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The United States Steel Company, 1890-1920: An Examination of Economic Cooperation and Competition

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Beginning in 1890, business and government engaged in a symbiotic relationship which juxtaposed congressional regulation and judicial precedence with the free-market tendency for profit and power, and which subsequently became an indisputable hallmark of American society. To modern businessmen and government policy makers, government regulation that alters and controls the structure of corporate organizations and the decisions of their managerial hierarchies is often contested. On July 2, 1890, Congress passed the Sherman Antitrust Act in reaction to the cartels, pools and trusts which had begun to stifle competition and produce monopolistic organizations in the American economy. These trusts and holding companies had the potential to control the prices, production and constitution of diverse markets, especially in the railroad and oil industries. Specifically, Section 3 of the Sherman Act prohibited "every contract, combination in form of trust or otherwise, or conspiracy, in restraint of trade or commerce." Thereafter, the federal government's position as regulator of American business could not be questioned. The case against U.S. Steel, regardless of its outcome, established the resolute hold of federal regulators on corporate decisions relating to market positions and monopolistic control.

The United States Steel Corporation, founded in 1901, was a holding company for 12 subsidiaries in the iron, coal, railroad, steel, wire and mining industries. Elbert H. Gary and the Board of Directors of U.S. Steel wielded ultimate control over all the subsidiaries and their maintenance of prices and output which fundamentally made these once competitive industries, cooperative. These subsidiaries included: Carnegie Steel, Federal Steel, Minnesota Iron, Duluth & Iron Railroad, Loraine Steel, Illinois Steel, American Bridge, National Tin Plate, American Sheet Steel, American Steel & Wire, National Tube and American Steel & Hoop. Most of these subsidiaries had subsidiaries of their own, including the Carnegie Steel Company, which owned multiple iron ore fields, blast furnaces, steel works, rolling mills and coke works, as well as large percentages of stock in other competing companies. After its incorporation, U.S. Steel possessed a 60% market share of steel production in the United States, an 80% market share for wire, and 100% of the critical Duluth, Mesabi and Northern Railroad.

The House of Representatives investigated the activities of the United States Steel Corporation to determine if such a huge incorporation of busi-
nesses involved in the production of steel from the mines to the consumer was an attempt to monopolize, or if competition in the steel industry had subsequently been stifled. From the House investigation, which included testimony from managers inside and outside of the company, it can be argued that the U.S. Steel Corporation had engaged in a "restraint of trade" and their activities as a dominant oligopolist replaced the "invisible hand" of the marketplace with industrial pools, price discrimination, and their immense conglomeration of subsidiaries as prohibited under the Sherman Act. The case, *United States v. United States Steel Corporation* (1919), was the culmination of the House investigation and several years of discovery. Although U.S. Steel was not found guilty of monopolistic intent, this case is indicative of the Federal Government's attempt in the late nineteenth and early twentieth century to establish judicial precedence with respect to anti-trust legislation.

The House Committee on the Investigation of the United States Steel Corporation provided concrete evidence on the activities of U.S. Steel during the time period of its incorporation to 1912. The advantage of such an investigation is that it was conducted during a time where records of business activity were infrequently released to the public. Three testimonies from these hearings will be considered which provides a variety of opinions and expertise. During the initial proceedings of the investigation, the testimony of J.W. Gates, stockholder and director of the Tennessee Coal and Iron Company, provides an exceptional perspective on U.S. Steel's activities. This was in large part due to the fact that Tennessee Coal, originally a competitor of U.S. Steel, was acquired by the company in 1907. The testimony of Mr. Elbert H. Gary, Chairman of the Board and CEO of U.S. Steel from 1901 until his death in 1927, also contributes an invaluable perspective on the inner workings of the company and its subsidiaries. Finally, the testimony of Andrew Carnegie, founder of the Carnegie Steel Company, will be addressed. These proceedings, in conjunction with other sources, will contribute to an analysis of U.S. Steel's questionable activities and its subsequent reaction to the legislation and litigation proscribed by the Federal Government.

The U.S. Steel Corporation's large market share was the result of managerial decisions to control steel prices by acquiring other steel-producing companies, finished product manufacturers and suppliers of ore. According to Gates, the acquisition of Tennessee Coal and Iron resulted from an attempt by U.S. Steel to stabilize steel prices by obtaining a majority market share through the purchase of other steel companies. Gates stated, "the control of the market necessitated getting a majority of the producers." Section 2 of the Sherman Act reads, "every person who shall monopolize, or attempt to monopolize ... shall be deemed guilty of a felony ..."

The proscriptions initiated by the Sherman Act stand in stark contrast to the actions taken by U.S. Steel and its acquisition of 60% of the steel market and over 80% of the steel wire market. However, before the *U.S. v. U.S. Steel* case, Section 2 was interpreted as stating monopolistic intent on behalf of a
The United States Steel Company

corporation (with or without a corresponding market share) was a felony and punishable as such. Mr. Justice McKenna ruled in U.S. v. U.S. Steel that the U.S. Steel Corporation had not obtained a large enough share of the steel industry to warrant the term monopoly. U.S. Steel’s lack of excessive power compared with Rockefeller’s Standard Oil Trust or American Tobacco, directly influenced the Court’s decision to acquit U.S. Steel in 1919.

J.W. Gates and Elbert Gary both testified that the power and size of U.S. Steel was large enough to drive all competitors out of business, particularly by their ability to control prices, ostracize competitors and discriminate on shipping rates by railroads owned by U.S. Steel. Gary reported, “we could drive a good many of our competitors our of business,” seemingly contradicting the stipulation in Section 2 of the Sherman Act prohibiting such a potentially disastrous exertion of power to control an industry. In a more resolute statement, Gates admitted that, “U.S. Steel could put all others out of business.” The dominance over steel and iron markets that U.S. Steel exerted can be more fully appreciated by understanding the nature of its subsidiaries prior to consolidation under U.S. Steel’s control. When the Carnegie Steel Company was purchased to form U.S. Steel, it produced all major finished steel products except hoop, wire, light sheets and tubes. Federal Steel Company, also acquired by U.S. Steel, produced all of the same finished products as Carnegie Steel. In essence, they were direct competitors until they secured common ownership under U.S. Steel. With the purchase of the Tennessee Iron & Coal Company in 1907, U.S. Steel gained Republic Iron & Steel, Birmingham Southern Railroad, Sloss-Sheffield (pig iron ore) and Woodard (pig iron ore.) U.S. Steel gained 15% of the market share for steel after the acquisition of Tennessee Iron & Coal.

The impact of U.S. Steel’s prowess in a number of diverse marketplaces is easily illustrated through examples of their managerial decisions. Prior to the incorporation of U.S. Steel, the Carnegie Steel Company depended on a number of buyers for its refined steel, including National Tube, American Bridge, American Steel & Wire and American Steel Hoop. These independently owned customers of Carnegie Steel had planned to vertically integrate their organizations and supply themselves with steel. However, upon realizing that an amalgamation of these firms would occur, plans for vertical integration, which would have reduced finished product prices for these firms, were canceled. The effect of this competitive re-alignment would certainly reduce Carnegie’s position as a monopolistic supplier to business buyers.

U.S. Steel’s apparent abuse of its dominant position in the marketplace was exemplified by a contract that U.S. Steel’s managers pressured Pittsburgh Coal & Coke to secure with U.S. Steel. This 25-year contract required Pittsburgh Coal to sell steam coke to U.S. Steel for nineteen cents less than their original production costs for every one-hundred pounds of coke. The cost of producing one-hundred pounds of steam coke was $1.26. According to E.H. Gary, U.S. Steel was buying this coke for $1.07. In return, U.S. Steel had
promised Pittsburgh Coal and Coke that it would not enter the steamship business in Pittsburgh, in which Pittsburgh Coal had secured a monopoly. As a result of this arrangement, U.S. Steel gained an unfair competitive advantage in obtaining steam coke, while Pittsburgh Coke remained a monopolist of the steamship industry in the Pittsburgh area.

Another poignant example of U.S. Steel's role as an immense conglomerate (i.e. possessing a well integrated system of subsidiaries and interlocking directorates) was provided by the railroad organizations that became the property of U.S. Steel after its inception. U.S. Steel owned the Elgin, Joliet & East Co., the Bessemer & Lake Erie Co., the Union, the Southern, the Chicago, the Lake Shore & East, the Duluth & Iron and the Duluth, Mesabi & Northern Railroads. Strategically, the advantage of owning these roads is evident in the following example. The Duluth, Mesabi & Northern Railroad Co. was the only viable mode of transportation from the richest iron ore fields in the U.S., the Mesabi Range in Minnesota, to Pittsburgh, the center for the conversion of iron ore into steel. After gaining control of this railroad, U.S. Steel raised the freight rate per ton of ore to 62 cents per 30 miles of haul. The railroad from Michigan to Pittsburgh, the Marquette, Menominee and Gagebic Railroad, is a comparable road, with similar demand. Its price for 80 miles of haul is 80 cents per ton of ore. This produced more than a 100 percent difference in the per mile freight rates, made possible by the monopoly that U.S. Steel had over this crucial line. In fact, Gary testified that his corporation controlled all outlets from the entire Great Lakes region which secured an awesome competitive advantage over other steel and coal producers. The dividends garnered by U.S. Steel from price gouging on the Duluth, Mesabi & Northern Railroad were 152% in 1904 and 40% in 1906. The increased freight prices disadvantaged U.S. Steel's competitors by an average of $2 to $3 per ton over the length of an average haul, as corroborated by the testimony of J. W. Gates. U.S. Steel, functioning as a parent company for a number of steel producers who controlled ore mines on the Mesabi, remained unconcerned about the overcharge because this sum, like all the revenue of its subsidiaries, returned to U.S. Steel's accounts at the end of the year.

Further accusations as to the immense size of U.S. Steel and its unfair advantages within the steel industry were directed at the excessive market capitalization of U.S. Steel. At its inception in 1901, U.S. Steel was capitalized at $1.7 billion dollars. An argument was made by the House Committee, that this was an over-capitalization of the actual value of the capital, labor and land that U.S. Steel owned in 1901. According to Gates and the House Committee, this tremendous capitalization rested on the premise that the size of U.S. Steel would produce unfair competitive advantages in the marketplace. In U. S. Steel's publication, *US Steel News*, this immense power is referred to as the, "important advantages in complete control of all operations from ore and coal to a full line of finished products." In this publication, the editor, G. L. Lacher, proudly notes how the formation of U.S. Steel stifled the same "cutthroat" competition the Sherman Act was attempting to
The United States Steel Company

preserve in the marketplace. Additionally, the Carnegie Steel Company was capitalized at $320 million dollars, while outside auditors estimated its value at $75.6 million.20 Gary’s testimony revealed that the Tennessee Iron & Coal Company was capitalized at $11.9 million when he had estimated its value a year before at not more than $6 million. According to testimony by Andrew Carnegie, the U.S. Steel Corporation capitalized its ore holdings at $700 million when an independent auditor had approximated the value at $100 million.21 In essence, this difference was a speculation by the investors of U.S. Steel on the potential competitive superiority that it would profit from after its incorporation. This immense over-valuing of its operations provided blatant proof of U.S. Steel’s competitive advantage in the steel market in the United States, primarily because such massive capitalizations indicated a prediction that the market would be dominated by this powerful firm.

In order to comprehend the questionable practices of the U. S. Steel Corporation with respect to anti-trust legislation more fully, an analysis of prices will be necessary. Both the actual numerical data of steel prices provides evidence of collusion, as does the qualitative testimony of Gates, Gary and Andrew Carnegie with reference to price pools, cartels and the “Gary Dinners,” which will be covered later.

Before 1901, the fluctuation in the price charged for a ton of rails varied between $17.62 in 1898 and $32.29 in 1900.22 This dramatic increase was purportedly caused by the optimistic outlook of steel manufacturers who foresaw stability and relaxed competition with the advent of U.S. Steel in 1901. Gary was quoted (in reference to steel prices of the late nineteenth century) during the House Committee in 1911 as saying, “I would say that prices are more erratic then, than they are now.” Similar consequences erupted from Federal Steel’s incorporation in 1890, which tied together a number of steel firms and suppliers, causing the price of a ton of steel rails to raise from $17.50, to $33 immediately after its formation.23 In fact, steel prices in the United States stabilized at around $28 per ton after the creation of U.S. Steel in 1901, in essence proving U.S. Steel’s formation reduced competition and allowed a single firm to dominate the market in price and power. These figures become more fascinating when contrasted with the estimate made by Andrew Carnegie in the Empire of Business. In this text, Carnegie argued that $15 per ton is a very reasonable estimate of the cost to produce rails.24 Additionally, testimony by Charles Schwab, an investment banker involved in steel and railroad concerns, estimated the cost to produce a ton of steel at $12.50.25 Carnegie’s price throughout most of his tenure as director and owner of Carnegie Steel Company was $13 or less per ton which significantly increased the competitiveness of the steel industry before 1901.26

In comparison to its pricing decisions in the United States, U.S. Steel charged $4 per ton lower in Mexico and Australia, among a number of other markets. The more intense competition in these areas, where cartels and pools were not in practice, forced U.S. Steel to lower its prices in these markets. The effect of the U.S. Steel merger on prices was not isolated to the
steel market. American Tin Plate, which produced coke (among a number of finished products,) raised its price for coke from $2.70 per 100 pounds in December of 1898 to $4.84 per 100 pounds in December of 1899 in anticipation of the stability of coke, steel and other related markets after U.S. Steel's formation.27

J.P. Morgan and other U.S. Steel investor's ostensible reason for creating U.S. Steel was to reduce the instability of prices that had occurred before 1900 for the alleged sake of consumer and producer satisfaction. U.S. Steel, in its trade journal bearing its name, pointed to the "destructive effects of cutthroat competition."28 Contrary to Carnegie's philosophy of setting competitive prices (achieved by economies of speed, i.e. running mills at full capacity), U.S. Steel's strategy was to secure a market share extensive enough to control prices merely by coercion and the use of its very well integrated subsidiaries. Specifically, these subsidiaries frequently ostracized and threatened competitors and suppliers that did not conform to the established rules and procedures of the trade associations and cartel arrangements. The House Committee accused Gary of coercive practices which commonly took place amongst suppliers who threatened to charge high prices for one product, "X", if another product, "Y," was not bought from that same supplier. Gary was unable to identify specific instances of such practices.

Section 3 of the Sherman Anti-trust Act specifically prohibits pools, cartels and other forms of contracts which restrain trade. The U.S. Steel Corporation, in an effort to control the volatility of prices in the steel market of the United States, began a series of dinners where the majority of steel producing concerns in the U.S. were represented. In fact, approximately 95% of the market share of the United States was accounted for in this trade association. These dinners were a primary focus of the House Committee during the investigation of U.S. Steel, and were termed the "Gary Dinners," after Elbert H. Gary.29 The precursor to these dinners was the Bessemer Steel Association, prior to the anti-trust act and until the incorporation of U.S. Steel. Carnegie admitted to his attendance at these meetings and to his knowledge of Carnegie Steel Co. managers' attending at those meetings when he was unable to be present. Although the Bessemer Association blatantly attempted to regulate prices, profits and production in the steel industry, Carnegie usually attempted to subvert these efforts by offering kickbacks in the form of free spikes and bolts, necessary for railroad construction. The nature of this association was considerably less dictated by a single entity, as was the "Gary Dinners."

The Addyston Steel Pipe case (1899), which was heard in front of the Supreme Court, clearly established the illegality of pools, particularly in the steel industry. Although Gary initially denied making concessions about price manipulation and output restriction with other steel manufacturers during the Gary Dinners, he eventually admitted to raising prices and establishing tacit agreements to stop competition.30 These pooling arrange-
The United States Steel Company

ments seemed to be effective considering that no price below $28 was ever set after 1899 for a ton of rails. Gary stated that a floor price of $28 was established, "as a result of conferences and discussions between the steelmakers as to what would be a fair price." Prices were set, Gary claimed, as the result of, "an interchange of opinion." Although U.S. Steel was by no means ruthlessly tyrannical in these "interchanges," the hegemony that they established allowed for the collusion of steel prices. Gary was quoted at one of the dinners in 1911 as saying, "we are bound to protect one another," a distressing violation of the principles set forth by the Sherman Act.

U.S. Steel, however, was vindicated by the Supreme Court in 1919, and the questions of pooling arrangements, price gouging and monopoly power were justified by U.S. Steel lawyers as cooperative arrangements, not maliciously intended to destroy competitors as in the case of Standard Oil and American Tobacco. The Supreme Court barely exonerated U.S. Steel with a vote of 4 to 3. The principal reason U.S. Steel was found not guilty was fundamentally due to their amiable demeanor when dealing with competitors, House investigators and customers. The Supreme Court found that the American steel industry warranted cooperative measures in order to sustain productivity and fair prices. The steel industry, primarily as a consequence of this investigation which influenced managers and corporate attorneys to cease all antitrust activity, became more competitive. U.S. Steel’s market share fell from 65% in 1907, to 52% in 1915, and to 38.3% in 1936. Additionally, the Gary Dinners immediately ceased during the House Investigation and thereafter, due to the potentially contentious methods that could be employed by the Department of Justice in the future. Gary’s training as a lawyer and a justice undoubtedly influenced his decision to end the pooling of prices in the steel industry which subsequently fell as low as $18 a ton after the pooling ended. U.S. Steel also made sure to comply with all federal regulations in the future, particularly with regard to their participation in World War I and World War II. Gary’s diplomacy was invaluable to the U.S. Steel case, especially with respect to his procedure of open disclosure of all balance sheets, memos and other relevant documents. Gary, during a surprising revelation of his personal convictions, admitted to supporting a measure that would allow the federal government to control price ceilings and floors, the amount of production to be manufactured and what would constitute a reasonable profit based on cost.

The progress gained from the acceptance of government regulation and the establishment of business communication was essential to the precarious relationship between industry and government that shapes the American economy. Ultimately, the federal government determines the organizational structure and competitive environment that industries will participate in. Managerial capitalism in the United States, because it is regulated by Congress and the Supreme Court, plays a dynamic role of testing and abiding by the legislation and litigation of the federal government. In the process,
corporate organizations create the future economic and political environment within which they will engage. This symbiotic relationship was aptly described by Carnegie in *The Empire of Business*:

"Given the freedom of competition, and all combinations or trusts that attempt to extract from the consumer more than a legitimate return upon capital and services, write the character of their own defeat."

While corporations driven by capital and labor relentlessly pursue profit and power through combination and expansion, government regulation ensures that the allocative and distributive efficiency of the free market economy is preserved for the benefit of consumer, employee, organization and shareholder. The dynamic equilibrium of any efficiently regulated economy must necessarily reconcile this motive for profit and its somewhat antithetical counterpart, administrative legislation.

**Notes**

7. Duggan, 299.
8. Neale and Goyder, 103.
10. Ibid., 143.
11. Ibid., 46.
12. Ibid., 155.
13. Ibid., 115.
15. Ibid., 52.
16. Ibid., 80.
17. Ibid., 142.
18. Ibid., 7.
21. Ibid., 2398.
22. Ibid., 231.
23. Ibid., 87.
26. Ibid., 36.
27. Ibid., 28.
30. Ibid., 74–76.
31. Ibid., 92.
32. Ibid., 267.
34. U.S. House of Representatives, 220.
35. G.L. Lacher, 4.
36. Ibid., 3.
37. U.S. House of Representatives, 236.