

Chandler's Three Faces of Capitalism

H.V. Nelles

Alfred D. Chandler, Jr., *Scale and Scope: The Dynamics of Industrial Capitalism* (Harvard University Press: Cambridge, Massachusetts 1990).

HISTORIANS HAVE INVOKED "industrial capitalism" as an all purpose explanation for events from changing demography to student riots. As a group we have been less than precise about what exactly the dynamics of industrial capitalism were that drove social and political epiphenomena before them. That is the kind of big question historians have tended to ignore, preferring instead the case study or monographic approach. This, then, is an unusual book both for the scale of the question and the scope of the evidence considered. For after having devoted a lifetime to studying the rise of the large scale industrial enterprise in the United States, Alfred D. Chandler Jr. has in this book taken on the world, or at least in statistical and economic terms the better part of it. Between 1870 and the Great Depression the United States, Great Britain and Germany accounted for roughly two-thirds of world industrial production. Building upon a systematic analysis of the historical experience of these core economies with large scale industry Chandler ventures a global, deductive, intermediate-level, theoretical explanation of industrial capitalism.

The question implied in the title is modified and narrowed somewhat in the text. Essentially Chandler attempts to explain how big business got to be big and, just as important, how it stayed big. For what is striking about the comparative data Chandler presents is not only the structural similarities of the three economies but also where within each national economy large scale enterprises appeared (mainly food, paper, chemicals, petroleum, glass, primary metals, fabricated metals, machinery, electrical and transportation equipment). And once having been founded in these sectors, large corporations have proven to be remarkably persistent. There has been little change at the top over the years.

Though we may take the existence of giant corporations for granted, or assume their existence needs no particular explanation, it is a curious fact that both marxist

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and neo-classical economic theory lack a convincing explanation for the existence of the multi-divisional firm. Marx anticipated that the fundamental dynamic of capitalism was toward monopoly, a tendency he summed up in a trenchant passage: "One capitalist kills many." But what if at some point they stop eating one another and form more or less permanent oligopolies? Neo-classical economics also lacks a theory of the multi-product company. The theory of the firm assumes a single product company. Multi-divisional companies are thought to be examples of inefficiency or opportunistic rent seekers. In either case, the logic of the theory presumes them to be temporary. If, however, there are regularities in the incidence, character and persistence of such firms they cannot be dismissed as theoretical aberrations.

Through his career Chandler has struggled to fill this theoretical lacuna with a convincing *historical* explanation of the corporation and to defend the legitimacy of the corporation as a constructive economic agent by explaining what value it has added to production. He has attempted to use history to correct theory and explain business to itself and economists.

Chandler begins by building for three countries a comparative data base recording the histories of the two hundred largest corporations at three periods (during World War I, the late twenties, and the end of the Depression) using the US Bureau of the Census Standard Industrial Classification system. His sources are the standard Manuals and Stock Exchange Yearbooks, along with an extensive secondary literature — in some cases of extraordinary richness. His analysis of these 600 companies at three points in time confirms his earlier analysis of the US experience. At the same time his rigorously comparative method brings to light important regularities and differences between US experience and that of Great Britain and Germany.

There are elements to Chandler's model which are highly deterministic, but on the margin, he is quick to point out, culture and choice do impinge. Thus, while he identifies similarities in the development of capitalist institutions in the three economies, he also finds distinct differences as well. The regularities he deals with in Part I, a synoptic general statement of the rules which appear to be in operation in all three economies. There are, to be sure, similar underlying forces at work in all three countries. Then in exhaustive surveys of the stories of industrial growth in each country (organized by SIC double digit classification number to permit precise comparison), Chandler explores the particularisms of each local variant of capitalism. In Part 2 he outlines the distinguishing characteristics of what he calls "competitive managerial capitalism" that developed in the United States. Parts 3 and 4, which build upon this already well known theme, contrast the form of "personal capitalism" and "co-operative managerial capitalism" that characterized British and German development before World War II. His conclusion brings together the regularities and particularisms of industrial capitalism in the core economies and ventures a few observations about what was new and different about post World War II developments.

In basic language his argument can be reduced to a few propositions. 1. **Manufacturing matters:** this sector drives economic growth in core economies. 2. **In the industrial sector the large scale multi-divisional corporation accounts for most of the growth and is fundamental to the process of economic development.** "The manufacturing enterprises whose collective histories are presented in this study — those enterprises that were responsible for the economic growth of the world's three largest industrial nations — have provided a fundamental dynamic or force for change in capitalist countries since the 1880s," Chandler notes at the outset. "They remain today the core of their national economies." 3. **Management matters:** corporations get big and stay big by making a "three pronged investment in manufacturing, marketing and management." And the third element, management, is if anything, the key to it all. This book constitutes an extended answer to the question frequently encountered in the labour process literature: what do capitalists do?

The basic dynamics at work in all three countries are the same but they can be pursued in slightly different ways. In the process the national economies perform more or less successfully. At root there is a strong element of technological and economic determinism about Chandler's model. Technology permits new "flow process" production systems (examples would be branded food, packaged goods, refining, chemicals, steel, equipment manufacturing and so forth) which in turn create a framework within which the economies of scale (declining marginal cost curve), and subsequently of scope (diversification into related product lines or new businesses where the existing organization can add value) can be ruthlessly pursued. Scale opportunities in production are necessarily linked to the size and wealth of the market. Lastly, management must not only realize these economies, but also create the organizations essential to supplying, financing, co-ordinating, distributing, selling, servicing and diversifying production. There are the fundamental deterministic forces at work, but they must act through human agency. In a key paragraph near the beginning Chandler observes:

Because this study is the history of human institutions, I focus on the decisions within the institution that led to changes in production and distribution, rather than on changes in the broader economy as indicated by economic statistics — changes that resulted from such decisions. The institutional history told here is the outcome of innumerable decisions made by individual entrepreneurs, owners and managers. For these decision-makers the choices among alternatives were limited and outcomes uncertain, but almost always there were choices. Indeed, where they made decisions collectively, the decision makers disagreed as often as they agreed.

Capitalists could make mistakes. Henry Ford might have understood the logic of mass production, but he and his company failed in relative terms in developing the organizational capability essential to maximize their "first mover" advantages in

US and foreign markets. As a result they were overtaken by "challengers." Getting minimum efficient scale right was an inherently risky business.

Those who did make the triple investment in building and supplying manufacturing facilities of efficient scale, developing the marketing systems needed to dispose of these unprecedented volumes of goods, and structured their organization in such a way as to divide strategic management at the head office from multi-divisional operations — these "first movers" obtained almost unassailable competitive advantages that accounted for their persistence. Scale and scope once fully captured presented formidable barriers to entry. The "integrative hierarchy" of management could perpetuate the firm by investing in new product development and the creation of new technologies upon which a second generation firm could at a competitive advantage follow the logic of scale, scope or both upon new processes. Chandler thus provides an explanation of why giant corporations appear where they do, and why this form does not characterize other sectors of the economy. Labour intensive processes and industries serving small, specialized market sectors do not give rise to large scale, peak firms. There are good reasons why the General Motors' of the world do not arise in, for example, the furniture business.

These ideas will be familiar to those who know his earlier work, in particular *The Visible Hand: The Managerial Revolution in American Business* (1977), and *Strategy and Structure: Chapters in the History of Industrial Enterprise* (1962). Readers with long memories may remember my review of this oeuvre in an earlier number of this journal. Where *Dynamics of Industrial Capitalism* breaks new ground is in the extension of the analysis to Europe. In the process Chandler discovers subtly different kinds of industrial capitalism and offers what might be called an "organizational" interpretation of Britain's relative industrial decline.

Compared with the United States fewer large scale firms appeared, corporations in the key sectors emerged more slowly, and they failed to make the necessary strategic investments. In the capital intensive sectors accommodation between firms to stabilize market share and control competition rather than restructuring into large scale units characterized the British scene. Most important from Chandler's point of view, and a matter which he is at great pains to show, the salaried professional managers who guided big business in the US were not as prevalent in the UK. Managerial teams were smaller, organizations flatter and more specialized, and significantly "founders and their families continued to dominate the management of enterprises." For this latter reason Chandler believes that the short term considerations of maximizing dividend payouts to the founding families which characterized British "personal capitalism" inhibited the long term investment in production, distribution and management which eventually hobbled British industrialization. Over time Britain lost market share in the world, and international competitors drove British firms out of their home markets. This analysis of British entrepreneurial failure grounded as it is upon a cultural or sociological foundation will likely prove to be the most contested part of Chandler's work. Critics will

question whether or not other "non-cultural" factors such as resource endowments and size of the domestic market are given their due. By pointing to managerial failure Chandler challenges interpretations of British decline which have emphasized biases in the capital markets, labour force considerations and technological change. Although he admits much more work needs to be done on the subject, Chandler contends that by insisting upon personal control and immediate returns on investment, British families inadvertently sacrificed their long term corporate prospects and weakened the competitiveness of the national economy in the process.

German industrialists proved more farsighted and successful notwithstanding a smaller, and slightly poorer economy in terms of per capita wealth. There giant corporations of the America sort did emerge in the predictable sectors. Though the Germans were weaker in consumers goods, refining and rubber, they were world leaders in chemicals, electrical equipment and machinery. In these sectors German industrialists did make the essential investments in production, distribution and management. Indeed, these early strategic choices allowed Germany to rebound after the debacle of World War I and regain markets temporarily captured by British and American producers. Chandler not surprisingly traces the resilience of the German economy to the organizational capabilities of its industrial structure. An emphasis on producers' goods marked the main difference between the industrialization of the US and Germany. Chandler detected also a second difference in interfirm and intrafirm relationships, one which provides him with his nomenclature — "cooperative managerial capitalism." Co-operation between firms rather than aggressive competition, a mediating role or half-way house on the way to large scale capital provided by cartels, trade associations and other forms, and somewhat looser internal divisional structure within the large scale enterprises emerge as key distinguishing features of German industrialization. Thus Germany offers another version of the dynamic of industrial capitalism; it evolved in a slightly different way and within a different legal environment.

Banks also play a larger role than in either Great Britain or the United States. But even in Germany "finance capitalism" was subordinate to rather than dominant. Indeed banking and finance in general are relegated to supporting roles in all three countries. In almost every instance, Chandler argues, "Bankers preferred to remain bankers and to let industrialists run enterprises. Moreover retained earnings provided industrial managers with most of the funding needed to finance continuing growth."

Governments are also only of peripheral interest to Chandler and the subject of business-state relations, which figures so prominently in the Canadian and German literature, hardly figures at all in these pages. At the peak of the metropolitan economies governments did little to change the course of development in the industrial process. To be sure they provided the order, infrastructure, and macro-economic parameters within which companies must operate, but on balance Chandler concludes government could not do much to alter these processes. Rarely did

they finance or control production in this sector unlike, for example, utilities, transportation, or communication. Indirect intervention, such as tariffs, patents, and regulations could be accommodated and frequently assisted first movers as much as challengers.

What emerges with reasonable clarity from the vast thickets of detail is a picture of three national economies dominated in the capital intensive sectors by large scale, multi-divisional oligopolies of long standing. These first movers and successful challengers compete at home and abroad with each other. But further competition is provided by similar firms based in other metropolitan countries. Once the national economy had become oligopolized the most strenuous competitive challenges frequently arose from either similar companies in other countries (national champions) or large scale firms at home with the financial, technical, and organizational capability of penetrating diverse markets. Entirely new large scale firms appeared with major technological change, shifts in the source of raw materials or the demand for goods. And these changes, however dramatic, did not shake the stability of the structure much. Tough mergers and new entrants shifted the ranks of the top 200 companies somewhat, the persistence of large scale corporations is more typical.

The Dynamics of Industrial Capitalism constitutes a powerful rejoinder to the fashionable cant of the 1980s that giant corporations were really just dinosaurs, living out their last dying gasps. The sooner they were broken up and made more efficient, with fees all around to the merchant bankers, the better. These are the very firms that have driven economic growth, Chandler argues, and their organizational aspects have been the keys to that capability. Secondly, these firms alone possessed the capability of undertaking the research and development and investing in technology upon which future growth depends. By way of conclusion Chandler muses upon the deleterious effects for US capitalism of post-war era developments such as conglomerization, the loss of operation expertise among top managers, divestiture, merchant banking, pension fund capitalism, and corporate raiding. Meanwhile other corporations in other countries, not similarly distracted, have stayed the course mapped out here. To those who read Chandler as "modernizer," or a mere celebrator of the American way — this will be the temptation on the part of British readers — the conclusion describing the intensification of global competition serves as a sobering reminder that first movers, whether companies or nations, can be overtaken if they inflict self-imposed wounds.

Standing back a little from the sheer magnitude of Chandler's undertaking, several general observations come to mind. In the first instance the great lumbering engine of industrial capitalism, whose laws of motion he describes, leaves small markets and therefore small countries to one side. Marginal producers will eventually be trampled either by branch plants or direct exports. This casts the Canadian debate over foreign investment into an entirely new light. If, in these sectors, metropolitan oligopolies are destined to triumph, local capitalism is necessarily shunted into the less profitable and less technologically dynamic labour intensive

sectors. A pessimistic future for capitalism in small countries is thus assured unless capitalists are able to overcome the disadvantages of small scale local markets either by developing a unique natural endowment or competing vigorously for international markets. *The Dynamics of Industrial Capitalism* poses a bleak challenge to students of Canada, even French, and other second rank economic powers.

While the deterministic factors making for uniform institutional development are, on the whole, convincingly adumbrated, the linkage of the cultural and sociological to his dynamic is less clearly established. I think Chandler himself would agree with this. At the outset, for example, he points out that even in 800 pages he could not address fully the legal, educational, and cultural environment of enterprise. And he ends with the hope — and it is more than false modesty to be sure — that at every level in each country more work might be done to “alter and enrich the explanatory theory derived from the patterns of dynamic change recorded here.” It is not entirely convincing to be told that British industry failed because its ruling families paid too much attention to minding the store. The British and German patterns correspond altogether too neatly with preconceived stereotypes. That does not make them untrue, rather merely suspect. On the margin, culture is made to bear quite a heavy burden of responsibility without a correspondingly robust theory to support it.

Readers of this journal may be repelled by — among other things — the almost total neglect of labour as either a factor of production or an actor in the making of corporate capitalism. Chandler pleads that “the labour story” along with such other important factors as government relations must be left to others. But in truth, insofar as labour is concerned, Chandler here as in *The Visible Hand* considers it an operational rather than strategic consideration. In the period discussed organized labour lacked the power to alter fundamentally the forces of production. Nor as a political factor did labour impose itself. This will be something working-class historians and others may well dispute.

Chandler does not enter the lists either on the larger question of the political dimensions of corporate growth. For example on the question of big business and its relations to Nazism, Chandler is silent, although by implication he might be interpreted as arguing that national socialism represented a deviation from “cooperative managerial capitalism” rather than its culmination. Nor does Chandler have much to offer directly to the debate over the role of industrial capitalism in the shaping of US foreign policy. In this case as well his silence might be taken as an indication of the relative autonomy of politics.

Finally, a thought about method. “Story” is one of the most frequently used words, as in the German “story” or the Pilkington “story.” And each story has a meaning, some even a moral, which added to all the other stories make a pattern. Chandler is a narrative historian. But in this subject he reaches the margins of narrative. Can the similarities and differences between large scale systems be revealed by narrative alone? Certainly the telling and retelling of fragments of

stories gives the impression, like a pointillist painting, of patterns emerging. The repetitiveness is not only numbing, the space consumed precludes full treatment of contingent factors. Those who might choose to follow Chandler or to test his generalizations, will not likely chose his laborious and somewhat circuitous method.

Nevertheless Chandler in this magisterial volume presents a daunting challenge to scholars in many related disciplines and in other countries. He has made a compelling case that the corporation has a function; that it has its roots in economies of scale and scope which are themselves socially and technologically determined; that manufacturing matters, and above all that management matters. Culture affects the style of management for better or for worse but it is organizational capability that plays the leading role in determining the success or relative failure of national economies.

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