For Release On Delivery
1:15 P.M., April 7

INTERNATIONAL CARTELS

An Address by

FRANCIS BIDDLE

Attorney General of the United States

At a Luncheon of
the
FOREIGN POLICY ASSOCIATION
Philadelphia Branch

Bellevue-Stratford Hotel

Saturday, April 7, 1945

Today there is a well recognized movement to get this country to adopt the cartel system. The Sherman Antitrust Act makes illegal cartel agreements which restrict the foreign commerce of this country. This is the policy adopted by Congress in 1890. The sponsors of the cartel movement say we must change this policy.

I recognize that there is very definite disagreement among Americans, and particularly American businessmen, on the whole cartel front.

For instance, the National Manufacturers Association has come out most vigorously against cartels; and only recently Mr. Pew, of the Sun Oil Company, in his annual report to the stockholders made it very clear that he was for open and unregulated competition in the oil field. On the other hand, the National Foreign Trade Council Incorporated, representing many of the exporting interests, has expressed itself as in favor of some modified and regulated cartel system.

It is hardly necessary for me to state that the Department of Justice is vigorously opposed to the cartel system, and to any proposed relaxation of our laws affecting cartels in international trade.

The world has had a great deal of experience with private agreements to restrict production or the marketing of goods, just as there is a long history of the attempts by government to manage private business. Cartels cannot be intelligently discussed without reference to this history.

Cartels are the attempts of private groups to regularize and stabilize trade. They do so by fixing prices, by determining through

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private agreements what the production of a given commodity shall be, how much each member of the cartel shall produce, and the conditions and terms upon which new enterprise may come into the industry. Cartels are an attempt to put each industry and each manufacturer into its proper place in accordance with a preconceived plan. This conception is known as control of the market.

This was indeed the theory of the medieval world. The medieval world, both from the economic point of view and from the standpoint of the relation of the individual to the community, was a well-defined and established organization into which each individual fitted and knew his place. It was shaped like a pyramid and based on a series of feudal classes running from the serf at the bottom to the squire, to the feudal baron, and finally to the sovereign. The system was not based on the belief in individual incentive, but on a carefully balanced order of caste and class. At the top, the king inherited prerogatives which gave him the right to treat large segments of trade as his own personal monopoly. He farmed them out at a large personal profit to himself. Workmen belonged to guilds whose prerogatives were inherited from the centuries. It was a system of security and stability.

There was no such thing as a free market and very little competition. Just as the individual's place in the community was recognized and fixed, so prices in the market place were fixed.

Immediately before the American Revolution, and indeed for some years thereafter, the prices of such everyday commodities as beer and bread were regulated by local ordinances. Massachusetts, for example, in 1696 provided that the weight of a penny loaf should vary according to a fixed scale with the price of wheat.

Indeed, it was government price-fixing which produced the first labor strikes in this country. In 1677 the street cleaners of New York struck not against capital or their employers but against price-fixing by the government. For a like reason, the coopers struck in 1680 and the bakers in 1741.

The Massachusetts General Court, in opposing any further governmental price-fixing, summed up the experience of the colonies and the states when it declared that these measures had

> "shut up our granaries, discouraged Husbandry and Commerce and starved our Sea Ports . . . created such a stagnation of business and such a withholding of articles as has obliged the people to give up its measure or submit to starving."

The system we know today is the product of a revolution against a "status society" and against limitations in production and distribution. On the political side, the revolution carried the banner of the rights of man. On the economic side, it was a protest against monopolies and restrictions which had been placed on the colonies. Indeed, Thomas Jefferson wanted to have included in the Constitution itself a prohibition against monopolies. Its economic philosophy was based on free competition. As such, it was the reflection of a liberal movement which had its eventual effect in England and Europe as well as in this country.

It was believed that a rigid regulation by the sovereign of what men could and could not do, or where they could live, or what they could produce, in addition to being contrary to the rights of free men, held down production and prevented trade and exchange from developing. If prices were not regulated, competition was freed and trade was opened to the vigor of new enterprise. If prices rose too high, lower prices from new and competitive sources brought them down. If, on the other hand, prices were below the cost of production, the producer would fail and the more fit would survive. The advantage was that you could do away with the rigid and arbitrary regimentation that had existed in the feudal world and in its place substitute a flexible and responsive law of economics which automatically exercised whatever regulation was needed. The free play of give and take, of demand and supply, was in itself all the regulation that the market required. In a word, the market was self-regulated.

This economic doctrine of <u>laissez-faire</u> dominated early nineteenth century economics and largely influenced our own development in this country. The views of Adam Smith, of the Manchester School, and of John Stuart Mill provided a theory in harmony with the desires of the growing commercial groups.

However, as the competitive market and the system of free enterprise superseded the feudal system, it became clear that certain abuses arose which were in themselves results of unchecked competition. <u>Laissez-faire</u> was ruthless if allowed to function with consideration only of the needs of competitors. Human labor, since wages were a very important part of the costs of a commodity, itself came to be considered a commodity. <u>Laissez-faire</u> unchecked disregarded human values.

In order to temper the rigors of the market and to prevent the abuse of human labor, factory reforms, bills to regulate the hours spent in work, laws dealing with dangerous occupations - such as coal mining, and finally old age compensation and mininim wage laws were enacted. The pattern of legislation in England, Europe, and in this country was much the same.

At the same time there developed in the economy the very monopolies which the new movement had attempted to abolish. They were no longer monopolies of the sovereign, but were created by private industry. During the period that followed the Civil War in this country, we were already faced with the danger of very large trusts dominating our economy to the exclusion of smaller business men.

The power of these monopolies and trusts was comparable to that of the medieval barons and sovereigns. They could effectively deny access to the market to the small competitor. They determined who was to be allowed to go into business, how much he could make and at what price he must sell. And because they dominated the market, they could by themselves determine the price which the consumer must pay. The situation which existed was described by Justice Harlan in his opinion in the <u>Standard Oil</u> case in these words:

> "All who recall the condition of the country in 1890 will remember that there was everywhere, among the people generally, a deep feeling of unrest. The conviction was universal that the country was in real danger from . . . aggregations of capital in the hands of a few individuals and corporations controlling. . . . , the entire business of the country, including the production and sale of the necessaries of life."

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The Sherman Antitrust Act did not seek to regulate monopolies or domestic cartels which fixed prices or allocated markets. Regulation would have required elaborate governmental management and direction. The Act on the contrary made monopolies illegal and outlawed cartels, foreign or domestic, which affected the commerce of this country.

The chief purpose of a cartel is to hold down production thereby maintaining or increasing prices, and to "regularize" the market rather than to expand it. It is for this reason that cartels are more often successfully applied in a shrinking economy than in an expanding one. And this would necessarily follow. In an expanding market, usually accompanied by rising prices, there is no necessity for protection and no scarcity of business. On the other hand, in a shrinking market with prices tumbling and purchases shrinking, the impulse to take protective means to hold back the spiral of deflation is natural.

I think that most of us are agreed that in the post war world, if we are to obtain anything like the size of our present economy and avoid an unemployment far worse than during the early thirties, it will be necessary for us greatly to increase our production in the year immediately after this war. Every businessman, every labor leader, every economist talks increased production. And yet, when we begin to examine methods suggested to bring about this increased production, it is surprising to find that cartels are being preached as valuable to a new and expanding world. Cartel agreements are intended to restrict production, and if American companies enter into them, the production of this country will be decreased.

The cartel looked at from one aspect is nothing more than a private tariff, and is peculiarly objectionable for that very reason. The cartel says what goods shall and shall not come in or go out of a country, and how much shall be added to their price for the privilege of import. That is exactly what a tariff says. A tariff excludes goods or allows them in only at a certain price. And a tariff is applied to protect home industry from the invasion of foreign competition just as a cartel is applied to protect the home producer from the competition of the foreign producers. But a tariff is adopted under the statute of a government, and expresses a government policy exercised for the national interest. A cartel is a private contract expressing the interests of a private group.

The loss of American markets through cartel restrictions can be documented by many examples. When the American companies stayed out of the International Tube Cartel, for instance, they were able to sell approximately 23% of the steel pipes bought in the Argentine. After the American companies joined the cartel, American export sales of pipes to the Argentine fell to about 5% of the Argentine market.

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The same thing went on in the rest of Latin America at a time when the German companies were doubling their position in that market.

Private agreements to create foreign spheres of influence and to keep American steel out of South America do not increase American trade. In the minutes of the London Committee of the International Steel Cartel for May 11, 1939, there is the following paragraph:

> "It was agreed that as the Argentine is not within the sphere of the American influence it should be eliminated from the list of Western Hemisphere prices which the American group has submitted."

International cartels inevitably breed domestic monopolies since they are dependent on domestic monopolies for their strength. An American company which cannot control its competitors cannot enforce a cartel agreement. It has nothing to trade. Its promise to stay out of a foreign market is worthless if other American companies will jump in and take the business. Therefore, when an American company bargains away the Latin American market, it assumes the obligation to police the domestic market. It must keep its competitors from exporting. For this reason international cartels are giant trade alliances between domestic monopolies. They are what Sir Alfred Mond of the Imperial Chemical Industries of Great Britain called "an armed truce between monopolistic groups."

Because a cartel agreement is at best an armed truce, it is exceedingly disheartening, particularly after the experience which we have gained from the events leading up to the present war, to hear it presented as a form of international cooperation which replaces the law of the jungle and brings peace and harmony to trade. It is the "peace and harmony" of the armed camp. Inevitably organized monopoly power in world trade comes to be used as an offensive weapon. Minor infractions of cartel rules produce retaliatory action. What should be treated as ordinary trade and commerce becomes a form of power politics. Thus when American steel companies offered their Swedish customers a lower price than exorbitant German prices, the German cartel members sent the following wire: "We protest most emphatically and reserve the right to take immediate counter-action in Mexico and South American markets provided American groups fail to relieve immediately and effectively unbearable situation."

Moreover in this armed truce the advantage lies with the largest producer. It is the fear of his productive capacity which has coerced the cartel into existence. In the hands of a dynamic society this advantage can be used to restrict the production of other countries while building up excess capacity constantly increasing the initial advantage. That is the story of the German domination over European industry.

The German use of cartels is, of course, well known. Only a week ago, the State Department in an official announcement stated:

> "Nazi party members, German industrialists and the German military, realizing that victory can no longer be attained, are now developing post-war commercial projects, are endeavoring to renew and cement friendships in foreign commercial circles and are planning for renewals of pre-war cartel agreements."

Mr. Milo Perkins in a widely read article in Harpers Monthly for November 1944, has spread a vague halo over cartels in the international field with the suggestion that they be registered under the discipline of the State Department. In effect, he would have us make the same mistakes Europe made. His arguments are worth examining because they present the typical pro-cartel view, stated in a somewhat confused form.

Mr. Perkins begins by pointing out that a "devastating case" has been made out against cartels in the past few years. He does not try to soften the hard realities about cartels in euphemistic terms, nor does he mistake their object and practices. They are, he says, controlled profit systems, and adds: "All cartels are in business to keep prices at levels which would not be held if free competition existed." He admits that they may endanger our military security. He does not like their attempt to control markets, and believes that "if goods moved freely after the war the world would have more production . . . more employment, higher living standards."

After having made out a pretty strong case against cartels, he concludes in the same breath that American business is helpless to compete with foreign business supported by the power of foreign governments, and that we must therefore either pull out of international trade or accept cartels and try to control them. "The pressure of circumstances," he says, "will tend to make us accept cartels because other nations accept them." He points out that several segments of our economy - fluid milk, coal, oleomargarine - have been taken out of the free market and that competition is already greatly restricted, but thinks we should go on fighting for free enterprise, though in what manner he does not suggest. He suggests that we should register cartels with the State Department, and approve or disapprove them on vague standards which include their effect "on our international trade, in sales, prices, volume and costs," and "on our domestic trade." This sounds like a highly technical administrative job. But apparently Mr. Perkins envisages a regulatory board which will glance at a cartel, determine whether it is "good" or "bad", and if "good" give it a sort of general sanction to operate, without fear of the anti-trust laws, until it becomes "bad".

Mr. Perkins would have us do what Europe did because we cannot help ourselves. We are caught in the wave of the future of the continent of Europe, according to Perkins.

Price fixing is one of the main functions of a cartel. The famous rubber cartel increased prices from 30 cents per pound in 1923 to $1.23 in 1925. Just how is the regulatory commission to determine what prices are fair? In a falling market is a price based on earlier costs a fair price? Is it fair to permit holding a price when a new cost-saving device threatens it? Is the standard of a fair price the least efficient or the most efficient member of the group?

Merely to suggest these questions shows what Mr. Perkins is in for if he wants actual regulation. Such regulation would mean a most intricate and elaborate system of minute analysis of cost accounting, labor standards, and profit supervision. We tried it under N. R. A. It failed. We are trying it now under OPA and while, under the pressure of the war need, it has proved on the whole successful, it involves tremendous administrative problems. The amount of paper work at present required by the Government of businessmen would be as nothing compared to what they would have to

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furnish under Mr. Perkins' regulated cartel system. Are we really ready for price-fixing in peace times?

Others, seeing this predicament, have suggested that the cartels regulate themselves, without any such interferences by the Government. But I cannot conceive of the public taking to a system under which business would be allowed to exclude competition, to create monopoly, and to decide, without any control, the extent of the profit, to which it would be entitled.

The net effect of Mr. Perkins' plan would have to be the control of profit of private enterprise by the government and minute supervision in order to make sure that technological advances were not being unduly retarded. Enormous discretionary power would have to be given back to the government.

And it would be impossible to maintain free enterprise for the domestic market. Not only do cartels presuppose and build up monopolies, but government regulation over a business could not stop with the export department. This is particularly true because if American companies, in order to raise domestic prices, are going to make agreements to keep out foreign goods, the government will have to keep a ceiling on domestic prices. And for all the fine expressions of standards, we would not only be putting a strait-jacket on American business, making any new business (with the idea no one believes in) an outlaw, but we would have committed ourselves to the idea of a shrinking economy.

An article in the London Economist puts the matter very well. The article notes restrictive practices in British industry cloaked under such euphemisms as "fair trading", "legitimate prices" and "organizing orderly means of distribution." And the writer adds:

> "All these fine phrases . . . taken together . . . are the chief reason why the productivity of British industry is falling so lamentably behind other countries."

But we are told that we have no choice. Why is that? For some years after the war we shall have more goods to supply than any country in the world. Europe, eager to reconstruct her economy, will be a ready customer. Already most of the European countries are negotiating enormous orders with us. For some time, we must be content with easy low term credit until the flow of European goods to us has been established - that is, if we want international trade. We must learn to consider ourselves as a great market for foreign goods as well as an exporter of our own products; that is, again, if we really desire international trade. The problem, for a while at least, will not be that Europe will be excluding our goods, but whether we will be ready to accept hers. The talk of Europe's excluding American trade, unless we agree to cartel restrictions, just doesn't make sense.

And in the period beyond can it be seriously urged that this country, with its enormous productive capacity and its large consuming market, is helpless in the face of the desire of some foreign monopolies to place restrictions upon us?

For example, in the early 1940's the steel production of the United States was equivalent to 72% of the total production of the principal foreign countries. In aluminum in some years our production has been equivalent to more than 70% of the other important producing countries, and in copper it was almost exactly equal to the remainder of the world. And even in those basic raw materials where the United States is not a large producer, it is usually a dominant consumer. We consume, for example, more than 75% of the world production of nickel and from 65% to 70% of all the tin mined in the world. Surely this country has a right to have its own economic institutions.

I sometimes doubt if the cartel advocates are doing Europe justice. Why should a continent which was held in the grip of a giant monopolistic system be assumed to be an advocate of that system in the years to come? Of course some of the monopolists have not changed their minds. But we have not yet heard from the people, from the ordinary businessman, from the men of vision who will reconstruct Europe with hope in new opportunities.

This country has become a symbol of political democracy. Because of our belief in political democracy we are opposed to excessive power whether it be in governmental or private hands. By accident or because of the power of our traditions, we have developed an economic system which with all its imperfections has been able not only to produce and to develop but has done so relatively free of governmental or private interference. Not only is our opposition to monopolies and restraints of trade, whether governmental or private, deeply engrained, but we have every reason to be proud of our endeavor and to hold fast to our course.

We think of cartels as being successful in the sense that they have been able to dominate their markets. But their history shows that unless they were able to include a very large percentage of the competitors involved, such control became impossible and they disintegrated because when any substantial competition intervened, it became impossible to hold the other members in line. So I venture to predict that the success or failure of the cartelization of foreign trade will largely depend on us, and that if we resolutely refuse to take part in it, cartelization will gradually disappear as a significant force from the international market.