fifty hours.[37] Again, the irony is that much of this improvement undoubtedly came out of fear of socialism.

The Great Depression and World War II

With the decline of socialism, capitalism had pushed back its most radical critics. After the triumph of progressive reforms, there was a period of high public confidence in big business during the prosperous, expansive 1920s. This rosy era ended abruptly with the stock market crash of 1929, and business again came under sustained attack. During the 1920s, the idea that American capitalism would bring perpetual prosperity had been widely accepted. The catastrophic depression of the 1930s disproved this and, in addition, brought to light much ineptness, criminal negligence, and outright fraud by prominent executives. There was a popular feeling that the economic collapse would not have occurred if business leaders had been more honest.

As the depression deepened, anger at business grew and the old rhetoric of populism reemerged. In the Senate, for example, Huey Long, a colorful populist Democrat from Louisiana who claimed to be the advocate of the poor against the rich, rose to condemn a "ruling plutocratic class."[38]

> The 125 million people of America have seated themselves at the barbecue table to consume the products which have been guaranteed to them by their Lord and Creator. There is provided by the Almighty what it takes for them all to eat: yea, more. . . . But the financial masters of America have taken off the barbecue table 90 percent of the food placed thereon by God, through the labors of mankind, even before the feast begins, and there is left on that table to be eaten by 125 million people less than should be there for 10 million of them.
>
> What has become of the remainder of those things placed on the table by the Lord for the use of us all? They are in the hands of the Morgans, the Rockefellers, the Mellons, the Baruchs, the Bakers, the Astors, and the Vanderbilts—600 families at the most either possessing or controlling the entire 90 percent of all that is in America. . . . I hope none will be horror-stricken when they hear me say that we must limit the size of the big man's fortune in order to guarantee a minimum of fortune, life and comfort to the little man.[39]

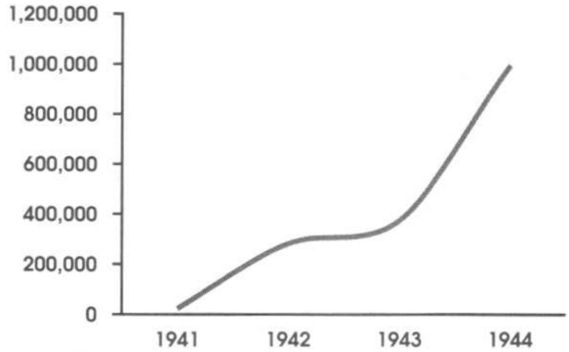
[37] Louis B. Wright et al., *The Democratic Experience: A Short American History* (Chicago: Scott Foresman, 1963), p. 302.

[38] *Congressional Record,* 73d Cong., 2d sess., 1934, p. 6081, speech of April 5.

[39] Radio speech broadcast March 7, 1935, inserted in the *Congressional Record,* March 12, 1935.

FIGURE 4.1 Production of .30 and .50 Caliber Machine Guns by General Motors: 1941–1944

Source: Based on data in James Truslow Adams, *Big Business in a Democracy* (New York: Scribner's Sons, 1945), p. 251.



These remarks echo the ancient Greek view that wealth in a society is limited and the accumulation of one person is a taking from all others—that great material wealth reflects greed. Long used these views to gain moral authority for his radical proposals. In 1934 he introduced a plan to redistribute wealth by collecting annual taxes on corporate assets and large fortunes and then giving every family a $5,000 initial gift followed with a guaranteed annual income of $2,500. In a collapsed economy, this populist-like plan had tremendous appeal, and Long attracted millions of followers. However, he was assassinated before it could be enacted, leaving the milder reforms of President Franklin D. Roosevelt's New Deal to carry the day.

During World War II, support for business rebounded. Industry wrapped itself in patriotism, and its high output proved essential to Allied victory. For example, General Motors converted itself almost entirely to war production. The company made 3,600 war items, including ball-bearings, bullets, rifles, torpedoes, trucks, tanks, bombers, and fighter airplanes. In a remarkable effort, it doubled its output of war material between 1942 and 1944. Figure 4.1 shows the production record for one item, machine guns.

Because of similar efforts by many corporations, the war years washed away the populist/socialist/depression era image of the corporation as a bloated plutocracy. It was instead the source of miraculous industrial production. In a radio address President Franklin Roosevelt labeled American business the "arsenal of democracy" that would turn the tide against evil dictatorships that sought to control the world.[40] The wartime performance was spectacular and in a postwar poll, only 10 percent of the population believed that where "big business activity" was concerned "the bad effects outweighed the good."[41] This renascence of respect lasted into the 1960s before the populist seed again sprouted.

The Collapse of Confidence

Strong public support for business collapsed in the mid-1960s. The nation was growing more affluent, but four strong social movements—for civil rights, consumer rights, and the environment and against the Vietnam War—attacked business for

[40] Radio address, Washington, DC, December 29, 1940. U.S. Department of State, *Peace and War: United States Foreign Policy, 1931–1941* (Washington, DC: U.S. Government Printing Office, 1943), pp. 598–607.

[41] Burton R. Fisher and Stephen B. Withey, *Big Business as the People See It* (Ann Arbor: University of Michigan Microfilms, December 1951), p. xiii.

FIGURE 4.2 Percentage of American Public Expressing "A Great Deal of Confidence" in Leaders of Major Companies: 1966–2006

contributing to a range of social ills including racism and sexism, consumer fraud, dangerous and alienating work, political corruption, and war profiteering. These attacks coincided with a negative trend in public opinion toward business. While in 1968, 70 percent of Americans agreed that business tried to strike a fair balance between profits and the public interest, by 1970 the number had declined to 33 percent, and by 1976 to 15 percent. This astonishing drop of 55 points took only eight years.[42]

Scholars who studied the polls theorized that turmoil in American society in the 1960s created a "confidence gap," or a gap between public expectations about how corporations *should* act and public perceptions of how they actually *did* act. Such gaps are perennial. They widened during the populist and progressive eras and during the Great Depression years. This new gap has now persisted for almost 40 years and continues to define the climate of public opinion.

Figure 4.2 shows the long-term trend for the percentage of Americans expressing "a great deal of confidence" in "people in charge of running major companies." In 1966, 55 percent of the public expressed such confidence, but over the next decade the percentage fell to 16 percent. Since then the confidence trend has bumped along a low road for 30 years, recovering to 28 percent in 2000 near the peak of a great bull market, but sinking again to 12 percent in 2004 after a cluster of fraud scandals including the Enron Corporation bankruptcy.[43]

[42] Seymour M. Lipset and William Schneider, "How's Business: What the Public Thinks," *Public Opinion*, July–August 1978.

[43] Figures are based on Harris polls asking this question: "As far as people in charge of running . . . major companies . . . are concerned, would you say you have a great deal of confidence, only some confidence, or hardly any confidence in them?" See Harris Poll no. 22, "Overall Confidence in Leaders of Major Institutions Remains Steady," March 2, 2006, tables 1, 2A–2D, at www.harrisinteractive.com.

The steep fall of public trust after 1966 opened the door for reformers to increase government regulation dramatically. During the late 1960s and early 1970s liberals in Congress created powerful new laws and agencies to protect the environment, consumers, and workers. However, by the mid-1970s corporations had organized to fight back. They soon dulled the blade of reform with a multifaceted campaign that included lobbying to block new regulation and public relations to influence public opinion.

A new group, the Business Roundtable, was set up to coordinate lobbying by corporate CEOs. Although business was unsuccessful in restoring basic public trust, it did alter key attitudes. Corporations funded conservative think tanks and used advertising to spread the message that excessive government regulation imposed unnecessary costs and burdens on companies, reducing their competitiveness and weakening the American economy. With the election of Ronald Reagan in 1980 a tide of Republican conservatism swept through the federal government, frustrating liberal reformers whose ideology of using government to control business was diminished—even discredited.

The New Progressives

Out of this liberal defeat rose a new leftist movement with a new ideology. The new movement adopted the label "Progressive" after the turn-of-the-century movement that sought a broad range of social and political reforms. Both movements have in common the desire to restrain corporate power in the public interest, but major difference exist between them. The *old Progressives* had wings in both the Democratic and Republican parties, so a wide span of liberals and moderates often supported reforms. Support for the *new Progressives'* agenda comes entirely from the left.

old Progressive A reference to political and social reformers at the beginning of the twentieth century.

new Progressives Members of left-leaning groups who advocate more radical corporate reforms than did the old Progressives. New Progressives seek to avoid being branded as liberals and try to take advantage of favorable connotations in the word progressive.

Unlike the old Progressives, who wanted to enact reforms through government, the new Progressive left seeks to carry out more radical change through direct action. And while the old-timers applied new scientific, legal, and management theories of the day to smooth the harsh edges of capitalism, the obsession of the new Progressives has been attacks on large corporations and the values and laws that support them. Largely blocked from the avenue of reform legislation by conservative and antiregulatory trends, activists confront corporations directly, one-by-one, trying to alter their behavior, even in the absence of laws against what the corporations are doing. Some seek to abolish the corporate form rather than to reform or regulate it. Underlying this deep antipathy are three basic beliefs.

First, corporations have too much power. Those with huge revenues and assets have excessive economic power in markets. They use their wealth to undermine democracy by dominating governments and corrupting politicians. Like entrenched oligarchs, they are unaccountable to the public for their self-interested exercise of power.

Second, corporations have inordinate legal rights. In the colonial era the charters that authorized corporations carefully restricted them to ensure that they acted for the common welfare. For example, they defined the company's business and limited its existence to a stated number of years. Today, instead of restricting corporations, state charters are very permissive. They allow branching out to new lines of business and grant the corporation perpetual life. Over the years legislatures, courts, and trade agreements have regularly added more rights, including the granting of "personhood" to corporate entities, entitling them to many constitutional rights of flesh-and-blood citizens.[44]

Third, corporations are inherently immoral. If often run or staffed by good people, the actions of these people are perverted by an implacable, master force, the very logic of the corporations itself. Corporations act to make money. They seek market expansion, sales growth, short-term financial results, and regulatory lenience. They value nature only as a production resource, workers only as costs, and human needs only as demand. Strong corporate cultures inculcate these values, pressuring and ultimately coercing the wills of even the most ethical employees, turning them into witting or unwitting agents of an antisocial institution.

The progressive network has no single leader, but in the United States a prominent figure and senior diplomat is Ralph Nader. Nader began his activist career more than 30 years ago by writing *Unsafe at Any Speed*, a book that attacked the auto industry for putting styling ahead of safety.[45] The popularity of the book helped Congress to pass auto safety legislation. Based on this success and his desire to seek change through government, Nader created more than 50 organizations to articulate consumer issues and lobby for protective laws. Over time, his hostility toward corporations has deepened and his desire to seek moderate reforms has lessened.

Announcing his candidacy for president of the United States in 2000, Nader said he was running to challenge "rampaging corporate titans," " runaway commercial imperatives," and "global corporations . . . astride our planet."[46] He declined to seek nominations as either a Republican or a Democrat because, he explained, both parties "feed at the same corporate trough."[47] Instead, he ran as a candidate for the Green Party, a global political movement that began as an antinuclear movement in Great Britain and New Zealand and has extended its platform to include main elements of the progressive agenda.

Although Nader got only 2.7 percent of the popular vote in 2000, he prevented Democrat Al Gore from winning the electoral votes of key states, allowing Republican George W. Bush, the more probusiness candidate, to win. In 2004 Nader again entered the presidential race, this time as an independent candidate, declaring that he represented "all Americans who wish to declare their independence from corporate rule and its expanding domination."[48] This time his impact was a faint two-tenths of 1 percent of the popular vote, making him insignificant in the outcome and leaving the nation, in his words, "a government of the Exxons, by the General Motors, for the DuPonts!"[49]

[44] For enumeration see Ted Nance, *Gangs of America: The Rise of Corporate Power and the Disabling of Democracy* (San Francisco: Berrett-Koehler, 2003), table 1.1.

[45] New York: Grossman, 1965.

[46] "Closing the Democracy Gap," *The Progressive Populist*, October 15, 2000, pp. 13 and 14.

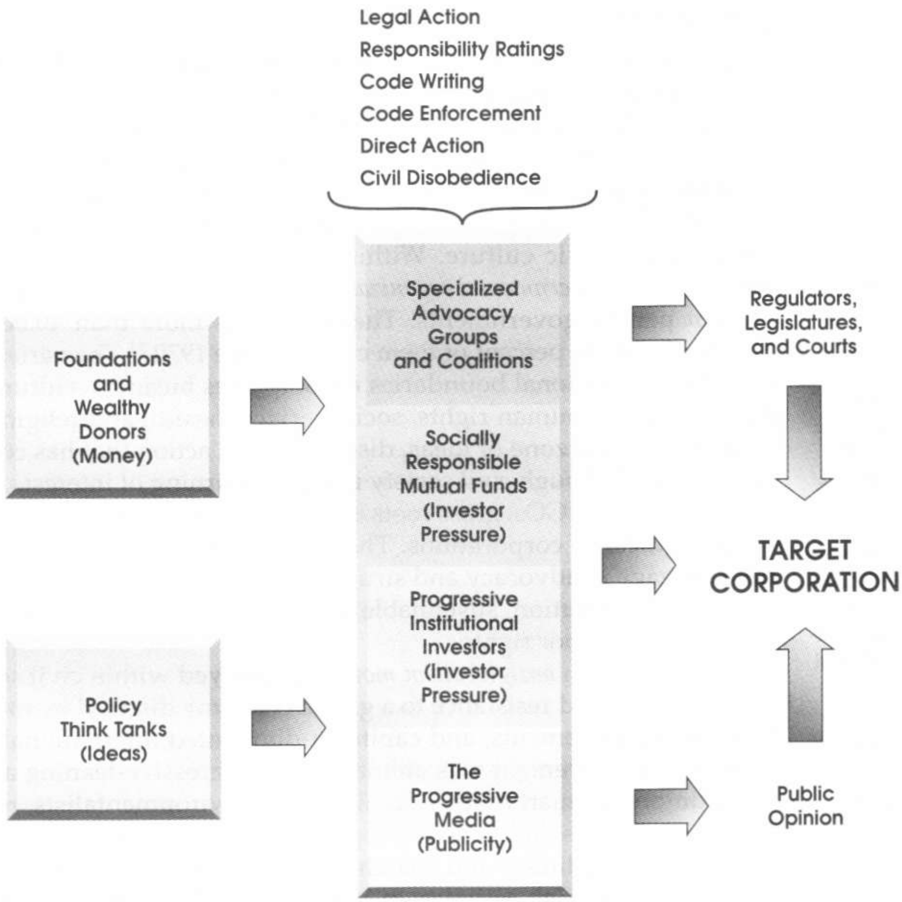
[47] Ibid., p. 14.

[48] "Ralph Nader Announcement of Candidacy: Toward a 'New Birth of Freedom' and Justice," February 23, 2004, p.1.

[49] Quoted in Patricia Sheridan, "Ralph Nader," *Pittsburgh Post-Gazette*, July 4, 2005, p. C2.

FIGURE 4.3
How the Progressive Network Attacks a Corporation

Source: Adapted from Jarol B. Manheim, *Biz-War and the Out-of-Power Elite* (Mahwah, NJ: Lawrence Erlbaum, 2004), fig. 10.2. Reprinted with permission of Laurence Erlbaum Associates, Publishers.



The progressive left movement is highly articulated and specialized. It has a network structure that includes leftist philanthropic and legal foundations; research institutes; publications; mutual funds; pension funds; unions; and groups of environmental, human rights, and labor advocates. The fraternity is knit together not only by shared ideology, but by flows of funding, program sponsorships, shared directorships, overlapping membership, information exchange, and coalition agreements.[50] Entities in the movement are specialized, creating an organizational symbiosis. Some groups use lawsuits to challenge business; others engage in civil disobedience. Some write conduct codes for industries; others train inspectors to enforce them. Some rate corporations on their social performance; others form mutual funds to invest in more responsible companies. Figure 4.3 shows various parts of the progressive left and how they combine to fight corporate power.

[50] For details on network dynamics see Jarol B. Manheim, *Biz-War and the Out-of-Power Elite: The Progressive-Left Attack on the Corporation* (Mahwah, NJ: Lawrence Erlbaum, 2004), pp. 38–40.

Global Critics

Corporate power increasingly challenges its antagonists on the world stage. With expansion of the global economy transnational corporations have grown in size and number, their mazelike structures spilling over national borders, their initiative eluding local regulation, their managers decreeing life chances for millions. Progressives fear corporate trickery in a void of weak social control over global markets.

Seeds of reaction against corporate power have sprouted in the soil of a new international civic culture. Within the international arena there is eruptive growth of *nongovernmental organizations* (NGOs), or voluntary organizations that are not part of governments. There are now more than 40,000 international NGOs, almost 90 percent of them created since 1970.[51] The variety of NGOs that operate over national boundaries encompasses business, cultural, educational, environmental, human rights, social service, health, and religious actors. They animate a global zone of ideas, discourse, and action that has come to be called *civil society*. Although civil society is a vast churning of interests, it is dominated by individuals, NGOs, grass roots movements, and institutions with progressive values critical of corporations. These actors, linked by electronic communications, engage in advocacy and struggle over a leftist design that includes global income redistribution, sustainable development, gender equity, and protection of human and labor rights.

nongovernmental organization
A term for voluntary organizations that are not affiliated with governments.

civil society
A zone of ideas, discourse, and action that transcends national societies and focuses on global issues. It is dominated by progressive values.

In the 1990s an *antiglobalism movement* evolved within civil society, its forces coalescing around resistance to a global economy directed by markets, corporations, trade agreements, and capitalist-dominated international financial institutions. The movement was animated by progressive-leaning actors including labor unions, human rights organizations, environmentalists, religious orders, farmers, socialists, indigenous people's movements, feminists, animal rights activists, Neo-Luddites,[52] and anarchists opposed to any overarching world order. It first achieved high visibility in 1999 when 50,000 activists gathered to protest World Trade Organization meetings in Seattle and street riots broke out. Two years later, at a *Group of Eight* summit in Genoa, Italy, as many as 100,000 came to protest as leaders of industrial nations met to discuss economic issues. Rioting led to the death of one activist.

antiglobalism movement
A coalition of groups united by opposition to economic globalization dominated by corporations and trade liberalization.

Since then the movement has created less visible turbulence. Concerns about terrorism made street protests more difficult and protests against trade became awkward after the September 11, 2001, attacks on the World Trade Center, a symbol of free trade.[53] But outside the limelight it has proved durable, growing in numbers and connectivity.

The antiglobalism coalition encompasses diverse, sometimes inconsistent agendas, so ascribing to it a specific goal or platform is difficult. However, its membership

Group of Eight
An annual meeting where leaders of the large industrial democracies discuss political and economic issues.

[51] Michael Edwards, *Civil Society* (Cambridge, England: Polity Press, 2004). p. 23.

[52] The Luddites (1811–1816) were English textile workers who blamed unemployment and low wages on new steam-powered textile machines. The name comes from a mythical figure, Ned Ludd. They wrecked the machines and violently attacked their makers before being suppressed.

[53] Juliane von Reppert-Bismarch, "Activists Take the Fight Inside," *The Wall Street Journal*, December 15, 2005, p. A10.

neoliberalism A term denoting both the ideology of using markets to organize society and a set of policies to free markets from state intrusion.

liberalism The philosophy of an open society in which government does not interfere with rights of individuals.

economic liberalism The philosophy that social progress comes when individuals freely pursue their self-interests in unregulated markets.

is united against the tyranny of *neoliberalism*, a term that encompasses both the philosophy and the specific practices on which current global economic expansion is based. To understand the meaning of neoliberalism, it is necessary to understand the history of the idea of liberalism.

Liberalism arose in Europe as a social philosophy in the 1500s. It promoted a free and open society in which the power of government to interfere with individual rights such as speech, association, conscience, and occupation was limited. Liberals had great faith in human reason and believed that this freedom would lead to social progress. For example, as freedom of speech allowed multiple opinions to be aired, truth would drive out falsehood. Liberalism proved compelling. It spread and today it defines the essence of a good society in much of the world.

One natural extension of liberalism was a philosophy of *economic liberalism* that sanctified the pursuit of individual self-interest in markets free from state interferences. It saw the market as another sphere of individual freedom. Liberals had faith that, like free speech, free markets would lead to positive social outcomes such as wealth creation and, ultimately, to human progress. Adam Smith's vision of *laissez-faire* capitalism defined this notion of economic liberalism.

Economic liberalism seized hold in the West. It was a critical ideology underlying the industrial revolution in England. Later, in the United States, it was used to justify the predatory capitalism of the 1800s and early 1900s that so aggravated Mary Lease, Mother Jones, and Huey Long. Then classical liberalism perished in the world depression of the 1930s. To end the depression and make economies perform for the public good governments decided to intervene in markets. Dropping the hands-off-the-market philosophy changed liberalism. It was no longer assumed that free markets always produced moral outcomes. They required state supervision. An era of growing market regulation followed. However, it was relatively short-lived, ending by the late 1970s when, in the opinion of the antiglobalists, corporate elites manipulated publics and governments to accept a new doctrine of free and expanding markets. This new doctrine came to be called neoliberalism.

To the antiglobalists, neoliberalism is the rebirth of the philosophy of economic liberalism coupled with a set of free-market economic policies including deregulation, privatization of state-owned enterprises, restrictions on labor unions, trade expansion, tax cuts, and reductions in the welfare state. Under the reign of neoliberalism, markets become the organizing principle for society. Corporate advertising makes our values more material. Corporations expand markets by, for example, expanding store hours, patenting genetic strains of crop seedlings, and running public services such as prisons for a profit. In neoliberal societies markets also guide personal lives. Individuals educate themselves to enhance their labor market value. They dress to please employers. They equate success in life with success in business. Neoliberal logic requires nations to tailor their economic policies to court foreign investors. On the international level undemocratic institutions—the World Trade Organization, the World Bank, and International Monetary Fund—enforce neoliberal policies on developing countries as the price of entering world markets. Overall, it is a pervasive, probusiness ideology that disgusts Progressives.

World Social Forum
The annual meeting of the antiglobalism movement.

The goals of the antiglobalism movement are elusive. Many in it find the antiglobalism label inaccurate. Few members reject globalization itself, and for this reason some prefer to call it the "global justice movement."[54] By whatever name, the brotherhood has come together each year since 2001 at a mass gathering called the *World Social Forum,* held in a developing country in January. The World Social Forum's charter states that it consists of "groups and movements of civil society that are opposed to neo-liberalism" and that these entities "are committed to building a planetary society directed toward fruitful relationships among Mankind and between it and the Earth."[55] But the movement is a cacophony of voices. According to one group of observers who attended a World Social Forum, the term neoliberalism was "little more than oratorical flypaper: an ugly, sticky mess to which everything the critics consider politically loathsome is made to stick in a single buzzing heap."[56] Yet the movement has goals including universal human and labor rights, income equity, equality of the sexes, democratic economic and political institutions, and sustainable development.

For now, debate and confrontation often center on the actions of transnational corporations seen as impeding progress toward a better world. The struggle against them excites many in the movement. Managers have come to fear clashes between market logic and the moral agenda of civil society. One estimate is that 6,000 of the world's 40,000 NGOs are of the variety that attack corporations.[57] A leading scholar within civil society issues the call to battle.

> [We are in] . . . a struggle between two globalizations grounded in sharply contrasting visions of human possibility—one imperial and the other democratic. It pits an alliance of state and corporate power devoted to a vision of global Empire against an alliance of people power devoted to a vision of Earth Community. Empire holds the edge in institutional power; Earth Community holds the edge in the moral power of the authentic cultural values of a mature consciousness.[58]

Global Activism

Activists, by definition, take action. Progressive elements have created unique webs of advocacy to correct perceived problems or abuses. An early example is the International Campaign to Ban Landmines, composed at its height of 800 groups in 50 countries. Activists from groups such as Human Rights Watch attacked corporations making antipersonnel mines. As a result, Raytheon stopped making mine components, and others, including Motorola, Hughes Aircraft, and General

[54] Naomi Klein, "Naomi Klein, Journalist," in Kate Holbrook, Ann S. Kim, Brian Palmer, and Anna Portnoy, eds, *Global Values 101* (Boston: Beacon Press, 2006), p. 117.

[55] World Social Forum India, *Charter of Principles,* 2006, at www.wsfindia.org.

[56] Matthew Sparke, Elizabeth Brown, Dominic Corva, Heather Day, Carolina Faria, Tony Sparks, and Kirsten Varg, "The World Social Forum and the Lessons for Economic Geography," *Economic Geography,* October 2005, p. 361.

[57] George Lodge and Craig Wilson, *A Corporate Solution to Global Poverty* (Princeton, NJ: Princeton University Press, 2006), p. 46.

[58] David C. Korten, *The Great Turning: From Empire to Earth Community* (Bloomfield, CT: Kumarian Press, 2006), p. 12.

Electric, quit selling parts used to make mines.[59] Similar advocacy networks have formed to fight sweatshop contracting by clothing makers and environmental abuses by energy and mining companies.

Such campaigns are not new. In the early 1800s a remarkably similar advocacy network led the global antislavery campaign.[60] In the 1970s international campaigns forced Nestlé and other infant-formula makers to change the way formula was sold in developing countries. And in the 1980s a fierce human rights coalition pushed foreign corporations out of very profitable markets in apartheid-era South Africa.[61]

Attacks on corporations marshal a range of devices that create pressure. Following is a list, hardly exhaustive, of tactics.

- *Consumer boycotts.* A boycott is a call to pressure a company by not buying its products and services. Perhaps the first global boycott, against white sugar, was called in 1792 by radical groups in England protesting brutal slavery in the British East Indies. It halved sugar sales in England and may have been crucial in ending the slave trade within the British Empire.[62] In recent years advocacy groups have called hundreds of boycotts. Here are some current examples. Friends of the Earth is boycotting Singapore Airlines because the government of Singapore threatened to jail violent protestors at World Bank meetings. A Belgian group, Mother Earth, is leading a coalition of 150 NGOs boycotting Altria Group, ExxonMobil, ChevronTexaco, PepsiCo, Coca-Cola, and McDonald's because they are big contributors to the Republican party in the United States. The groups are angry with President Bush for failing to act against climate change. A British NGO, Vegetarians International Voice for Animals is running a worldwide boycott of Adidas for using the skins of inhumanely killed kangaroos to make soccer boots.
- *Shareholder attacks.* In the United States and European nations rules permit shareowners of public companies to sponsor resolutions on which all stockholders may vote at annual meetings. Religious groups often lead in sponsoring resolutions in line with the progressive agenda. One group, the Interfaith Center on Corporate Responsibility, coordinates more than 200 religious orders and denominations that sponsor as many as 250 social responsibility proposals annually at shareholder meetings. Recent examples (with the percentage of the shareholder vote they received in 2006) are a proposal asking Ford Motor Company to reveal its lobbying activities to block higher fuel economy standards (7 percent) and a proposal calling on DuPont to cut its use of toxic chemicals (29 percent).

[59] Christina Del Valle and Monica Larner, "A New Front in the War on Land Mines," *BusinessWeek*, April 28, 1997, p. 43.

[60] Margaret E. Keck and Kathryn Sikkink, *Activists Beyond Borders* (Ithaca, NY: Cornell University Press, 1998), pp. 8–22.

[61] S. Prakash Sethi and Oliver F. Williams, *Economic Imperatives and Ethical Values in Global Business: The South African Experience and International Codes Today* (South Bend, IN: University of Notre Dame Press, 2001).

[62] "Sick with Excess of Sweetness," *The Economist*, December 23, 2006, p. 93.

Few social responsibility proposals have gotten a majority vote, but they create bad publicity and often lead to serious negotiations with management.

- *Harassment, ridicule, and shaming*. Essential Action, a group started by Ralph Nader, chartered a corporation named Licensed to Kill, Inc., in Virginia, stating in the charter that its work was to make and sell tobacco "in a way that each year kills . . . Americans."[63] Members of Essential Action then attended the annual shareholders meeting of Altria Group, whose Philip Morris subsidiary is the world's largest cigarette company. When the question and answer period came, an "executive" of Licensed to Kill invited Altria's CEO to join the new firm's board of directors, bringing his "experience in making a killing around the world."[64] The offer was declined.

  Forms of harassment are limited only by the imagination. Activists bring lawsuits based on clever charges such as racketeering. They disrupt the lives of executives and their families by picketing their homes, protesting at their children's schools, and interrupting services at their churches. They climb corporate buildings to unfurl banners. Some groups hand out mock awards to corporate targets. Corporate Accountability International regularly inducts corporations into its Hall of Shame. Each year on the eve of the World Economic Forum, advocacy groups meet to hand out "awards" to corporations nominated by NGOs around the world for exceptional irresponsibility. Past "winners" include Nestlé, Citigroup, Walt Disney, and Wal-Mart.
- *Codes of conduct*. Some advocacy groups develop codes of conduct that essentially enact progressive agendas. Corporations are pressured to sign on. If they sign, they often must submit to compliance monitoring done by specialized organizations with connections to activists. An example is Social Accountability 8000, a detailed code created by organizations in the worldwide campaign against sweatshop labor. The code sets forth principles for ethical treatment of workers. It requires corporate signers to be certified and then submit to periodic monitoring by examiners trained in code enforcement. An organization named Verité, with progressive ties, was set up to verify compliance.
- *Corporate campaigns*. A corporate campaign is a broad, sustained attack, usually by a coalition of groups, that mobilizes activists for coordinated warfare and employs a wide range of tactics.[65] The campaign depicts the firm as engaging in antisocial behavior to make a profit while representing the advocacy groups as moral crusaders for some universal truth. Transnational corporations have enormous financial resources, strong influence on governments, and trusted brand names. Activists typically have slender financing, little political influence, and low public recognition. However, a key source of strength is the tendency of the public to see environmental, religious, or human rights groups as selfless and acting for justice. Using this perception, activists seize the ethical

[63] "Articles of Incorporation, 2003." See www.licensedtokill.biz.

[64] Ibid., "Licensed to Kill Invites Altria CEO to Become an L2K Director!" 2003.

[65] For an extended discussion, see Jarol B. Manheim, *The Death of a Thousand Cuts: Corporate Campaigns and the Attack on Corporations* (Mahwah, NJ: Lawrence Erlbaum, 2001).

high ground and engage the corporation with an assault that might be likened to warfare because the action sometimes stretches or breaks the bonds of civility. A recent example is the campaign of ForestEthics to get Victoria's Secret, a subsidiary of Limited Brands, to stop using pulp from virgin Canadian forests in its catalogs. The company agreed to use recycled paper after enduring two years of a "Victoria's Dirty Secret" campaign that included store picketing by chain-saw wielding women in lingerie, civil disobedience in shopping malls, and shareholder meetings picketed by hecklers in bear costumes.

The activism of global civil society challenges traditional notions of democracy. Advocacy groups have limited memberships. Unlike representative legislatures, they are not accountable to a broad base of voters even as they claim that their ideas about everything from sustainable forests to healthy diets represent the public interest. They are unwilling to accept as responsible corporate behavior that which is guided merely by laws, trade agreements, or the choices of individual consumers in markets. Instead, they argue that since corporations have corrupted governments and manipulated consumers, they are justified in taking action to impose standards of "responsibility," "justice," "equity," and "rights" as defined by the progressive vision. This vision is not uncontroversial. Once into a campaign, progressive advocates tap the deep cynicism in public opinion to build anger against the corporate target. If the company capitulates and changes its policies, the activists have, in effect, appropriated its power and assets to further their policy agenda. And this may have been accomplished by an end run around formal institutions and regulators.

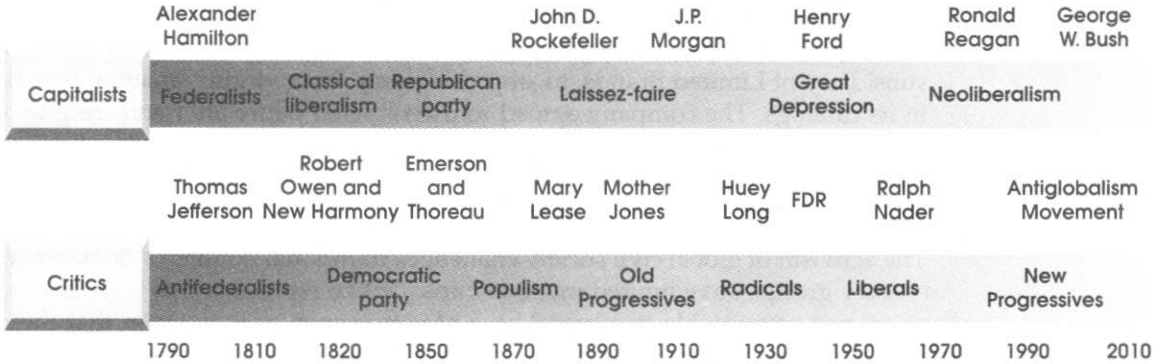
CONCLUDING OBSERVATIONS

We have narrated a history in which basic criticisms of business are repeated over and over. Each era brings new personalities, new targets, and some new issues, but the fundamental substance endures. The story is one of endless dialogue between critics and defenders of capitalism. Figure 4.4 shows two timelines that represent this dialogue. Imagine a dinner party at which Aristotle, Saint Augustine, Thomas Jefferson, and Ralph Nader sit at one table while Adam Smith, Benjamin Franklin, Alexander Hamilton, and Ronald Reagan sit at another. Now imagine the harmony among tablemates as contrasted with the gulf between the two groups.

There is no question that industrial capitalism is a historical force for continuous, turbulent social change; it is, as the economist Joseph Shumpeter wrote years ago, "a perennial gale of creative destruction" that strains institutions and challenges existing authority.[66] The defense of capitalism is that, for the most part, the changes it brings represent progress, a condition of improvement for humanity. All the while that critics have been objecting, it has steadily improved living standards for hundreds of millions of people. As against promoting greed and avarice,

[66] *Capitalism, Socialism and Democracy* (New York: Harper & Row, 1976), p. 143; originally published in 1942.

FIGURE 4.4 **Timelines of Ideological Conflict**



The two timelines show how a debate between business and its critics moves through American history. Each timeline represents the sweep of people and ideas associated with one side of this enduring debate.

it has promoted positive cultural values such as imagination, innovation, cooperation, hard work, and the interpersonal trust necessary to conduct billions of daily business transactions.

In the end, a broad spectrum of criticism is an important check on power. Legitimate criticism exists and demands attention. If criticism is properly channeled, it can preserve the best of the business institution and bring wide benefit. In Ralph Nader's words: "Whenever, in our nation's history, people successfully challenge the excessive power of commercial interests, whether over workers, child labor, minorities, consumers and the environment, the country became better and the economy stronger."[67]

Not all antiglobalists and Progressives reject capitalism. Many now believe that corporate-led economic development underlies social progress even as companies sometimes behave badly. They have come to accept that growing trade holds the potential for alleviating poverty. These critics now promote the doctrine of corporate social responsibility, the subject of our next two chapters.

[67] "Human Need Trumps Corporate Greed," *The Wall Street Journal*, October 25, 2000, p. A22.

A Campaign against KFC Corporation

War was declared on January 6, 2003. In a press release, People for the Ethical Treatment of Animals (PETA), a militant animal rights group, announced it was beginning a pressure campaign against KFC Corporation, the world's largest chicken restaurant chain. PETA held KFC responsible for the "cruel treatment" of poultry raised and slaughtered for its restaurants.[1] It demanded that KFC force new, more humane practices on its suppliers. KFC responded with a statement dismissing "allegations made by PETA" and saying that its chickens were treated humanely.[2]

KFC does not raise any chickens. In the United States it buys them from 18 independent companies operating more than 50 chicken farms and slaughterhouses and pursues similar arrangements in other

[1] "Company Stonewalls on Animal Welfare Reforms," press release, People for the Ethical Treatment of Animals, January 6, 2003, available at www.peta.org.

[2] "KFC Denies PETA Claims," press release, KFC Corporation, January 7, 2003, available at www.kfc.com.

nations. PETA is angry about how chickens are handled by these suppliers, but their facilities are out of public view and make difficult targets. KFC, with its popular restaurants, is highly vulnerable to attack. By assaulting its brand image PETA hopes to make KFC use its market power as the world's largest purchaser of chickens to force reform on growers and slaughter plants. If this occurs, PETA will have harnessed a reluctant giant to accomplish its goals.

Going into the chicken war, PETA had a record of success. Its initial effort was a campaign against McDonald's in 1999. After less than a year of exposure to a boycott, restaurant demonstrations, and the group's mccruelty.com Web site the company succumbed, imposing stricter animal welfare standards on its suppliers as a condition for ending the assault. It forced changes on reluctant growers, including roomier cages for hens, surprise slaughterhouse inspections, and more effective stunning of chickens before killing them. After McDonald's capitulated, its smaller rivals followed. Burger King adopted animal welfare guidelines after a five-month campaign. Then Wendy's buckled. Safeway lasted only three months. Albertsons and Kroger's were subdued by campaigns of only one week each.

INITIAL SKIRMISHES

KFC learned of PETA's intentions in 2001, when Cheryl Bachelder, its president, received a letter from Bruce Friedrich, director of the group's restaurant campaigns. The letter asked why KFC, knowing of PETA's actions against its competitors, was doing "nothing at all" to improve the lives of chickens raised for its restaurants. Friedrich asked what KFC intended to do, offered to put the company in touch with animal welfare experts, and added "we are looking ahead to our next target."[3]

Over the next several weeks Friedrich had a series of phone calls and meetings with Bachelder and David Novak, CEO of KFC's parent corporation Yum! Brands. Yum! Brands was created in 1997 when PepsiCo spun off its KFC, Pizza Hut, and Taco Bell chains as a separate corporation. Subsequently, the new firm bought the Long John Silver's and A&W chains. Today, Yum! is the world's largest quick-service restaurant corporation with 35,000 restaurants worldwide. The KFC brand traces its origins to the Kentucky Fried Chicken franchise started by the avuncular Colonel Harlan Sanders in 1952. It has 14,500 restaurants in 100 countries and serves about 12 million customers every day.

The dialogue revealed a wide gulf between the company and its interlocutor. KFC told Friedrich that it included humane treatment guidelines in its poultry supplier contracts. He accused the company of using only inadequate industry standards permitting ghastly treatment of chickens and considering their welfare only at the point where deaths from abuse lowered profits. He stated that the suffering of chickens was an ethical issue going beyond financial considerations.[4] KFC said it would review its guidelines and promised to keep PETA informed.

In the months that followed, KFC took several actions. It convened an Animal Welfare Advisory Council composed of outside academic and industry experts. It began unannounced audits of growers and slaughterhouses. And it worked with industry associations to develop new poultry welfare guidelines. However, its efforts were unsatisfactory to PETA because they did not lead to specific, more radical changes including the following.

- *Gas killing.* KFC chickens are stunned by electrical shock before immersion in scalding water (to loosen feathers) and then exposed to mechanical blades that slit their throats. PETA believes that gas killing is preferable because it ensures that chickens are insensate before these painful procedures, whereas electrical stunning is less reliable.
- *Cameras in slaughterhouses.* Cameras would supplement audits and make oversight more reliable.
- *Mechanized chicken-catching.* Hand-catching crews gather KFC chickens from grower buildings. PETA believes that the crews treat the birds roughly and that mechanical catching systems are less likely to result in bruises and broken bones.
- *New genetic strains of chickens.* The chickens eaten in KFC restaurants, known as "broilers," are bred to gain weight rapidly over their brief lives. However, the "broiler breeders" used to produce the flocks of chickens slaughtered for restaurant meals live longer. They exhibit the rapid weight gain

[3] The letter is at www.kfccruelty.com/letter-042501.asp.

[4] Letter of May 14, 2001, from Bruce G. Friedrich to Jonathan D. Blum, senior vice president, Tricon Global Restaurants, at www.kfccruelty.com/letter-052401.asp. Yum! Brands was formerly named Tricon Global Restaurants.

characteristic of all broiler strains, but their skeletons and joints do not grow commensurate with their overall weight and they are prone to painful joint conditions as they age. PETA requested introduction of leaner genetic strains that did not exhibit skeletal deficiencies.

- *Elimination of forced growth.* Broiler strains bred for rapid weight gain under forced growth regimens suffer from metabolic pathologies and excess mortality. Slowing growth means longer upkeep of chickens before slaughter, but it reduces premature deaths.
- *More room for birds to move around.* PETA requests that KFC give its chickens at least two to three times more space per bird and give them sheltered areas and perches in the warehouselike buildings where they are raised.
- *Allowance for instinctive behavior of chickens.* PETA believes that birds raised in captivity suffer from chronic stress and boredom induced by suppression of natural behaviors. Among other measures, it suggests that they get whole green cabbages to peck and eat.[5]

Debate between the antagonists was dysfunctional. PETA addressed the corporation in the tone of a parent scolding an errant child. It was "extremely concerned" that the firm "has no interest in making real progress to stop animal cruelty," adding that "we have pressed you to take action on this issue, yet you have done nothing."[6] KFC, on the other hand, wrote to PETA "[i]n the spirit of open communications," but kept it at arms length, giving only brief and general information about conducting audits, holding meetings, and working on animal welfare standards with industry groups.[7] PETA believed that KFC was dragging its feet.

A LOOK AT PETA

PETA is dominated by its founder, Ingrid Newkirk, who became an animal rights activist after a formative experience. Living in Maryland in 1972, she was training to become a stockbroker. A neighbor moved, abandoning cats that soon bred litters of kittens nearby. She gathered them up and took them to a nearby animal shelter to be cared for. Yet a short time later she learned they had been killed. The episode changed her. With no desire to become a stockbroker remaining, she talked her way into a job at the shelter. Observing brutal treatment of animals, she began to arrive early in the morning to kill them in a humane way before others came. "I must have killed a thousand of them," she says, "sometimes dozens every day."[8]

From the shelter Newkirk moved on to work as a deputy sheriff on animal cruelty investigations, then headed a commission to control animal disease. She was inspired to form PETA after reading a book, *Animal Liberation*, by philosopher Peter Singer.[9] In the book, Singer argues that animals have moral rights. Moral rights are strong entitlements to dutiful treatment by others—in this case human beings. He asserts that the traditional, absolute dominion of humans over animals is an unfair exploitation. Because animals are living, sentient beings capable of suffering, their interests are entitled to equal consideration with human interests. In his words: "No matter what the nature of the being, the principle of equality requires that its suffering be counted equally with the like suffering . . . of any other being."[10] Thus, he argues, animals have an unalienable right to have their needs accommodated by humans. Denial of this right is speciesism, or the prejudicial favoring of one species over another. Speciesism, according to Singer, is an evil akin to racism and sexism because it restricts moral rights to one species just as racism and sexism have restricted them to one race or sex. The PETA Mission Statement, Exhibit 1, reflects the inspiration Newkirk found in this philosophy.

Newkirk has a combative attitude about animal rights. "The animals are defenseless," she says. "They can't talk back, and they can't fight back. But we can. And no matter what it takes, we always will."[11] After reading about a Palestinian bomb put on a donkey and detonated by remote control she wrote to Yasir Arafat requesting that innocent animals be left out of

[5] Letter of August 6, 2002, from Bruce G. Friedrich to Jonathan D. Blum, available at www.kfccruelty.com/letter-080602.asp.

[6] Ibid.

[7] Letter of July 17, 2002, from Jonathan Blum to Bruce G. Friedrich, available at www.kfccruelty.com/petakfc.asp.

[8] Quoted in Michael Specter, "The Extremist," *The New Yorker*, April 14, 2003, p. 56.

[9] New York: Avon Books, 1975.

[10] Ibid., p. 8.

[11] Quoted in Specter, "The Extremist," p. 54.

EXHIBIT 1
PETA's Mission Statement

Source: Courtesy of People for the Ethical Treatment of Animals (PETA).

People for the Ethical Treatment of Animals (PETA), with more than 1.6 million members and supporters, is the largest animal rights organization in the world.

PETA focuses its attention on the four areas in which the largest numbers of animals suffer the most intensely for the longest periods of time: on factory farms, in laboratories, in the clothing trade, and in the entertainment industry. We also work on a variety of other issues, including the cruel killing of beavers, birds and other "pests," and the abuse of backyard dogs.

PETA works through public education, cruelty investigations, research, animal rescue, legislation, special events, celebrity involvement, and protest campaigns.

the Arab-Israeli conflict. Her will stipulates that when she dies the meat on her body is to be cooked for a human barbeque, her skin used to make leather products such as purses, and her feet made into umbrella stands.[12]

PETA is creative. Since most people give no thought to animal rights, its actions are designed to attract attention, even at the cost of offending some. Perhaps the mildest attention-getting tactic is the use of theater. For example, PETA demonstrators have dragged themselves down streets with their feet in leg traps to publicize the evils of fur trapping. Another tactic is that of the outrageous act. To protest pictures of women wearing fur in *Vogue*, activists went to the expensive Manhattan restaurant where its editor was having lunch and threw a dead racoon on her plate. Young ladies at county fairs are crowned as Pork Queens only to have pies thrown in their faces by PETA activists. The group has asked Wisconsin, the "Dairy State," to change its state beverage from cows' milk to soy milk.

PETA freely uses sexuality to get attention. When the American Meat Institute puts on its Annual Hot Dog Lunches for government officials in Washington, DC, former *Playboy* Playmates wearing bikinis made of lettuce hand out "veggie dogs" outside. It recruits celebrities to present its message. Fame and glamor attract. Their presence endows a view that might otherwise be disregarded with the celebrity's aura of success and legitimacy. PETA also uses the Internet well to get its message out. It has multiple Web sites for issues such as zoos, circuses, and animal testing. The network of sites is easy to navigate, informative in depth, and often entertaining. There are facts, games, pictures video clips, humor, and celebrities. PETA makes a special effort to influence children. One comic brochure, "Your Mommy Kills Animals" shows a crazed woman wielding a bloody knife over a rabbit. "Ask your mommy," it suggests, "how many animals she killed to make her fur coat."[13]

All these tactics, and more, have been employed in the fight against KFC.

THE CHICKENS

At the center of the conflict are the chickens. Chickens are a species of the order Galliformes, which includes turkeys, pheasants, grouse, and partridges. Galliformes are heavy-bodied, short-duration fliers that feed on insects and seeds, nest on the ground, and hatch precocial (self-caring) young. They are social birds that communicate with each other and establish complex hierarchies in flocks.

The earliest wild chickens, members of the species *Gallus gallus*, inhabited jungles of southeast Asia. About 4,000 years ago they were domesticated. From Asia the domesticated chicken, *Gallus domesticus*, spread across the globe. In ancient Greece they were valued for the sport of cockfighting, and in imperial Rome prophets read the future in their entrails. Chickens had such a hold on the superstitious Romans that generals kept special flocks in the belief that their behavior could foretell victory or defeat in battle. In the hours before combat, hardened legionnaires crowded around these flocks seeking portents. As the legions marched, they spread *Gallus domesticus* across the empire. Centuries later, the earliest European settlers brought chickens to North America.

[12] Ibid., pp. 57, 58.

[13] At www.furissdead.com

In the United States, large-scale chicken production developed slowly. As late as the 1920s chicken farms had flocks of only about 500 free-ranging birds. Today the industry is highly specialized, with some farms in egg production and others raising broilers (or chickens slaughtered for meat; literally, chickens for broiling—or baking or frying). Flocks are now raised in long, windowless, buildings with automated equipment to maintain as many as 100,000 birds. Consumption of chicken has risen. In 1955 only a little more than 1 billion broilers were raised, or 6.5 chickens for each American; by 2005 there were 8.7 billion raised, or 30 per American.[14]

Chickens, like other animal species, adapted for survival in an ecological niche. In doing so, certain behaviors became instinctive. They live in flocks of approximately 10 and establish dominance hierarchies called pecking orders. The dominant bird in a flock can peck any other bird, and that bird will yield. Status in the pecking order is conveyed by sounds such as crowing or cackling, aggressive or passive postures, spacing, use of more or less desirable nesting sites, and running at or away from rivals. In mixed-sex flocks there are two pecking orders, one for cocks and one for hens, but the hen hierarchy is completely subordinate. All hens yield to even the lowest cock. This is a genetically predisposed trait essential for species survival because a cock will not mate with a dominating hen. Pecking orders have survival value. Once dominance is established, fighting ceases and energy is used in socially productive ways.

In nature, chickens are omnivorous, eating plants, insects, and small animals such as lizards. Hens are secretive and build hidden nests, preferably on the ground. During the day chickens spread out to forage, but at dusk they reduce the spaces between them. At night they often roost in trees. According to PETA, chickens are "inquisitive and interesting animals" and "as intelligent as mammals like cats, dogs, and even primates."[15] In nature, they are individuals with "distinct personalities" that "form friendships and social hierarchies, recognize one another, love their young, and enjoy a full life, dust-bathing, making nests, roosting in trees, and more."[16]

Life in high-density growing environments frustrates these natural behaviors. Cages or crowding prevent division into flocks with established pecking orders. Without a complete pecking order, individuals may not yield to threat displays, and physical attacks occur as birds compete over space, food, and water.[17] Weaker animals have no place to hide and may be assaulted repeatedly until they die. In addition, crowded chickens are unable to engage in a range of ordinary foraging, grooming, nesting, brooding, and roosting behaviors. Critics claim that such deprivation violates the right of an animal to satisfy its needs through natural behaviors.

THE CAMPAIGN

At the start of the campaign, PETA sought to inflict damage on the KFC brand and harass company executives. In the first months it conducted hundreds of demonstrations at KFC restaurants around the world. Protesters dressed like chickens and locked themselves in cages. They handed out "Buckets of Blood" containing "Psycho Col. Sanders" figures and toy chickens with slit throats. When Yum! Brands CEO David Novak appeared at the opening of a restaurant in Germany, two activists doused him with fake blood and feathers. According to campaign leader Friedrich: "There is so much blood on this chicken-killer's hands, a little more on his business suit won't hurt."[18]

KFC issued a statement calling the attacks "corporate terrorism" that "crossed the line from simply expressing their views to corporate attacks and personal violence."[19] In Paris, Ingrid Newkirk and celebrity Chrissie Hynde of The Pretenders led activists who stormed into a busy KFC restaurant at the noon hour. They smeared red paint symbolizing chicken blood on the front window and talked to customers until security guards threw them out. Outside, the protest blocked traffic on a boulevard for two hours. Back in the United States, PETA put up roadside billboards depicting Col. Sanders hacking a chicken with

[14] *Statistical Abstract of the United States 1956, 77*th ed., tables 1 and 857; and *Statistical Abstract of the United States 2007*, 127th ed., tables 2 and 842.

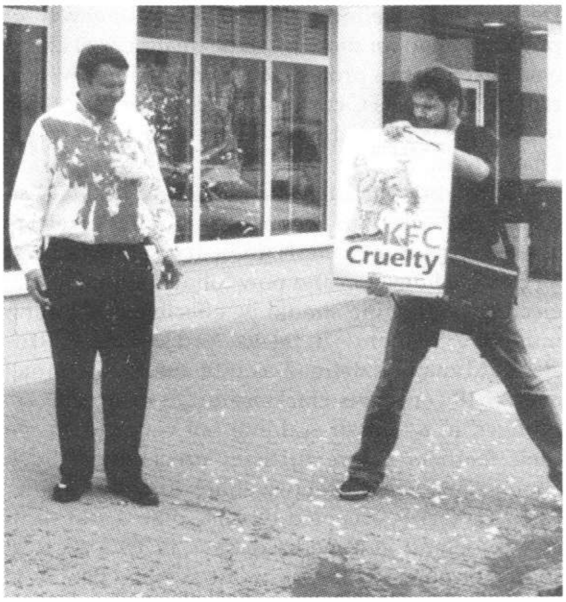
[15] "Chickens," at www.peta.org.

[16] "PETA Reveals Shocking Cruelty to Animals at KFC Factory Chicken Farm," press release, October 2, 2003, at www.peta.org.

[17] T. R. O'Keefe et al., "Social Organization in Caged Layers: The Peck Order Revisited," *Poultry Science*, July 1988, p. 1013.

[18] Quoted in Jay Nordlinger, "PETA vs. KFC," *National Review*, December 22, 2003, p. 28.

[19] Cited in "Animal Rights Activists Spray KFC Chief with Fake Blood and Chicken Feathers," The Associated Press State & Local Wire, June 23, 2003.



Yum! Brands CEO David Novak after being splattered with blood at a demonstration in Hanover, Germany, on June 23, 2003. Source: © AP Photo/PETA Deutschland.

a bloody knife under the slogan "Kentucky Fried Cruelty. We do chickens wrong."[20]

Although the main effort of the campaign went into publicly associating the KFC brand with cruelty toward chickens, another focus was on pressuring KFC and Yum! Brand executives at a personal level. After several months of the campaign KFC President Cheryl Bachelder failed to keep what Ingrid Newkirk though was a commitment to call her. So Newkirk phoned Bachelder at home on a Saturday evening. When Bachelder objected to being called at home, Newkirk responded with a letter that read, in part:

> Of course you would rather not be disturbed in the privacy of your own home, but the animals you torture and slaughter pay for that home with their misery and their very lives yet have nothing remotely like a life or even a nest of any kind. . . . It is merely an accident of birth that you are not one of them.[21]

Newkirk wrote to both Bachelder and CEO Novak at their homes in Louisville, Kentucky, posting the letters with their home addresses on PETA's kfccruelty.com Web site. It enlisted former Beatle Paul McCartney to write to Novak. His letter, which requested an end to "the egregious forms of abuse endured by chickens," ran as a full-page ad in the Louisville *Courier-Journal*. A KFC spokesperson responded that "PETA should follow one of Sir Paul's songs and just 'Let It Be.'"[22]

PETA also wrote to friends and neighbors of Yum! Brands and KFC executives, requesting to visit their homes and speak with them. Bachelder's home was picketed. Pickets also came on Sunday to the Louisville church attended by Novak and another top executive. Outside the service, PETA parked its "Reality TV" truck that displayed big-screen images of slaughterhouse abuses.[23] On Christmas Eve and Christmas Day 2003 Friedrich dressed up as Santa Claus and blocked a sidewalk outside the church. He also demonstrated at the home of a KFC senior vice president, leading to a conviction for trespass.[24]

In the first summer of the campaign, KFC President Bachelder flew to Norfolk, Virginia, for a meeting with Newkirk at PETA's headquarters. At the meeting, she agreed to install cameras in slaughterhouses that supply KFC chickens, to provide more stimulation for chickens, to use mechanized chicken-gathering equipment, and to increase the space for each bird. In return, PETA agreed to scale back its campaign for 60 days.[25] However, the agreement fell apart when Newkirk accused Bachelder of not following through.

As time went on, PETA rolled out its broad strategic inventory. It recruited a long list of celebrity supporters. Actress Pamela Anderson narrated video clips showing how chickens are abused. Ms. Anderson freely lent her sex appeal to the campaign by, for example, posing for billboards in a white satin bra.[26] His Holiness the Dalai Lama wrote to ask that KFC end plans to build a restaurant in Tibet. The Rev. Al

[20] "Finger-Lickin' Foul" *"Houston Press*, December 18, 2003, p. 2.

[21] Letter of March 24, 2003, from Ingred E. Newkirk to Cheryl Bachelder, available at www.kfcruelty.com/petakfc.asp.

[22] Mark Naegele, "McCartney Accuses KFC of Fowl Play," *Columbus Dispatch*, July 25, 2003, p. 2C.

[23] Scott Sonner, "PETA Steps Up Campaign against KFC Farm, Slaughter Practices," The Associated Press State & Local Wire, September 19, 2003.

[24] "Christmas Protests Net Conviction for PETA Exec," *Restaurant Business*, May 18, 2004, online at restaurantbiz.com.

[25] Wesley J. Smith, "PETA-Fried," *National Review*, July 11, 2003, p. 25.

[26] "Billboard Companies Refuse to Run PETA Ad," *The Globe and Mail*, February 2, 2006, p. S2.

Sharpton spoke out asking the black community to boycott KFC.

Taking advantage of Securities and Exchange Commission rules, PETA gained entry to the Yum! Brands 2003 annual shareholders meeting in Louisville. After activists spoke, CEO Novak called on the group to end its campaign, saying, "We don't want to be abused, just like you don't want the chickens to be abused." In 2004 PETA qualified a shareholder resolution asking for a company report on actions to reduce cruelty toward chickens. Only 7.6 percent of shareholders voted for it. When PETA introduced a similar resolution in 2006, it went down to defeat with only 9 percent voting in favor.

PETA sued Yum! Brands alleging false statements about treatment of chickens on its Web site. The company deleted the wording. In a bizarre show of dedication a PETA staff member changed his legal name from Chris Garnett to KentuckyFriedCruelty.com.[27] PETA has conducted a dozen undercover investigations at KFC supplier plants in the United States, Europe, and Asia documenting incidents of sickening animal abuse. Protests continue. There have been more than 10,000 all around the world, many with female activists wearing bikinis to get attention.[28]

A MUTED CORPORATE DEFENSE

Throughout the PETA campaign, KFC and Yum! Brands have tried to maintain a low media profile while working to elevate animal welfare standards. This reticence is characteristic of the animal agriculture, food, and restaurant industry generally when animal welfare becomes an issue. In mass growing and slaughter some pain for animals is inevitable. Altering production to address chicken discomfort, injury, and behavioral deprivation raises costs.

Most consumers are ignorant of factory farming methods and fail to entertain the link between a KFC meal and the life experience of the creature in it. Despite PETA's efforts, there is no groundswell of public opinion for more humane treatment of chickens. Reacting to a protest going on outside a restaurant in Israel, a KFC customer said: "There's nothing to do. This is life and it is all part of the food chain. I have to eat."[29]

The vacuum of interest and concern sustains industry calculations balancing poultry welfare against costs. For example, industry guidelines that KFC helped develop and now follows stipulate that electrical "stunning should be effective at [a] minimum of 98% of birds in [a] 500-bird sample."[30] This standard may be defined as humane, but it is met even if 10 conscious chickens out of every 500 are plunged in a tank of scalding hot water to loosen their feathers before further "processing." Such compromises in chicken welfare to avoid higher costs are tacitly accepted by KFC diners, but difficult to defend in a media debate. PETA's greatest source of power is the desire of average people to think of themselves as humane and decent.[31] The impossibility of defending a standard that lets chickens be boiled alive makes cautious nonconfrontation a better policy than frontal attack on PETA.

In response to attacks, the company consistently makes these points. It complies with all laws in the more than 100 countries where it has restaurants. It is only a purchaser and does not own the animal farms and slaughterhouses where abuses may occur. It accepts that its size as a chicken buyer gives it responsibility and the power to lead in the humane treatment of chickens and it is taking action.

Since 2000 KFC has followed the Yum! Brands Animal Welfare Guiding Principles (Exhibit 2) and since 2004 it has implemented a more comprehensive set of KFC Poultry Welfare Guidelines covering breeding, chicken houses, catching, transport, holding, stunning, and slaughter. KFC calls these guidelines "industry leading," but PETA rejects them because they do not require the changes it demands. Yum! Brands set up an Animal Welfare Advisory Council composed of distinguished animal scientists and industry

27 Dave Golowenski, "Activist Group Squawks over KFC's Treatment of Chickens," *The Columbus Dispatch*, January 8, 2006, p. 17C.

28 For example, "Bikini Protester Ruffles Feathers," *Nelson Daily News* (British Columbia), May 4, 2006, p. 1; and Maria Levitov, "Bikini-Clad Activists Target KFC," *The Moscow Times*, August 2, 2006, and "Bare Boycott" *South China Morning Post*, November 6, 2006, p. 3.

29 Yitzchak Mokitada, quoted in Jenny Merkin and Yael Wolynetz, "KFC Diners Remain Unflappable in Face of Chicken Cruelty Protest," *The Jerusalem Post*, July 4, 2006, p. 5.

30 *FMI-NCCR Animal Welfare Program, June 2003 Report*, at www.fmi.org.p.2.

31 Eric Dezenhall, *Nail 'Em* (Amherst, NY: Prometheus Books, 2003), p. 80.

EXHIBIT 2
Yum! Brands Animal Welfare Guiding Principles

Source: www.yum.com (2004).

Food Safety: Above all else, we are committed to providing our customers with safe, delicious meals and ensuring that our restaurants are maintained and operated under the highest food safety standards. This commitment is at the heart of our entire operations and supply chain management, and is evident in every aspect of our business—from raw material procurement to our restaurant food preparation and delivery.

Animal Treatment: Yum! Brands believes treating animals humanely and with care is a key part of our quality assurance efforts. This means animals should be free from mistreatment at all possible times from how they are raised and cared for to how they are transported and processed. Our goal is to only deal with suppliers who provide an environment that is free from cruelty, abuse and neglect.

Partnership: Yum! Brands partners with experts on our Animal Welfare Advisory Council and our suppliers to implement humane procedures/guidelines and to audit our suppliers to determine whether the adopted guidelines are being met.

Ongoing Training and Education: Yum! Brands recognizes that maintaining high standards of animal welfare is an ongoing process. Training and education has and will continue to play a key role in our efforts. Yum! Brands will continue to work with experts to ensure our quality assurance employees and suppliers have the training and knowledge necessary to further the humane treatment of animals.

Performance Quantification & Follow-up: Yum! Brands' animal welfare guidelines are specific and quantifiable. Yum! Brands measures performance against these guidelines through audits of our suppliers on a consistent basis.

Communication: Yum! Brands will communicate our best practices to counterparts within the industry and work with industry associations such as the National Council of Chain Restaurants and the Food Marketing Institute to implement continuous improvement of industry standards and operations.

representatives from supplier companies. When the Council was set up, PETA recommended people acceptable to it as members and the company appointed four of them. In 2005 three of these panel members submitted to KFC a carefully prepared set of recommendations for promoting animal welfare. They suggested that consumers were becoming more conscious of humane treatment and the time had come to elevate standards for chickens. Their recommendations called for actions that would have satisfied all of PETA's demands.[32] At about this time PETA had suspended its campaign to engage in secret negotiations with KFC. After a series of meetings, it asked KFC to pledge it would carry out the panelist's recommendations, but it refused. Soon after, PETA renewed its campaign and two of the three resigned.

KFC STANDS FIRM

As the campaign moved into its fourth year, KFC stood firm. PETA's boycott seemed of little financial consequence. Yum! Brands does not break out sales by each of its restaurant chains, but its overall financial performance has been very strong. Between 2003 and 2005, revenue was up 12 percent and net income (a measure of profitability) was up 24 percent. Shareholders have fared well. If you had invested in Yum! Brands' on the day PETA announced its campaign, your shares would have risen 133 percent by its fourth anniversary, far exceeding a 52 percent rise in the S&P 500 over the same period.[33]

[32] "Animal Welfare Recommendations and Proposed Plan of action for Implementation at KFC Suppliers," memo from Dr. Iam Duncan, Dr. Temple Grandin, and Dr. Mohan Raj to Harvey Brownlee, Chief Operating Officer, KFC, March 11, 2005.

[33] January 6, 2003, to January 5, 2007.

During that time earnings per share rose 26 percent and the company would have increased your dividend by 48 percent.

Now and then KFC and Yum! let strong feelings about PETA show. At the beginning of the campaign a spokesperson promised that "just like the U.S. government we will not negotiate with corporate terrorists."[34] In 2004 Gregg Dedrick, who replaced Bachelder as president of KFC, said that PETA had "distorted the truth time and time again" in its "campaign of harassment, invasion of privacy and what I'd call 'corporate terrorism.'"[35] In 2006 a Yum! senior executive said, "we're not going to capitulate" giving as his reason that "PETA's ultimate goal is to end meat consumption."[36]

This comment points to an assumption, surely existing at KFC though unstated by the company, that meat eating is good. In this the company is supported by Richard Martin, editor of the industry magazine *Nation's Restaurant News*. Martin says PETA errs in its "rejection of the animal kingdom's remorseless food chain paradigm" and in its "repudiation of the worldwide acceptance of meat eating as a proper option for descendants of hunters. . . . "[37] This position is entirely at odds with the values of animal rights activists, including one who writes, "if we cannot imagine how chickens must feel . . . perhaps we should try to imagine ourselves placed helplessly in the hands of an overpowering extraterrestrial species, to whom our pleas for mercy sound like nothing more than bleats and squeals and clucks—mere 'noise' to the master race in whose 'superior' minds we are 'only animals.'"[38]

[34] Paul Holmes, "If KFC Wants to Combat PETA, Using Similar Over-the-Top Rhetoric Isn't the Best Method," *PR Week*, April 5, 2004, p. 7.

[35] "Press Conference Comments by KFC President Gregg Dedrick," July 21, 2004, at www.kfc.com, p. 2.

[36] Jonathan Blum, senior vice president of public affairs, quoted in Tom Price, *Activists in the Boardroom: How Advocacy Groups Seek to Shape Corporate Behavior* (Washington, DC: Foundation for Public Affairs, 2006), p. 11.

[37] Richard Martin, "Game of Chicken: Critics Say Capitulation to PETA Will Worsen Animal Rights Reprisals," *Nation's Restaurant News*, July 28, 2003, p. 31.

Questions

1. Do you support KFC Corporation or People for the Ethical Treatment of Animals in this controversy? Why?
2. What are the basic criticisms that PETA makes of KFC? Are they convincing? Are its criticisms similar to timeless criticisms of business mentioned in the chapter?
3. What methods and arguments has KFC used to support its actions? Is it conducting the best defense?
4. Is the range of PETA's actions acceptable? Why does the group use controversial tactics? What are its sources of power in corporate campaigns?
5. Is it proper for PETA to pressure KFC for change when the company is following the law and public custom? Does PETA represent so compelling a truth or enough people to justify attacks on, and perhaps damage to, major corporations supported by and supporting millions of customers, employees, and stockholders?
6. Do animals have rights? If so, what are they? What duties do human beings have toward animals? Does KFC protect animal welfare at an acceptable level?

[38] Karen Davis, "Animal Suffering Similar to Human Slaves," *Chicago Sun-Times*, September 6, 2005, p. 50.