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THEORY OF MARKETS AND MARKETING

by

Henry H. Bakken

University of Wisconsin

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Madison, Wisconsin

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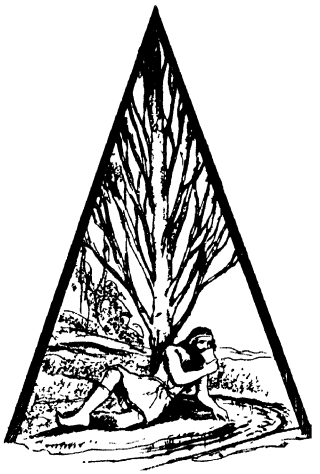

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PREFACE

THE ever increasing flow of goods and gadgets which emanate from the farms and the factories in this technological age has taxed our market facilities and their *modus operandi* to the limit. Advancements in the sciences of production still appear to be transcending those in the arts of distribution even in the underdeveloped areas of the world. Rapid expansion of trade and industry in some regions has made it necessary to impose a number of changes on existing market organizations and systems of distribution, but many more innovations of a basic nature are needed to elevate the plane of market services to a level equal with that of production.

Pioneer writers on the subject of marketing relied primarily upon general economic principles for their idees-forces, and some authors still favor this view. In recent years a gradual defection from this concept of the province of marketing has been evident. A prevailing idea held by a number of scholars is that the subject matter is too narrowly circumscribed by the traditional framework of economics. Transactional negotiations are so extensive in nature and of such deep significance to everyone that they require a special array of precepts enlarging the domain of the science of marketing. This formulation presumably will be interrelated with the applicable doctrines of other social sciences. Market theorists assume the task of collating, co-ordinating, test-

ing, and modifying these precepts for the purpose of analyzing both general and particular situations, and suggesting possible solutions.

The author's intention in this book is to present in broad outlines a general theory of the evolution of market institutions, their structure, purpose, functions, and inherent characteristics. His objective is sought in what may be considered an unorthodox manner by calling into play a combination of disciplines such as economic history, law, and institutional economics. This series of avenues to the subject appear to have more than usual merit. It makes possible setting up in apposition different views and arranging them in sequence according to their relative fire-power in what might be called the battle of the approaches. Such a contrast between the traditional and the unconventional entrees to marketing should provoke and intensify inquiries into the subject both inside and outside academic circles. The distinction between marketing functions and those of production economics has long been vague, and to many a source of bewilderment. When considered from the legal and the institutional point of view, the two are dichotomized and the relationship becomes more conclusive. Another advantage of special value attained from blazing new trails of entry to the subject is that they are distinctive and in some degree incisive as points of departure for planning and executing market research on a scientific basis.

Price formulations and value determinations in all their ramifications are generally of paramount interest to everyone concerned with marketing. Attention is given to special phases of the subject in various places throughout this volume particularly in chapters 4, 7, 10, and 11. It was not deemed necessary, however, to restate the neo-classical and the mathematical concepts of pricing since these views are rather fully expounded in a number of excellent publications.

While the range of subject matter and the heterodoxy of ideas in this first edition may seem sweeping, they serve the purpose of staking out a common claim for future diggings. Any traces of over modesty either in design or methodology are assuredly unintentional for no one fully realizes the possible lapses and limitations more than the author. These aberrations occur as the price of brevity or they are the scions of overconfidence nurtured by countless miles of travel, enumerable months of research in the field and libraries, or years of testing various generalizations in the classrooms attended by scholars from many countries of the world.

Acknowledgement and deep appreciation is extended to my colleagues in law, commerce, philosophy, history, and economics for their encouragement and for their helpful suggestions. My greatest debt, however, is to the many students who assumed an active part in appraising and testing the ideas which are reproduced on the succeeding pages.

Henry H. Bakken

Madison, Wisconsin
January 27, 1953

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PART I

THEORETICAL BASES

THEORY OF MARKETS AND MARKETING

Introduction

Contemporary markets represent survival forms of organization that have withstood all the corroding influences of time. Various discoveries by research workers in the different branches of the Social Sciences have shed new light on the evolutionary nature of markets revealing significant changes in their character and functions through the ages. From these findings, one learns that the market institution was a relatively mature socio-economic invention centuries before the Christian era. Clay tablets have been found in the ruins of ancient cities along the valley of the Tigris and Euphrates which disclose amazing facts about long caravan routes extending into other lands eastward and westward, business partnerships, kinds of goods offered for exchange, legal agreements and contracts, and formal trade customs prevailing among middlemen five thousand years before our time. The early perception and the enduring persistence of market institutions can be attributed to the indispensable means and services they have provided man in securing some of the refined necessities of life which otherwise might not have been attainable.

Market organizations can be found in all stages of development today owing to the uneven degrees of social and economic advancement extant in the nations of the world. This general cross-section view of markets show-

ing progressive gradations of development as they have come down to us from the past, range from a system of ceremonial gift-giving which prevails among certain primitive tribes in the Southwestern Pacific to the highly formalized modern produce exchanges dealing exclusively in futures contracts. A knowledge of these variations in organization forms for peoples of different racial and cultural origins gives one an historical perspective which compliments the general theory of marketing. The application of these concepts in the ebb and flow of human affairs in barter and exchange transactions from time immemorial constitutes at least two rich veins of source material that have been mined only superficially by students of marketing. Figuratively, the vein bearing the richest deposition is the one containing the basic principles and ideas on which our market institution is founded. Exploratory prospecting of this source will be our immediate concern in defining a market and presenting a version of its purposes and character. The second vein assumes the position of a drift denoting its relationship of dependence upon the former. It is to be identified by its narrative content of human affairs and experiences. These factual accounts of the past supplement the main theme under consideration by providing a psycho-social environment and a vivid background that will enliven the subject and infuse it with the substance of reality. This source, for two reasons, should be tapped with moderation in outlining and arranging the theoretical precepts of a market and its functions of exchange. On the one hand, it is assumed that the meticulous details of history have only a limited appeal to impatient youths and to the assiduous men of business. On the other hand, much of the documentary information supplementing the main thesis of this work is reserved for later consideration because it would lose significance if

lifted out of its setting and if torn away from the sequence of other events in the period of its origin.

Consequently, the chapters treating with the origins of markets have been set over to part II of this book. Those who prefer tracing the evolution of our market institutions in historical sequence should read chapters 12, 13, and 14 before turning to the main thesis of this text.

The function of marketing taken up in the first chapter presents familiar terrain to those who have had either a formal or informal introduction to the subject, and it serves to join issue with other points of view. The environment within which the forces of exchange operate has been something of a nemesis to most students of the subject considering the numerous and varied definitions presented to explain what a market is. The concept of the market in this writer's opinion should be sharply delineated from the precepts of production for analytical purposes. If marketing as a field of specialization within the social studies is to attain the status of a science of exchange, it must of necessity be recognized that it embraces and influences a much greater area of human endeavor than has hitherto been ascribed to it. The purpose of this book is to seek out some neglected areas of consideration and to open to view other great potentialities through new approaches to the subject.

1

THE FUNCTION OF MARKETING

IN the formative years of this field of specialization in economics most of the writers conceived the function of marketing as an indistinguishable relationship so closely interwoven with the processes of production that the functions of the two could not be dichotomized. This idea was popularized by the dictum that "marketing begins with the selection of good seeds and sires." Some textbooks on the principles of marketing were almost entirely dedicated to this thesis. In the course of time, this interpretation of marketing became less tenable as the principles of production economics were more precisely formulated. It had never been made clear exactly how elemental utility could be considered a result of exchange. In some quarters it had been accepted as a fact simply because some writers had declared it inclusive. The yielding of this point opened the way to challenge the inclusion of form utility as a realization of marketing. A number of market theorists rather reluctantly ceded this point affecting the traditional subject matter classifications because they still held to their original conviction that production and exchange were ostensibly inseparable. It was conceived, eventually, that form utility was primarily a function of manufacturing and processing which involved changes in the form of

materials. This means of production was not greatly different in many respects from the creation of elemental utility. Later the authorities became reconciled to the view that a dividing line should be drawn somewhere between producers and consumers to indicate which phase of economic activity held sway at any particular moment. The question naturally arose as to whether the dichotomy occurred sharply at some critical point or whether the line of separation was blurred and possibly overlapped.

The chaos which still prevails among writers in interpreting marketing functions is evident from the text of one group of authors to wit:

> "There is no standard group of them — *(services as components of marketing functions.)* It therefore remains for us to treat only those which seem to be most important and most generally regarded as indispensable parts of the marketing process. The following list seems to include all of this character:
>
> | | |
> |---|---|
> | Merchandising | Assembling |
> | Buying | Financing |
> | Selling | Traffic Management |
> | Standardization and grading | Storage |
> | Risk Management | |
>
> The student should bear in mind at all times the fact that this list is constructed on no logical or consistent basis. These functions are not mutually exclusive but overlap one another."[1]

Most of the conventional texts on the subject now concede that elemental and form utility are properly classified under the head of production economics.[2]

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[1] Alexander, Ralph S., Frank M. Surface, Robert F. Elder, Wroe Alderson. "Marketing," P. 89, Ginn & Company, Boston, 1940.

[2] Refer to Duddy, Edward A., and David A. Revzan, "Marketing an Institutional Approach," pp. 4-6, McGraw-Hill Book Company Inc., New York, 1947.

Antithetically many writers came to the conclusion that place, time, and possession utilities are characteristically the results of marketing. The difficulty with this analysis is that it will not stand out in clear relief under the flood lights of logic. Those who subscribe to this classification of functions must do so with reservations because the boundary line between the divisions of subject matter is not definitive. Consequently, marketing as a science has remained in a nascent state, at least, in some areas of indecision. The phrase, "areas of indecision" is used apologetically here because so many of the contemporary writers have uncritically accepted the current broad division of functions. They are by no means in unanimity in the matter of considering the borderline exceptions. Furthermore, they are patently influenced by the vestigial notion held over from the original concept that production and exchange are corollary concepts. Under these circumstances, it would seem worthwhile to re-examine the whole question of market functions to discover a new approach to this provocative problem if such is possible.

Marketing Defined

> *Marketing is the act of creating possession utility. In this theatre of economic activity, men assume the principal role in marshalling the forces of supply and demand at focal points of exchange where the results are expressed in terms of price. Traditionally, human conduct in this sphere assumes certain patterns governed by law, order, and justice in the business of bargaining, contracting, and transferring rights and titles to goods, services, and properties.*

It is the job of the marketeers to find buyers and sellers, to determine when and where and what to exchange, to negotiate the terms of the transaction, and finally to

facilitate deliveries and settlements. Persons who specialize in transactional activities must gather much information concerning the kind, degree, nature, and duration of rights which they may offer in any particular thing in exchange for a similar array of rights in other things. Traders must form judgments about the market values of these rights. Moreover, they should select the most propitious times to consummate a deal which will redound to their advantage. In any formal market organization designed to perpetuate trade, these commercial enterprisers are expected to formulate a standard of procedure and nurture a code of ethics which will enable them to function in a most effective manner in determining market values. Furthermore, they must discharge their responsibilities as principals or as agents in making certain that all the terms of their agreements are fulfilled to the letter in reality as well as in spirit. One of the first writers to perceive the idea that the function of marketing is a legal as well as an economic phenomenon was Henry Dunning McLeod. He maintained that it is not physical commodities, but legal rights which are bought and sold on the markets of the world. The physical handling of commodities is incidental to the transaction.[8] Prior to this trenchant observation the essence of marketing was obscured by the act of passing physical goods from hand to hand at the very moment that legal title was also transferred from the seller to the buyer. Physical materials are so much more obvious than percepts that most people re-act subjectively when they are engaged in economic pursuits. This is especially true for those who work in the genetic and extractive industries as farmers, miners, and fishermen. Likewise,

[8] McLeod, Henry Dunning "The Elements of Economics," Vol. I, Book II, Chapter I, Appleton & Company, New York, 1881.

this fact seems apparent to housewives and children, who are concerned with the ultimate use of consumer goods. To all of these people, the characteristics and attributes of the physical goods are real and useful and necessary to gain a livelihood or to sustain life.

Interestingly, the traders of medieval Europe recognized long before McLeod lived that the essential service which they rendered was that of transferring legal rights to objects of sale. It was this insight into the nature of exchange that caused the fair merchants to begin dealing in contracts and agreements covering deferred payments and future deliveries of goods. They formulated the means to enforce their agreements with one another, and through long experience learned to disassociate the performance of physically handling goods from the function of transferring ownership titles. The development of modern markets has resulted more and more in a cleavage of the acts which create the different utilities.

The divorcement of marketing from the act of receiving physical goods is clearly evident in the transfer of rights to certain things. In the case of immovable properties for example, an owner of a building site may desire to sell his urban possession. He receives an offer from a prospective builder. A sales agreement may be drafted stipulating the price, reservations, date possession will be given, terms of payment, and other details. After the abstract and other documents of title have been examined the buyer and seller meet to execute the agreement. The deed will be ceremoniously delivered by hand from seller to buyer in the presence of witnesses signifying that the terms of the agreement have been fulfilled and the transfer of rights completed creating possession utility.

Functions of Production and Exchange

The basic idea forming this concept of marketing in which the economic processes of distribution are sharply differentiated from those of production can be tabularly rearranged in two major and one minor categories:

Functions	Utilities
I. Production	
A. Exploring and exploiting natural resources, e.g., farming, fishing, and mining	Elemental
B. Transforming materials into goods and machines	
Grading, sorting, sizing, processing and manufacturing	Form
packing and packaging	
assembling, dispersing	Place
storing, aging, curing, freezing	
transporting, shipping	Time
II. *Ancillary Services*[4]	
1. Researching	
2. Advertising	
3. Financing	
4. Risk bearing	
III. Marketing	
A. Buying — Involving change of ownership or transfer of title to rights and privileges	Possession
B. Selling	

[4] These four services are complementary to both production and marketing functions since they contribute to the creation of all utilities. Neither production nor distribution in the broad sense can be conveniently realized without some investigation, publication, capital resources, and risk assumption.

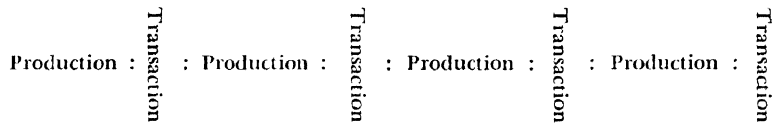
In this classification of functions the act of marketing is conceived to be intermittant phenomena which accentuates the movement of goods and services giving them direction as they flow toward points of ultimate use. From the farms, forests, and mines, and seas men extract raw materials to create elemental utility. Near the point where these substances are wrested from nature someone stands ready to acquire title to the supplies. When ownership changes, possession utility has been accomplished.

The assemblers may render a series of services such as processing, grading, storing, and transporting these materials to some terminal point of distribution thus effecting form, place, and time utilities. Again, a transaction takes place between the assembler and the wholesaler interlinking their services and forming possession utility for the second time.

The wholesaler or manufacturer may process the materials combining them with other ingredients to produce semi-finished materials which may be sold to manufacturers creating possession utility for the third time. From this point on, the operations may become more and more diffused, but portions of the original material will flow into different channels changing its form possibly a number of times before it appears as finished units either as producer capital or as consumer goods. In the meantime, progress in production toward an ultimate use form may be momentarily interrupted a number of times by changes of ownership.

The retailers who perform the final services of distribution are thought of often as exclusive specialists in performing marketing functions. This layman's notion is in error as will become apparent to those who analyze the day to day management of a retail establishment. Retailers perform many tasks which are properly classified as production in preparing their merchandise for

sale. They spend much time wheeling cartons, boxes, and crates about the sales floor opening them, inspecting, sorting, and marking the merchandise for resale. They spend hours during the week setting up window and floor displays, hanging signs, shifting shelf displays, grading and trimming produce to enhance their appearance. The ringing bells of the cash registers interrupt these manifold merchant's chores to denote that sales are being made effecting an actual transfer of ownership in the rights to the merchandise. Retailing under this concept combines two functions — production and marketing — but it is heavily weighted on the side of production by creating place, form, and time utilities preliminary to sales. The successive steps of production and marketing can be depicted in another way. As products flow from points of origin toward their destination of use, the stream is broken by a series of recurring transfers. The brief intervals of transactions, then, constitute centers about which the forces of exchange agglomerate terminating in ownership transfers somewhat as follows:



In this sequence marketing is conceived as a separate and distinct function — a function which provides a basis for independent scientific analysis. This point is of paramount importance to those who aspire to direct, study, teach, or philosophize about the range of human aspirations involved in marketing. Thus the services of production are made distinct from those of exchange.

> *The processes of production are clearly a continuous series, while the acts of those engaged in trade assume the nature of a discrete series.*

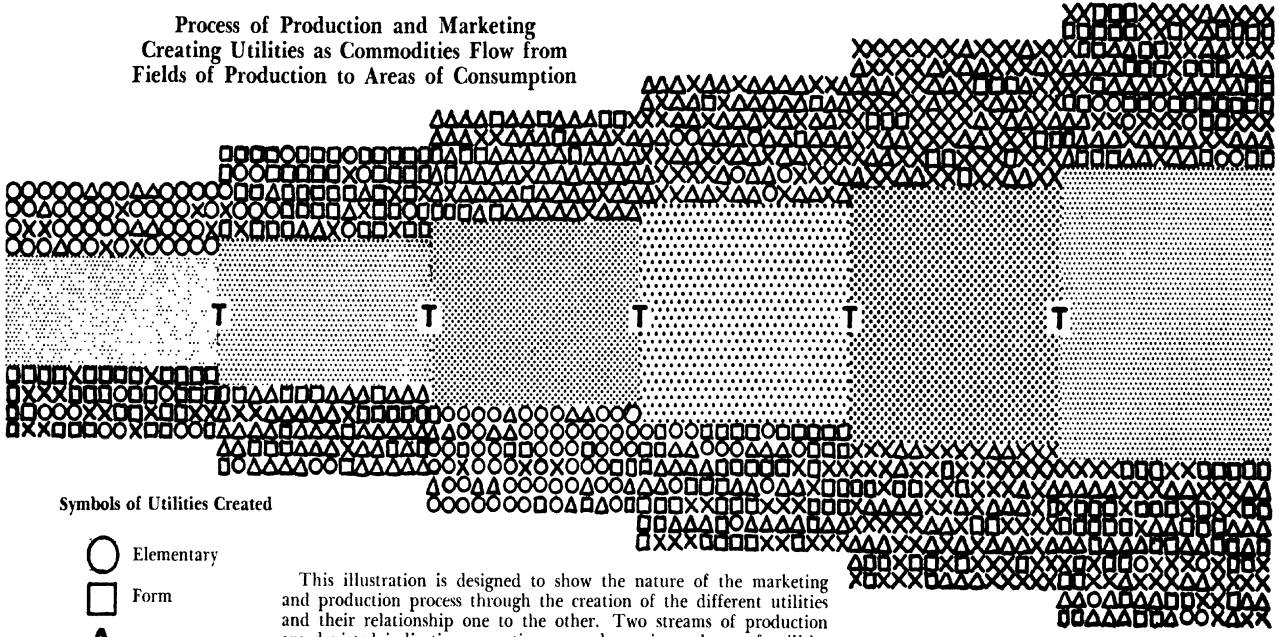


Figure 1

This illustration is designed to show the nature of the marketing and production process through the creation of the different utilities and their relationship one to the other. Two streams of production are depicted indicating a continuous and growing volume of utilities created as time passes. At various junctures along the way ownership changes altering the nature of production and the management of these resources. The creation of possession utility is a discrete function projecting ownership into the future so each interchange in the production is dictated by an anticipated transfer of legal rights or titles to the goods and services.

The principles of production economics on the one hand are broadly applicable to all phases of physical phenomena which measure inputs against outputs. They ascertain the most advantageous combinations of factors, considering variations in productivity, capacity, and efficiency to achieve maximum physical outputs. These factors may be juggled about to determine the turning points of increasing or diminishing productivity, or the level at which constant output is obtained. Essential to this analysis is the function of pricing or valuation which results from transactions. When prices have been determined, the production specialist can calculate the least cost combination, the highest profit arrangement, and the marginal productivities of given quantities. All business organizations and enterprises which undertake the laborious tasks of building up or breaking down either materials or commodities in order to change their form, convey them from point to point, or hold them for future distribution are actually engaged in some phases of production as well as rendering market services. It is the task of their management to distinguish the two major classifications of functions in order to give intelligent direction to the business.[5]

The point that is made here is that negotiational activities involving the mental processes of bargaining between principals to determine prices cannot be made to conform to the principles, doctrines, or laws which are applicable to the physical incidents of production. The abstract principles which govern human conduct when men are in pursuit of economic gain through exchange are still nebulous. When formed, they will represent a merging of the concepts of different social sciences such as psychology, law, economics, sociology, and philosophy. Some

[5] See Black, John D. and Albert G. Black, "Production Economics" Henry Holt & Co., New York, N. Y. 1929.

principles are suggested in this text, perhaps not in perfect form, but they comprise the beginning of what is believed to be a new and stimulating approach to a dynamic field of socio-economic activity.

In the hierarchy of middlemen of this country, it is the brokers, commission agents, and speculators who maintain business offices primarily, if not solely, for the purpose of receiving orders, finding buyers and sellers, negotiating the terms of the transaction, and arranging other details pertaining to the transfers of ownership. They normally do not perform any of the tasks involved in handling the physical goods. These are the agencies which approach in purist form the singular function of marketing.

In a world of scarcity bounded by certain imposed rules and regulations the merchants devote their energies to driving bargains. They adulate, wheedle and charm their prospective clients and customers to win their favor. In the interval of time preceding actual negotiations the principals to a transaction may do some footwork and preliminary sparring to get an impression of the metes and bounds limiting a prospective agreement, and to learn what barriers in the form of opinions and attitudes must be hurdled to attain an objective. These maneuvers for tactical position are achieved with weapons of persuasion and inducements often in the form of advertising. Then negotiations may begin by sounding out the relative intensity of the notions each hold toward the rights being transferred and their respective exchange values. Where prices have not attained a rigid status and where trade has not been conventionalized, the deal may involve a bit of haggling to approach a point of agreement. In this process, the seller will exercise control by virtue of possession of the scarce good exerting all the influence he can command in his right to withhold it from the buyer short of an acceptable offer.

The buyer, conversely, presses any point of advantage he can summon with his purchasing power to incline the deal in his favor. The pitched battles of marketing are fought out in the primary markets where basic prices are determined. In these crucial markets, particularly where wage agreements are struck and wholesale prices established, the principals don whatever economic and legal armor is necessary to win their point, and in some instances they go beyond the delicate grounds of propriety to disconcert their adversaries through deception, dictation, and intimidation.

The ostensible dualism of the intermediate ancillary services listed on page 12 requires a few words of explanation for the sake of consistency in order to sustain the idea that the functions of production and distribution can be sharply differentiated.

Advertising is a business which is sometimes regarded as a service closely related to market distribution. In reality the actual work involved in copy writing, planning the layout, developing the design, going into production, directing the distribution of plates, selecting the media, and maintaining accounts is all more closely related to production than to marketing because it has much to do with the handling and shaping of materials. True the purpose is to promote sales, but a greater part of this activity is applied to spreading inks on paper, running printing presses, pasteing signs on billboards, assembling, and binding folios, and delivering copy to the public. Like retailing the bulk of the tasks fall in the category of production and only a fraction of the time and energy is expended in selling the services of advertising.

The ingredients of research are formed by long hours of assiduous mental labor. This form of skilled labor is generally regarded as the most productive of all forms of human effort and its findings may greatly facilitate both production and distribution. The fact remains, however,

that this service has been utilized mainly in the field of production, but it might be applied equally effectively to problems of exchange.

Financing per se is composed of a series of complementary transactions in the form of conditional agreements which are either closely related or tied to the purchases or sales of rights to the physical goods serving as collateral for the loan. It is a service of marketing in that credits are arranged under specific conditions either explicit or implied involving the transfer of rights to the use of wealth on a temporary basis. As a general rule loans are conjoined with transactions in one way or another to assure repayment when title is passed to another owner.

The assumption of risk may involve a financial gain or loss by transfers of rights to property, credit or reserves in the case of losses, or to profits when the enterprise is successful. This transfer constitutes a transaction for a consideration and is not greatly different in the final analysis from that of financing.

In the first decade of this century, a considerable number of bulletins, brochures, and articles appeared as forerunners of the formal books on the principles of marketing. Reminiscent of the medieval intolerance toward middlemen, one or more sections of the subject matter content in these early publications was usually given over to criticisms of marketing procedures, particularly against the prevalent practices occurring on the commodity exchanges. Some of the attacks by the pamphleteers on middlemen were intemperate in the extreme. Compared with some of the principals in terminal markets, pirates of the high seas were considerate and respectable buccaneers. One author devoted a full chapter to moral preachments in which he classified the men of trade into "straights and crooks."[6] Other folios

[6] Seibels, William T., "Produce Markets and Marketing," Chapter II, Private Publication 1911.

were couched in moderate and philosophical terms stressing the need for reforms and reorganizations to attain particular objectives. This obsession with the evil machinations of merchants considerably influenced the general tenor of and the approach to the subject matter of marketing. It called for reams of description to substantiate and to illustrate the acrimonious charges leveled against wicked men, unethical agencies, and nefarious practices of the time. These same writers were wont to deprecate the middleman system, its costs, margins, profits, services, and influence upon prices. In the post-Sherman anti-trust days, attention was centered on the potential conflict of agriculture and industry and the notable differences in the market techniques adopted by the two divergent economic interests.

The Functional Approach

The first formal books on the subject were influenced to some extent by the biases of the pamphlet literature. The main effort, however, was directed at a physiological analysis of the processes of marketing, more popularly known as the functional approach. It was an approach initiated by Shaw and dramatized by Macklin.[7] This attack on the problem, as pointed out in the first paragraphs of this chapter, has had its distinct limitations. Aside from the difficulty of clearly differentiating the functions of production from those of marketing, the fundamental bases of marketing remained abstruse. Its inclusiveness results in staking out a larger claim to areas for market dominion, than rightly exist, and it overemphasizes particular phases of the subject matter which tends to distort one's view of the whole field in its relationship with other economic activities. It does have the merit of brevity, and of being non-repetitious. It permits

[7] Shaw, A. W., "Some Problems of Market Distribution," Quarterly Journal of Economics, August 1912, pp. 703-765. Macklin, Theodore, "Efficient Marketing for Agriculture," MacMillan Company, 1921.

writers to present a dynamic view of the services of merchandising by describing specific operations.

The Commodity Approach

During the past 40 years a number of books have been published comprised chiefly of a descriptive account of marketing particular commodities. This plan of presentation is known as the commodity approach and the chief products of a country or region are taken up *seriatim*. The sequence in which the selected commodities are arranged in the text is usually considered important because one may proceed from the simple to the complex and topics under one heading may supplement or complement the points to be stressed in a succeeding division. Some writers contend that the characteristics of different commodities determine in a large measure the form of organization and the type of management that will be required for a successful market venture.

Those who presume to cover the "waterfront" will select as broad and diverse list as possible to portray variable situations and conditions for a fuller understanding of the subject. Some commodity specialists may be influenced in their choice of commodities by their natural characteristics, be they animal, mineral, or vegetable. The peculiarities of consumer demand or the special requirements of manufacturers and processors may be a determining factor.

The historical significance of a product might be weighed in the balance to influence choice. It is certain that some commodity might be arbitrarily picked from a grouping if an account of its distribution serves as an analogy for other products. The array of products that is chosen for a treatise on commodity marketing can be subjected to some scientific tests to obviate complete empiricism.

To the academician primarily interested in theoretical considerations, the commodity approach is deadly repetitious and prosaic. The reader is deluged with factual details which may have little or no practical value at a later time. This is especially true in dynamic industries and where technological progress is rapid. A number of colleges have adopted the commodity approach in teaching marketing almost to the exclusion of other methods. The content and frame of reference for their courses may be exemplified by Dr. Breyer's text — "Commodity Marketing." Other schools use this same approach modified in some degree by a brief presentation of functional aspects with comments about the factors of demand and supply in price determination.

This avenue to the subject of marketing is a tempting one for its ease of approach and its seeming practicality. The manner in which the subject matter is usually presented is highly subjective, but this approach does not preclude an objective treatment when given under the guidance of a talented instructor. The chief obstacle to this pedagogical procedure is the transient nature of the subject matter. The factual data grow stale in their transmission through the statistical and descriptive accounts of various government and private publications. Invariably, the textual material is outdated and of historical significance only when it is assigned the students.

If the industries under consideration are dynamic the instructions of the classroom may actually prove to be a handicap to the graduate going out to make his mark. Many firms institute an intensive trainee program, vocational in nature, to acclimate their workers to the job. Under the circumstances, it would seem that our citadels of higher learning could render the greatest service in this field of endeavor by promulgating the relatively imperishable basic concepts, principles, and theories. These elements of marketing would serve as tools for

the technicians for analysis and understanding of facts as they discover them in the practical walks of life.

The early history of marketing for the most part is fragmentary. One finds here and there a bit of interesting information which may be correlated with the basrelief of an ancient coin dug up by some archaeologist. Or possibly a runologist deciphers the characters chiseled deeply in a slab of granite telling about a gruelling viking expedition. A story of an exciting commercial exploit may be translated from hieroglyphics etched in a tomb of a Pharaoh. An ethnologist studies the moods and modes of a primitive people noting their inclinations and taboos affecting exchange. All that remains for the modern chroniclers is to judiciously select the inimitable facts from these scattered sources and piece together a story of the evolution of market institutions. Although we are fortunate in the volume of evidence concerning man's commercial activities which is available from papyrus records and other scattered sources, information on the development of markets is fragmentary and discontinuous. The historian must interpret and correlate events of the past, then relate the absorbing tale that may be useful as a guide to our future activities. In recent years the history of commerce and exchange has appeared in a number of texts, but it is a narrative usually so broad in range of interpretation that each writer must sift and winnow the gleanings for the kernels of truth his special purpose requires.

The Historical Approach

The historical approach is probably not of great value in itself, but it is indispensable to an understanding of the primary elements which comprise the framework of a market institution. If it were not for the fact that history repeats itself substantially in the same manner and form down through the centuries, many of the basic

elements underlying present market operations would be lost to antiquity and modern interpretations would be largely in essence pure speculation. Human progress is uneven in different regions of the world; so that in any given period marketing activities exist in all stages of evolution. This provides an almost perfect laboratory for first-hand observations in tracing the growth of market organizations and institutions. The author's brief interpretation of this development up through the medieval period is presented in Chapters 12, 13, and 14.

The Institutional View and the Functions of Marketing

A market will be defined as an institution in Chapters 2 and 3, and its composition is analagous in some respects to a constellation. The major institution may be composed of a series of minor institutions which together represent a universe in their own right. The rule is that each unit must be a totality, complete unto itself. When it is broken into segments, they are either an equation or a function of the whole. To some readers, this concept in its broadest application may seem inscrutable, because its complexities may extend to infinity.

Those who are specialists in particular fields of study, however, should experience little difficulty on this score. For example, those who are familiar with the details of economic exchange can easily perceive the component parts of a market system which will be described later. In other words an institution is a rounded out concept embracing complex integrated units such as one may find in the labor movement, Mormonism, the banking system, or a national political party. The emphasis is on a going concern which represents change whether it be progressive or regressive. Moreover, it implies an authority which directs and controls human activities within its sphere.

The economics of institutionalism embodies the notion

that it represents a universe of ideas both concrete and abstract which influence the actions of men engaged in economic pursuits. It is a phase of macro-economics applied for basic analysis and for determination of general policy. When the generic idea is narrowed down to the field of marketing, its interpretation is restricted to those legal-economic-social relationships clustered around the various kinds of negotiational transactions involving the use and disposition of corporeal, incorporeal, and intangible properties. These relationships are called rights, duties, privileges, powers, liabilities, and interests, each of which is differentiated by gradations imparting to them certain characteristics in species, rank, and continuity. These differences will be appraised in succeeding paragraphs when the legal view of marketing is considered.

Some writers have uncritically listed the various functional merchants such as brokers, jobbers, retailers, and the like as institutions. This interpretation by contrast is one of micro-economics which characterizes the functional and commodity approaches, and it is open to serious question when applied to the institutional view of marketing. These agencies are in reality subjective functional units which are incomplete and dependent enterprises. They are simple segments of a market institution which perform the function of rendering particular services. An extension of this idea may be illustrated by describing the nature of an agency such as a commodity exchange. The futures market on the Board of Trade at Chicago for example may exist solely by virtue of its environment as an integral part of a total market institution. It is not completely dependent upon the physical facilities it utilizes. The telewires may grow cold and the grain pits may be deserted, and yet the institution transcends these mundane paraphernalia. An institution is the cause, and the various enterprises which were created to perform its missions are the effect.

The Legal Entree to Marketing

The essence of marketing is found in the legal relationships that are created by the agreements to buy, sell, and barter. The means and the authority to effect exchange through contracts were worked out early and eventually consolidated into a system of rules known as the merchants' law as described in Chapter 14 of this text. Subsequently this code was incorporated in the common law when the state usurped the right of dispensing justice relating to commercial affairs. Later the common law was modified by statutes to keep abreast with the changes in a dynamic society. There is more in the legal approach to the subject of marketing than meets the eye, and some of the concepts are basic and essential to the progress of all commercial communities.

It will suffice merely to define some of the common legal terms essential to transactions in the next few paragraphs. Their application is either explicit or implied in the theory of marketing as it is taken up later in Chapter 6.

Elements of Transfer

Property gives one dominion or unrestricted control over objects to do with or dispose of as one wishes. This exclusive right extends to attributes of the things exchanged to possess them or to exclude others from their enjoyment. It is said to be the highest right a man can have over temporal things. The term property in the legal sense may be construed in different ways.[8]

Absolute property is the right to own exclusively chattels and other attributes which cannot under any circumstances be transferred without the rightful owner's full consent.

Real property includes such possessions as lands, houses, and hereditaments. It may be either corporeal or incorporeal.

[8] Brown, Ray Andrews: "Cases and Materials on the Law of Real Property," Chapter I, Callaghan & Co., Chicago 1941.

Private or personal property generally refers to all manner of movables which attach special importance to the personality.

Common or public property usually connotes land or buildings devoted to the use of all the people in a community or of a whole society.

Right is a generic term which has many meanings depending upon the context. In the abstract sense it means justice, or consonance with the rules of the law. In the concrete sense, a right signifies a power inherent in a person.

The fundamental legal conceptions have been classified and arranged by Hohfeld in an effective manner as follows:[9]

Jural opposites	right no-right	privilege duty	power disability	immunity liability
Jural correlatives	right duty	privilege no-right	power liability	immunity disability

These terms denoting jural relationships are particularly germane to commerce wherein so many contracts are made to transfer legal rights and titles from one person to another.

The word *right* as used commonly in marketing denotes according to Black's Law Dictionary, "an interest or title in an object of property; a just and legal claim to hold, use, or enjoy it, or to convey, or donate it, as he may please." The many kinds of rights which have been conceived over the centuries through legal usage vary only slightly in interpretation, but these different shades of meaning are significant in conveying a precise meaning for purposes of law. The various rights limited or unlimited may be listed in apposition as follows:

[9] Hohfeld, Wesley N. "Fundamental Legal Conceptions," p. 36, Yale University Press, 1923.

abstract or concrete
absolute or qualified
primary or secondary
perfect or imperfect
legal or equitable
in personam or in rem

This whole series may be further affected by one's constitutional rights enumerated as: natural, civil, political and personal. All rights are offset by correlative duties. That is, the person against whom a right exists has a duty to act or not act in compliance with the wishes of the one to whom the duty is owed.

A privilege denotes freedom. In this legal relationship one is not under compulsion to perform or not perform certain acts. The correlative of a privilege is an absence of right. There is no right on the part of a second person to force the first person to enter or not enter into a particular course of action.

A power enables a person to generate changes in legal relationships by acting or not acting in any given situation. Under this concept, a person may acquire powers of sale, appointment, disposition or the right to act for another called power of attorney. There are a number of gradations in degree and kind of powers delegated to an individual such as: collateral and appurtenant; general and particular; unqualified and qualified, etc.

Liability — The fountainhead of liabilities flows as a consequence of granted powers. That is, if a person with delegated power chooses to act in altering legal relations, it obligates the second person subject to this power.

Immunity — A sequential concept of law following that of power is immunity. It is the freedom of a person against those having power not to have his legal relationship disturbed through the acts or omission of acts on the part of another.

The correlative of immunity is disability. That is, the person vested with immunity has no ability to alter a given legal situation.

There are five other legal terms which appear essential as nomenclature for a discussion of marketing. They are:

Interest is a sort of a catch all term in law meaning an aggregate or combination of rights, privileges, powers and immunities. This collective ability may apply to properties, things or persons, and it sums up the legal relations arising from various abilities.

Owner is one who possesses one or more interests whether they be corporeal, incorporeal, tangible, or intangible realizations.

Conveyance means the act of creating property interests whether such act is effective or not. Legal effectiveness is not implied in the act.

Devise is a testamentary act by which a deceased person manifested an intent to create an interest in things or properties.

Transfer — when a transfer is effected, it means that one person has extinguished his interest in the thing transferred and created a compensatory interest in it for another person. These transfers may be either voluntary or involuntary. Finally, it is to be noted that legal developments generally trail in the wake of commercial progress. Innovations in business procedure are pressed into action by those who seek profits. There is a need consistent with good public policy to streamline the law relating to business transactions, even now, to facilitate commercial intercourse. Each state in the union is empowered to frame its own laws affecting trade. All enterprisers engaged in interstate commerce may be exposed to eccentric regulations and uncommon interpretations of the law governing business. These legal obstacles which clog the stream of trade are for the most part

needless barriers. They seriously affect the terms of sale, conditions of delivery, collections, negotiable instruments, documents of title, and security transactions. One group of legal authorities is attempting to devise a new commercial code to inspirit the business captains and eliminate frictional legal elements which tend to slow down the tempo of mercantile affairs.

It is the ameliorative work of the National Conference of Commissioners on uniform state laws that is alluded to here.

Another phase of government influence which has come in for a good share of indignant criticism from businessmen imbued with ambitions is the myriad forms of regulation, control, and intervention. Much research might be initiated embracing a complete review of administrative orders, rules, instructions, and other delegated discretionary powers and acts which appear to affect commercial operations detrimentally.

From Retrospect to Prospect

It is concluded from the foregoing discourse that the functional approach has been too broadly interpreted hitherto for purposes of differentiation. If the scope of the functions is limited and reclassified as shown in the tabular arrangement on page 12, this view of marketing may become a useful analytical device in that it permits a sharp distinction between production and marketing services.

The commodity approach has its distinct limitations both for theoretical considerations and as a pedagogical method. It is repetitious and mainly descriptive in nature. When used generally to the exclusion of other plans of presentation, too much emphasis is given to facts which are, at best, ephemeral.

The institutional view sometimes incorrectly interpreted and generally treated in a narrow sense bordering on the functional concept is in reality basic in proportions. As it will be outlined in the second and third

chapters of this text, the institution is a generic concept applied to the whole framework of socio-economic and legal relationships involved in a system of transactional economics. The institutional view provides first of all the necessary background for a legal analysis of marketing. Second, it embodies a number of abstract ideas which exert an inestimable influence upon the course of action and the fortunes of every going economic concern. It is, in one sense, not only the physical features of market organization, it is also the spirit of the related units of enterprise and their invisible powers of coherence. This notion of the function of marketing will be more fully developed in Chapters 5-7. The institution transcends the bare physical features which are readily apparent. It is the cause which gives rise to the formation of business concerns and they in turn spawn the effects.

History is but the prologue of the future. Its main events serve as points of reference to orientate the scholar's efforts along lines of useful research. These landmarks are the various types or forms of market organizations now extant in the world. A close study of these survival forms in their various stages of development gives one a cross sectional view of the total evolution of market institutions ranging from primitive barter to modern futures exchanges.

A neglected phase of the functions of marketing is the development of legal concepts. It involves, first of all, the addition of many new and singular terms unfamiliar to the ear of the laymen merchants as well as the economists. More difficult is the notion that the act of buying and selling is centered in an exchange of rights to the product rather than any concern with the physical features of the product itself. Finally, the innovators of commerce have through time forced their hand against the weight of precedence and tradition concerning negotiations and ultimate transactions. As

the tempo of an industrial society is accelerated, it becomes necessary to give increasing attention to the revision and streamlining of laws consistent with sound business practices affecting all exchange relationships.

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THE MARKET INSTITUTION

2

What is a Market?

IS this query germane? What useful purpose is served in defining a market? Nearly every living soul who has reached the age of reason has of necessity entered the market and become one of the actors in the business of negotiating an exchange. In fact, the market seems so commonplace, to most people it is taken for granted. To some students of marketing and economics in general, this question presents a challenge. If they turn to the standard texts in marketing and economic theory in their search, they will be amazed first of all by the apparent inattention given this question, and second, to the confused and diverse answers they find given by those authors who attempt to define the market.

The market has been defined as a sphere within which the price making forces operate, but it is not made clear what is meant by the word "sphere." Neither has the phrase "price making forces" been made explicit. An old proverb often quoted, "Two women and a goose make a market" answers the question with an absurdity.[1] Some claim a market is a place or area, others think of it as a particular commodity e.g. the cotton market. Then, there are those who visualize it as an element of time or as a group of persons. A current theoretical economic concept describes a market as a group of buyers and sellers of a commodity who are in close

[1] Hibbard, Benjamin H., "Marketing Agricultural Products." P. 13, D. Appleton Co., New York, 1921.

communication with one another acting to equate the forces of supply and demand.

The National Marketing Association in a review of definitions pertaining to market functions cautions its readers to stick to terms of common usage in the trade rather than follow the cue of the economic theorists. The question, "What is a market," is fundamental because one cannot very well discuss the whole subject of marketing without delineating some of its major characteristics. To this end the next two chapters will be devoted mainly to formulating definitive concepts of a market per se.

> In the judgment of the author, *a market is an institution designed to facilitate the transfer of legal rights and titles to ownership in goods, services, and properties.*

A lexical study of the generic term "institution" will give the reader a comprehensive idea of the breadth and profundity of this verbal symbol. Some encyclopedic sources define institution as a cluster of habits or social usages. It is a combination of customs, conventions, laws, forms, rules, regulations, restrictions, and practices operating generally in conformity to some ideal pattern or mode of activity. Any one who has had some experience in the business of buying and selling things may be vaguely conscious of the institutional atmosphere that surrounds every transaction. His actions and intentions are encompassed within certain metes and bounds whether they be imaginary or real. In some instances these boundaries of limitations and restraint are quite distant permitting the individual much latitude in his wealth accumulating pursuits. On other occasions, the individual may feel that he is imprisoned in a deep chasm behind towering walls of inhibition that seem too narrow and foreboding to admit any avenues of escape for personal initiative.

The Pattern of Imprescriptible Rights in a Free Market

The particular network of basic factors comprised of rights, powers, duties, and opportunities that are synthesized within the skeletal framework of the institution known as a market are:

1. Emancipation of man and individual freedom in economic activity.
2. Recognition of private property ownership.
3. Guarantee of rights of assembly and association for purposes of trade.
4. Protection and regulation of an accepted medium of exchange to facilitate trade.
5. Freedom of contract in commercial transactions.
6. Power to create and extinguish debts.
7. Opportunity to protect one's rights and proprietary interests by recourse to law and justice maintained by orderly government.

Let it not be assumed that this series forms a conclusive list. Probably it is only a beginning enumeration, but these directive factors may educe other points as scholars continue to probe into the mysteries of social organisms.

In running the gauntlet of human relationships, Laski suggests that men began from a point of recognized *status* in society advancing toward *contract* and from there they proceeded to *relationship*.[2] In other words, the varied points of contact men now make in their daily rounds in a complex society are so numerous that it is impractical to emphasize their formalization in legal terms exclusively. We simply proceed in a rational manner reflecting on the consequences of our acts and behaving with consideration for other people's interest as well as our own. This, in short, is institutionalized conduct.

[2] Laski, Harold J., "Liberty," Encyclopedia of the Social Sciences, Volume 9, Page 445, MacMillan, New York, 1933.

1. Emancipation of Man and Individual Freedom in Economic Activities

The realization of individual liberty and economic freedom has ever been an elusive objective of man. Slavery in one form or another has always been a spectre haunting societies either savage or civilized from time immemorial. A League of Nations Committee concerned itself repeatedly about the extent and evil effects of slavery prior to World War II. Before 1940, it was estimated, on incomplete information, that slavery still persisted for several million persons. It was most prevalent in some parts of Asia and Africa. In Ethiopia, about one-fifth of the total population is still considered to be in a slave status. There is also a considerable number of serfs in this African commonwealth.

A British delegate informed the United Nations Social Committee recently that Russia was chaining millions of workers to a "monstrous slave system which has no parallel in world history." Irrefutable evidence from many sources has been collected to prove that masses of humanity are incarcerated behind barbwire barricades in forced labor camps to work and live under intolerable conditions in occupied zones as well as within the boundaries of the Soviet Union.

The implications of slavery in any form are of crucial interest to market theorists. Slavery received its initial impetus as a consequence of the division of labor. Among primitive tribes it was extensively known, but probably never intensively exploited. Captives were adopted as members of families to fill the place of departed ones lost in battle. When pastoral peoples made war upon one another for booty, the herdsmen of the defeated were a concomitant part of the prize as a means of supplying the additional labor required to care for the increase in livestock numbers. The Sumerians began commercial-

izing slavery as early as 3000 B. C. From that time to the present, human beings have been an object of exchange, and the detailed accounts of the infamous slave auctions are some of the blackest pages in the history of Commerce because of their enervating effect on the body politic.

Trade and Thralldom

Bondage and business enterprise are incompatible. This apothegm stands despite the impression one may gain from glowing accounts in some historical references on commerce in ancient and early medieval periods. The many limitations of commerce are obvious when one considers the nature of the trade prevailing in these early times. The principal items of exchange were comprised of three kinds of chattels:

weapons
slaves
luxuries

These strange categories of articles in commerce were not in themselves conducive to great expansion in trade. On the contrary, trade in these chattels evoked acts of attrition which decreased the total volume of exchange. The aggressive businessmen of that age realized the greatest profits in the production and distribution of scalping knives, daggers, and wonderful two-handed swords finely drawn to a keen edge. These implements of war were effectively used for hewing a path to the very borders of the barbarian frontiersmen and they were duly impressed with the efficiencies of an advanced technology.

It would have been most difficult for the traders of this early period under any circumstances to distribute weapons of warfare impartially among their barbaric customers. The disproportionate distribution, whether intentional or otherwise, created demand for defensive

weapons, and there is reason to believe that the swarthy tycoons from the east supplied this newly created demand with avidity. What is more, these shrewd and indomitable traders of the pre-Christian era pressed inland, ever expanding the area of their influence beyond the Pomeranian moors and the plains of Champagne. "Every few centuries they brought out a new and improved line of goods. They produced excellent axes; in one deposit in Brittany, four thousand standardized hatchets, neatly bundled with wire, have been recovered. Presently, during the period 1800-1200 B.C., the primitive bayonet was introduced, a dagger on a handle. Then, as the yet newer metal, iron, was being worked successfully around 1000 B.C., the inventive genius of the Mesopotamian industrial districts achieved a most formidable weapon, broad and long of blade, true-cleaving and trusty, well fitted to a hero's hand — the sword."[3] The obvious use for these weapons was that of carrying on more successfully warfare against neighboring peoples. The inducement for robbery and pillage of neighboring tribes was to weaken them as competitors by carrying off their able-bodied warriors and young women to be sold as slaves in exchange for more and better weapons. Another turn in this vicious trade spiral brings out the fact that no inconsiderable number of these primitive people, particularly women and children, were shuttled into the channels of slave trade by patriarchal consent in exchange for exotic silks, spices, and sweets. The estimated percentage of the total population comprising the status of bondage for different regions and for different periods of time is from 10 to 40 per cent. The ratio of slaves employed in the building of the Temple of Erectheus at Athens in the 5th century B.C. was 22.5%.[4]

[3] Beard, Miriam, "A History of the Business Man," Page 13, MacMillan Co., New York, 1938.
[4] Encyclopedia of Social Sciences, Volume 14, Page 76.

Malevolence Toward Merchants

The disconcerting part about this primitive traffic was the widespread piracy and violence that followed in its wake always endangering the basis of trade. The very implements of war distributed by tradesmen were turned against them by lusty swordsmen. Continual warfare existed between those who sought to carry on trade and those who opposed the nefarious activities of the traders. Warriors' weapons became a boomerang which swiftly glided back on the very heads of those who distributed them. Traders were legitimate prey and it became necessary to travel under armed escort and even then to pay tribute to the robber barons at the enumerable boundaries of the petty kingdoms.

Slaves were in many periods the chief item of commerce before medievalism. The distribution of weapons and luxuries only serve to complement and intensify conditions of bondage. In conclusion then it can be affirmed that there was no sound basis for either the intensive or extensive development of commerce because peace, protection, and industry were imperfect. There is no more effective way of limiting a market than reducing the number of potential suppliers and demanders that may participate in such a market. As long as slavery was tolerated, it served as an effective deterrent to the extension of trade. Freedom of action is a requisite of individual ingenuity and initiative in the arrangement of the factors of production and in the association of men to secure the advantages of specialization.

Status Is Essential to Liberty

Ideas concerning liberty have been slow in dawning upon the conscience of man. The first notion of liberty formulated in a world of tribal warfare under the law of tooth and claw was one of defense in order to survive.

Inclusion with these gregarious, nomadic fighting groups meant comparative security to the individual. There could be no general disintegration of these units until some form of peaceful government could be established wherein each individual might safely follow an independent course of action. Tribesmen still held tenaciously to the custom of affiliating in groups as an assurance against dangers of invasion and as a means of securing recognition of a *status,* a position of eminence as a group among groups. The crudest means of attaining liberty — liberty to its own votaries — is by physical force, and humanity has been intermittently locked in deadly combat either to achieve liberties, rights, and privileges for themselves or to deprive others of these rights and liberties.

Eventually man evolved greater security for himself by making laws either ecclesiastical or civil governing his conduct in society. The right to use force was theoretically surrendered to the state which organized a militia and engaged police to maintain order. In this transformation of living, the individual abandons a position of dependence and relies on his citizenship rights of a nation. At this juncture he passes from *status* to *contract* in his obligations to society. The pantheistic philosophy of the stoics was a potent influence in emphasizing the primacy of man. It taught men to cultivate freedom in thought and action and to regard all persons as equals in the "mother cosmos and the father void." Stoicism has exerted a socializing influence upon western civilization ever since the time of Hellenic Greece by its creedal doctrines: the natural rights of man, *jus naturale* in Roman Law; Liberty, equality, and fraternity, the battle cry of the French revolutionists; the inward peace, calm, and self-reliance of freemen in the democracies.

The Ladder to Freedom

The ladder of emancipation from medieval slavery had several rungs, each elevating the status of the subservient from one stratum in society to the next until he reached the high, firm ground of freedom. Feudalism as a system of organized society was so heterogeneous in character for different periods of time in the various kingdoms where it thrived that it is not safe to generalize about it except in the broadest terms and then only as it applied to a particular country. In England the climb from slavery to freedom can be roughly divided into four steps:

1. Slavery — A slave is a form of absolute property transferable at the will of the owner.
2. Serfdom — A serf or villain is one who is attached to the soil and cannot be separated from the manor except by manumission. (A) The villain lived under the authority of his manorial lord and master (bailiff) deeply rooted in the soil which he could not leave without consent of the master. (B) He was obligated to render praedial services as his lord willed and commanded. (C) If the serf acquired any goods by chance, chase, or dint of industry, it could be immediately seized by the lord without compensation.
3. Peasantry — A freehold tenant permitted to reside on the manorial estate by forbearance of the lord and under authority of the manorial courts. As long as feudalism prevailed these so-called freemen tenants were obligated to pay rents, fines, and fees to the manorial lord as well as to render some praedial services quite

similar to those performed by the serfs, although in some instances these labor tasks were somewhat lighter and less odious.

4. Freemen — A person free of all bonds to a landlord or master owing fealty only to his king and his country. This freedom was most often secured through manumission, purchase, or escape.

The bubonic plague — Black Death — scourged Asia and Europe during the 14th century, decimating the population in great areas. This catastrophic affliction contributed more than any other single factor toward the eventual disintegration of feudalism. The heavy hand of tradition, released the serfs in the widespread demand for labor. There was more material wealth to go around among the survivors, money circulated more freely and ideas of civil rights gained currency as an aversion to the stern discipline of the self-sufficing feudal manor. Liberty was to be administered in limited doses to the benighted serfs, however, until they learned to cultivate the delicate flower of possession just as they learned to cultivate the lord's fields.

From the thirteenth to the seventeenth centuries, there was spiritual and religious turmoil which turned on the fine points of an individuals' rights in relationship to society and to the supreme intellect. Throughout the fourteenth to the seventeenth centuries much ground was won and much was lost in the struggle for liberty. During the renaissance, the outlook was rather dismal. The individual at times seemed completely submerged by the chaos and the confusion of that period. Then followed the triumphant eighteenth and nineteenth centuries when again the rights of individuals emerged and were proclaimed to the world in historic political documents by many states. The twentieth century has been

one of industrial and international strife in which men and nations have been caught in the vortex of commercial rivalry. Now, we have emerged from a great global war. In this conflict millions of individuals were forced to surrender many rights to the state for the sake of centralization of authority and effective planning to assure a successful conclusion in this struggle for the defense of ourselves from domination by foreign powers. We, in effect, surrender certain liberties to ourselves to maintain freedom from alien autocrats.

2. Property Ownership Rights

Speculation upon the subject of property ownership origins has been rife ever since the inception of the social studies. These origins are prehistoric, therefore, their character and scope have been quite obscure. The discovery of a few simple ethnic facts has provoked a number of theories on property ownership by writers who seem to believe implicity in their ability to penetrate the heavy veil of time by the sheer powers of their logic. Economists have concerned themselves with a specialized phase of the problem in their relentless search for truth about value. Refinements in the concepts of economic value are dependent to some extent upon our understanding the probable origins of property rights.

A natural part of every American's intellectual heritage is the vivid impressions of the tribal life and exploits of the red savages we found living in virgin forests and on vast plains of the American continents so recently discovered by our intrepid explorers. Here, the wealth seeking white men found a new world seemingly of unbounded space, sparsely populated by aboriginal tribes — a whole hemisphere of fabulous natural resources. The attitude of the Indian and the reaction of the Caucasian to these undeveloped riches provides some recent clues to the origin of property ownership

rights which may supplement the theories postulated upon prehistoric Indo-European settlements.

A case in point is the actions of the viking Norsemen in their discovery of new lands in the middle ages. In the occupation of Iceland and Greenland the Norwegians revealed an insatiable hunger for spatial possession totally unlike those of the "skraelings" — (Eskimos and Indians).

"The land a man wished to acquire was passed over with fire! Bonfires must have blazed over South Greenland in 985 and the years that followed. After having their bearings the landnamsmen (settlers) have at first travelled around about and like Helgi the Lean in Iceland lit a fire at the mouth of every river within the area they took in possession, or they followed the custom adopted in the later landnam period in Iceland in order to restrict the expanse of the landnams' claims. A man had to light a fire when the sun was in the east and it was to burn till nightfall. Thereafter he had to walk till the sun was in the west, and then make another fire. No man, it was laid down, could take a larger landnam (claim) than he could pass over with the fire in the course of one day together with his shipmates."[5]

Genesis of Communal Property — Whenever a relatively small number of Homosapiens wander into an expansive, unclaimed territory where nature is bountiful, they enter a province of free goods. To take possession of these goods, however, involves some effort in picking, gathering, and chasing in order to overcome whatever resistance nature provides against appropriation. By this intrusion, man simultaneously performs three distinguishable acts which later assumed legal significance:

1. Occupancy — or right of inclusive enjoyment. At first this right was regarded as a temporary con-

[5] Norlund, Poul — "Viking Settlers in Greenland, and their decendants during five hundred years" pp. 21-22 (Translation) Cambridge University Press, London 1936.

venience for the group, but as civilization advanced it became both exclusive and perpetual for the individual.

2. Appropriation of things *res nullius* — or objects never previously owned by anyone. Appropriation arises as a natural consequence of occupation to supply the needs and comforts of the intruders.
3. Labor — or effort expended in garnering and wresting things from nature. This principle was proclaimed in the institutions of Manu five centuries before Christ.

   "The sages declare a field to belong to him who first cleared away the timber and the deer to him who first wounded it."[6]

Wherever primitive peoples abound they have always displayed a propensity toward ecological grouping. Tribal organizations satisfy at least two basic requirements; an inward craving to be social, and mutual protection from the ravages of nature. As the population increased, however, it became more difficult to eke out an existence by nomadic pursuits. Natural boundaries between tribes began to take form and eventually occupancy was limited to an area held inviolate by other tribal groups except in times of war. In all tribal forms of social organization, property is held in common and trade is effectively inhibited by formalities. The obstacles to intertribal exchange of communal properties are admirably described by Maine.

"The undivided state of property in ancient societies is consistent with a peculiar sharpness of division, which shows itself as soon as any single share is completely separated from the patrimony of the group. This phenomenon springs, doubtless, from the circumstance that the property is supposed to become the domain of a new

[6] Baden-Powell, "Land-Systems of British India," Volume I, Page 227, Clarendon Press, London, 1892.

group, so that any dealing with it, in its divided state, is a transaction between two highly complex bodies . . . . As the contracts and conveyances known to ancient law are contracts and conveyances to which not single individuals, but organized companies of men, are parties, they are in the highest degree ceremonious; they require a variety of symbolical acts and words intended to impress the business on the memory of all who take part in it; and they demand the presence of an inordinate number of witnesses. From these peculiarities, and others allied to them, springs the universally unmalleable character of the ancient forms of property. Sometimes the patrimony of the family is absolutely inalienable, as was the case with the Sclavonians, and still oftener, though alienations may not be entirely illegitimate, they are virtually impracticable, as among most of the Germanic tribes, from the necessity of having the consent of a large number of persons to the transfer. Where these impediments do not exist, or can be surmounted, the act of conveyance itself is generally burdened with a perfect load of ceremony, in which not one iota can be safely neglected. Ancient law uniformly refused to dispense with a single syllable, however, its meaning may have been forgotten; with a single witness, however superfluous may be his testimony. The entire solemnities must be scrupulously completed by persons legally entitled to take part in it, or else the conveyance is null, and the seller is re-established in the rights of which he had vainly attempted to divest himself."[7]

Natural and Personal Objects of Ownership

The divergent theories on property ownership naturally fall into two classifications; the most numerous are those founded on the premise that property origin-

[7] Maine, Henry Sumner, "Ancient Law," Pages 262-264, Henry Holt & Company, New York, 1888.

ated in personality or moveable things, the others maintain that ownership rights were first clearly recognized in land or other immoveable objects. Again the difficulties of generalizing life habits on a world-wide basis are made apparent. We know that all habitable parts of the globe have been occupied by successive generations of man since times immemorial. These heterogeneous peoples of different racial characteristics, temperaments, customs, and mores, there are reasons to believe, originally sanctioned ownership rights simultaneously both in moveables and immoveables in widely separated places. Our preconceptions of property origins, however, are derived from deductive reasoning primarily. Scholars in the various branches of the social studies interpret property rights differently again by the emphasis they give to specialized phases of human activities. The historians, anthropologists, and sociologists may present one view while the economists and legalists perceive these rights in another light.

Acts of acquisition or evidence of possession should not be regarded as conclusive proof of vested property rights. Some writers have assumed that property ownership originated in moveables first because primitives were nomadic, and, therefore, they only attached value to those things which could be seized and carried away. Those who present this argument beg the question on two counts. First, all things moveable and immoveable are *res nullius* until appropriated, and second, possessory rights in a communal society are quite ephemeral. The subjective attitude of primitive people toward property is attributed to intimate personal experiences or to some imputed psychic powers infused in the thing by a particular individual. Some of the usual moveable objects of attachment are: articles of adornment, slaves, weapons, and wives. These rights, however, are so inextricably enmeshed with the proprietary rights of the tribe that

the duties and powers of the individual respecting their disposition cannot be clearly distinguished from those of the familial group.

It is a well known fact that communal societies proverbially exist on a relatively low plane of living because the material benefits of personal exploits are lost in a system of distribution which favors the welfare of the group as against the interests of any particular individual. The first step in the liberation of ownership rights was taken by individuals within these communal societies when they sought ways and means of improving their lot. Impelled by want, they forsook the insular, subjective sharing of material things under the compulsion of tribal ceremonies. Instead of communistic rationing, they gradually adopted an objective point of view toward all economic goods, thus letting down the bars to extensive trade among men which eventually broadened the concepts of private ownership rights.

In this transition of the individual from a natural society to a civil state, he passes from a position of status to contract. This contract is one of mutual respect for the personal relationships and the property rights of each citizen within the newly formed civil communities.

Private Property Origins — It was in times of great dearth that the asocial individualists probably broke off from their native clans or tribes to fend for themselves. They may have settled on some choice meadow or woodland area for more intensive exploitation of the land within a limited radius from their dwelling places. Obligations to their paternal groups for the use of these areas of land may have originated "a form of tenure intermediate between an absolutely free use of the soil, and property, giving to the cultivator the right to retain a field until he has collected from it the fruits of his labor."[8]

[8] Lewinski, Jan St., "The Origin of Property," Page 14, Constable & Co. Ltd., London, 1913.

The transitions from temporary possession to absolute possession were evolved over a long period of time and in most regions property rights were transient as long as its inhabitants remained semi-nomadic.[9]

A natural sequence in the affairs of men which occurs all too often is that, soon after the act of appropriation from nature, conflicts arise between envious rival groups. Domains are invaded and occupied by force displacing the original settlers. The victors then proceed to establish law and order to legitimize their possession. Markets are inevitably re-established for the purpose of exchanging the spoils of war for the harvest products of labor wrought by the hands of the vanquished. In this way, quiritarian rights prevail over bonitarian ownership.[10]

The most outstanding example we have of this procedure in history was the grand paternalistic experiment of feudalism in the latter middle ages. Feudalism formulated a tenure system limiting property rights to the sovereign and permitting the use of these properties to a hierarchy of classes ranging from the most favored lord down to the lowliest serf, all for a consideration.[11]

Property Personified by the Philosophers

As an anticlimax to an age of great discoveries in exploration, science and religious experience, John Locke presented his theory of the origin of property late in the 17th century, a theory that was destined to sound the death knell for monarchial despotism and provide a basis for the rise of democracies.[12] His brilliant logic seemed irrefutable, then, because property as he visualized it

[9] Ibid pp. 11-20.

[10] Veblen, Thorstein, American Journal of Sociology, Vol 4, No. 3, pp. 352-365, Nov. 1898, Also Vol. 4, pp. 503-514, January, 1899.

[11] Rent could be paid either in the coins of the realm or by services, e.g.: military, personal, frankalmoin or socage.

[12] Locke, John, "Philosophy of Civil Government" — Two Treatises; book I, Chapters I and II, and Book II, Chapters I - V., J. M. Dent & Sons Ltd., London.

was cloaked in sacrosanct robes emerging directly out of nature for the salvation of the common man who had just thrown off some of the last vestments of feudalism. It was a time when Englishmen everywhere chaffed under the intolerable rule of the Stuarts. The doctrines of Locke's philosophy became popular with the masses because they sought freedom interpreted in its broadest sense as well as individual liberty in both economic and political pursuits.

In defense of individual liberty, Locke insisted that everyone has an exclusive right over his own person. The admission of this point provided the basis for private property in the products one creates in his mind, or appropriates and shapes with his own hands because if a person's property in himself is absolute then he may also claim exclusive right to the fruits of his faculties within certain reasonable limits. One should not take more land than he can cultivate himself nor should he appropriate objects of nature beyond his own needs. If these bounds of moderation are exceeded, others may be deprived of that which belongs to them even in a realm of "divine abundance." Locke established by this line of reasoning a definite relationship between personality and property. A relationship which formed a vital part of socialistic theory and classical economic polemics. This pragmatic idea ascended to a high creedal status expressed in the constitutional proclamations of free states. It was at that time considered the essence of the capitalistic order.[18]

Locke's private property, then, was material wealth produced by a just man through dint of labor under the

[18] Weber, Max, "The Protestant Ethic and The Spirit of Capitalism." Talcott Parsons, foreword by R. H. Tawney, George Allen & Unwin Ltd., London, 1930. Also see refutation by: Robertson, H. M., "The Rise of Economic Individualism," Cambridge Studies in Economic History, Cambridge University Press, England, 1933.

surveillance of God. The reason men were compelled to labor at all arose not from scarcity but from the original sin. In this view one finds no justification for the great mass of property arising from the appropriation of scarce natural resources. Nor does it explain acquisitions subsequently realized through transactional negotiations which formed the great fortunes of Europe and America much admired and respected as a characteristic feature of the capitalistic system.

Evolving Property by Legal Gradations

Property came into existence only after its legal foundations were established by law. The origin of private property according to Roman jurists was founded upon the legal principles of occupation, adverse possession, and prescription.[14]

1. Occupation *ipso facto* is a prerequisite for possession.
2. Adverse possession presumes opposition requiring prowess in conquest as well as brawn and ingenuity for turning away interlopers and antagonists.
3. Prescription is modified in degree by labor — time expended on improvements such as assarting, draining, leveling, and fertilizing. Usually if one holds uninterrupted possession of land for a long period of time, prescription is fulfilled and the possessor holds indefeasible rights.

The close relationship thus evolved between liberty and property rights was succinctly expressed by Montesquieu:

"As men have given up their natural independence to live under political law, they have given up the natural

[14] Maine, op. cit. p. 27.

community of goods to live under civil law. By the first, they acquired liberty; by the second, property."[15]

Property in Land — Since ownership of things within the closed groups of primitive societies was never decisive for the individual, one may proceed on the hypothesis that legal private ownership of property, in some parts of the world at least, originated most clearly in land. The presumptions in favor of this thesis are:

Subsistence by direct appropriation on the part of primitive nomads became precarious in times of scarcity and unsatisfactory as a means of providing for the needs of an increasing population.

Isolation for the individual before the establishment of civil government was tantamount to death, but relative isolation in a civil state was the only positive means by which individual initiative could be rewarded — (occupancy).

Occupation was in most instances achieved through selection. Superiority over other claimants was establishable through — (adverse possession).

Exclusive rights to location were crystalized by duration of residence — (prescription).

Ownership was ripened by labor incorporated in the soil.

Land was the most abundant factor; as a capital good combined with labor, it provided the most available means for creating new wealth in the form of derivitive economic goods. (Locke's Labor Theory).

The transfer of alloidal properties, such as land, slaves, and other permanent fixtures thereto was rigidly consummated under the meticulous Roman law principle of *res mancipi.*

"But the higher class of property in the ancient world

[15] Nugent, Thomas, "The Spirit of Law," by M. De Second at Baron De Montesquieu, Volume II, Cincinnati, Robert Clarke & Company, 1873. Chapter 15, Vol. II, p. 173, Book XXVI).

comprised not only land but several of the commonest and several of the most valuable moveables. When once the wheels of society had begun to move quickly, there must have been immense inconveniences in demanding a highly intricate form of transfer for a horse or an ox or for the most costly chattel of the old world — the slave."[16]

Ownership Transfers Liberalized — Before the time of Justinian a distinction was already being drawn between classes or kinds of goods. Common products of soil and industry were gradually released from stiff formalism in trade under the principle *res nec mancipi.* In the Justinian Code the distinction between *res mancipi* and *res nec mancipi* was finally abandoned and simpler methods of transfer and recovery were evolved. Actual delivery or evidence of delivery from hand to hand became the principal means of conveyance. This forward step in procedure, even though it did not convey perfect titles, did much to facilitate market transactions, but it did not preclude other classifications and distinctions like that between real estate and chattels.

The Welfare Theory of Property

After tracing the origin of private property, Ely concludes that "the general welfare theory" of property is the only correct and tenable theory. He places social utility above private interest in property rights. This trend, he maintains, is irresistible as a final stage in social evolution.

"Free goods make way for property. Public property is transformed into private property, and private property again into public property, and extensive forms of property make way for intensive forms, because all this evolu-

[16] Maine, *op. cit.* p. 268.

tion promotes the general welfare."[17] The general welfare theory, predicated upon diverse social means of expropriation is an effective answer to the critics of private property, who insist that scarce resources, particularly land, will be engrossed by a limited number of "sooners" and squatters. Absolutism in dominion over property by individuals is restricted primarily to intercourse between individuals. Where the public interest is involved, the rights of the modern state are universally considered superior to those of individual citizens.[18]

Incorporeal Property — The right to own or control property in any form emerges from societal consent. Historically, this consent, affecting the conduct of men in all human relationships, was by long continuance first crystallized into custom and then graduated into unwritten laws. In the era of centralized governments, laws were promulgated as the most efficient means of governing the conduct of individuals in their daily rounds of economic and social activity.

Under early common law, titles to chattels could only be transferred by actual delivery of physical objects. A promise of one person to another was a personalized relationship not to be transferred to others except to heirs at time of death. They were not considered assets in the general sense nor were they negotiable. Exceptions to this rule were eventually admitted in the use of the deed and still later in the formation of sales contracts. These two instruments were the first bridges devised for industrial societies to span the deep chasm between subjective exchange of corporeal properties on the one hand and the objective transactions of incor-

[17] Ely, Richard T., "Property and Contract in Their Relations to the Distribution of Wealth," Vol. II, pp. 545-546. MacMillan Co. 1914.
[18] Ibid. Vol. I. Chapter VI.

poreal properties on the other. Moreover, the improvisation of the deed and the contract permitted traders to oscillate freely from possession of tangibles to the ownership of intangibles. The terms, incorporeal and intangible are closely related, but they are distinguishable. They are the figments which are created by contemplation. Their incorporeous beings are bodiless, vague, inpalpable attributes providing the means to a vast area of trade in which credits and debits are the elusive forces of motivation. These substanceless qualities sought after in exchange are simply the possession or command over all kinds of rights and interests having value which can be magically transformed by exchange into tangible objects. A case in point are the inpalpable air-rights extending upward over railway terminals or over right of ways.[19] This appearing and disappearing phenomena from a real to an unreal status constantly recurring in the counting rooms and the halls of trade serves to create confidence in the mystic reality of incorporeality. The common species of these incorporeal concepts are: debts, patents, goodwill, copyrights, options, leases, annuities, easements, and shares.[20] There are individualized exceptions to this list which have not been endowed with the mantle of transferability even though they are not without their economic implications such as: licenses, franchises, and injunctions. Society has for the most part reserved these means as instruments for disciplinary sanctions.

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[19] For a discussion of these property rights read: Pence, William D., "Railway Terminal air-rights developments and the movement of local land values," pp. 150-168, Journal of Land and Public Utility Economics. Vol. 5, 1929.

[20] The distinction between incorporeal and intangible properties is elucidated in Chapter VII.

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THE MARKET INSTITUTION (Continued)

THE series of relationships formed in the development of a market institution may for analytical purposes be conceived as emerging from the natural and civil rights of man. Equality and freedom in economic affairs considered in Chapter 1 are natural and basic to the complex relationship which is formed by self-imposed rules and regulations governing the conduct of individuals who participate in market operations. We now turn to a consideration of the factors which are composed by consent through legislation, agreement, and mediation to round out and make more effective the means of consummating transactions.

3. Rights of Assembly and Association

All forms of commercial intercourse are reposed in the rights of assembly, communication, and association. Without these rights, which are relative rather than absolute, there can be no legitimate free trade. The inclination toward mutual exchange is so general that any serious abridgment of these fundamental rights is likely to drive commerce into underground channels. The furtive, illegal transactions consummated in defiance of excessive government regulations creates what has lately become known as "gray' 'and "black markets". In times of war and grave national emergencies, the

proration of foods, fuels, and furnishings may be in the public interest. Consequently, controls and restrictions in the allocation and use of essential materials temporarily cast a shadow over normal free trade.

The Right of Assembly. — In the democracies, the right of informal assembly for social purposes is freely sanctioned, particularly where the objective is that of amusement, recreation, or religious worship.[1] The rights of assembly and free speech are most precious in times of turmoil and unrest, but it is also the critical period for established forms of government. Their popular support and stability are put to the test in maintaining relative peace and orderly procedure in safeguarding the lives, happiness, and property of its citizens. In capitalistic societies, assemblies are often held under strict surveillance particularly when their avowed purpose is to secure reforms of an economic or political nature. The repressions are greater under despotic forms of government than in the democratic states. The rights of man are more narrowly interpreted in weak governments than they are in strong governments. In all civil forms of government, police power is vested in the public authority and intercessions between groups of conflicting interests depends upon the nature of provocations, the training, and the judgment of the law enforcers.

Justice in a free nation is assured to everyone, but it may be variable as determined by the ordinances of local autonomies and by the zealous diligence to duty of its petty officials. Equality before the law becomes more uniform as the individual seeks redress in the higher courts of the land.

[1] Local authorities may attempt to constrain these rights from time to time: Ex parte, Winnett, Okla., 1942, 121, p. 2d., 312. In some notable instances restrictions of rights have been sustained by the courts: Solomon vs. City of Cleveland 1926, 159 N.E. 121, 26 Ohio App. 19. Also Kline vs. Robert McBride Co. 1939, 11 NYS 2d, 674, 170 Misc. 974.

The more complex and interdependent markets become, the more important are the privileges of unrestricted communication. The first amendment to the constitution of the United States expressly provides in part, that Congress shall make ". . . . no law abridging freedom of speech or of the press; or the right of the people peaceably to assembly and to petition the government for a redress of grievances." The nearer this ideal is realized the more perfect will all markets function. Even the primitive silent trade is dependent upon some means of transmitting ideas, however crude they may be, for mutually striking an agreement on the terms of barter.

Mobility Under Surveillance — Let us momentarily consider some of the limitations that have been imposed upon these rights during the last century. Existing forms of government impart authority to its officials and in turn require an oath of allegiance which tends to assure stability in state affairs. Reluctance in adopting innovations in administrative policies, on the one hand, may eventually retard progress and interfere with the activities of freemen seeking livelihood and contentment in their daily enterprises. On the other hand, a liberal government may be overzealous in projecting reforms that are either impractical or immature, then, that species of rights bibliographically listed under the subject head of free speech may be invaded with impunity by certain contemporaneous despots who imagine themselves vested with the powers and rights of censorship. In some parts of this country transient laborers drift from place to place seeking jobs in seasonal industries. The life and plight of the "vagabond harvesters" inspired one of the classic novels of the depression era, John Steinbeck's "Grapes of Wrath". When swarms of migratory labor descend upon communities, they often disturb the

indigeneous residents and upset their normal mode of living. Furthermore, transiency creates problems of dislocation in some industries, and it strains to a breaking point the capacity of the local authorities in making necessary adjustments and in accommodating this vitally necessary labor force.

Imitative of many European states, Peruvian laws require that citizens secure authoritative permission to travel from place to place within the country. Failure to apprize the police of one's movements outside the confines of the home community makes him liable to arrest, fine, and imprisonment. More than half of the states of this nation have at one time or another attempted to impede the free movement of its citizens across state borders by passing Elizabethan laws designed to freeze indigents in their home communities. The immobilization laws, of course, are prompted by the selfish motive of shunning responsibilities for the care and comfort of those who may perchance become public charges.[2]

Right of Association. — The right of association has gradually acquired a respectable patina through centuries of experimentation, thought, and criticism. Interpreted in its broadest sense, association can include both formal and informal groups bent upon attaining a wide range of objectives. In former times people intermingled in religious pilgrimages to assuage their consciences and pacify their gregarious inclinations. They were spiritual associations primarily, but they were tinged with some temporal interests. In their bivouacs at palm sheltered oases, on the banks of estuaries, and at shrines of druid worship, market transactions were incidental at first because the carefully organized caravans were almost self-contained units. They embraced all elements of administration, justice, authority, and

[2] Edwards vs. California, 314 U. S. 160, (1941).

defense in the offices of chiefs, judges, councilmen, priests, and escorts.

The Carolingian dynasty established rights of association for trade by maintaining peace in the markets, granting concessions, giving asylum and security to foreign travelers, invoking acts and regulations governing fiscal, political, economic, and moral conduct of the traders. Gradually, these trade associations exacted from the kings some rights of self-determination such as an independent system of justice governing transactions. Fees, tolls, and other exactions were subject to review and revision after a long battle with noblemen and church powers. Finally, the right to found markets was localized by settling it upon the feudal barons who were more amenable to the wishes of the people. Later, the medieval market fairs became more specialized in the functions of facilitating barter and exchange, but these seasonal, colorful pageants were considered a great social event by the manorial dwellers. Through custom of long standing, certain trade centers of the world became venerated for the pleasurable and profitable associations they engendered.

Corporate associations provide mass franchise — The bazaars and fair markets of Europe were one of the ameliorating forces in averting a total eclipse of Western civilization during the dark ages of national isolation and provincialism. The cosmopolitan character of these market assemblages, self-contained in administering commercial justice, tended to promote international good will and inter-social appreciation. Slender though this strand, the medieval fairs connected a pretentious commercial past with an age of trade and world-wide exploration. These fairs contributed no small part in giving impetus to innovations and unheralded economic advancement, in an era implemented with such inventions as the compass, gun powder, and moveable type for printing. Among the outstanding positive changes

induced by the innovations of man, probably the concept of corporate association should be placed first in economic importance. The modern corporation as distinguished from informal partnerships and organizations under special charter has only recently emerged in a Laissez Faire Society case-hardened by rugged individualism. The corporate procedure has been refined to the point of admitting various types of mutual associations for business as well as for benevolent purposes. Through the instrumentality of these associations, now broadly recognized as a proletarian movement for mass franchise in political and economic spheres, further progress was made in legalizing certain phases of labor unionism for collective bargaining, cooperative organization for efficient and equitable distribution, and universal suffrage for broadening the base of democracy.[3]

The right of association is a fragile one not yet sufficiently grounded on historical precedent in some forms to secure its sanctity from invasion. The capitalistic, democratic states motivated by the ideal of free enterprise fear the formation of monopolistic groups. The anti-trust laws of 1890 and the periodic indictments by the Justice Department for curbing concentration and control in production and distribution by corporate interests serve to illustrate how the Federal Government has waged an unrelenting war against the abuses and exactions of powerful economic interests.

[3] The legalization of collective bargaining was not generally recognized before the middle of the 19th century. The conspiracy laws of England were revised in 1824-25 and the Clayton Act became law in 1914 without appreciably immunizing workers against prosecution under anti-trust legislation. Innocuous business enterprises operated by agricultural producers on a cooperative basis were legalized by Congress in the Capper- Volstead Act of 1922. The 19th amendment to the Constitution of the United States of America admitted women to the polls on the same basis as men, but some of the states still deny this sacred right in a democracy to certain citizens on the grounds of racial prejudice or social status.

Political divisions, a form of association — The democratic state, in reality, is an association of autonomous associations possessing jurisdiction and authority paramount to other associations operating within its province Local authorities are entrusted with upholding the laws of the state and keeping the peace. Should voluntary acts of individuals approach questionable grounds of propriety they may be constrained by the police. Any unusual assembly or association of individuals which the authorities fear might induce a riot may at their discretion be dispersed. The officers of the law are generally prompted to this action in order to safeguard property rights. They also frequently disperse crowds because they impede traffic, disturb the peace, and spread fear of violence. On other occasions, the state may take action in arbitrating disputes which arise between employers and employees. In the field of industrial conflicts there has been much "pulling and hauling" on the part of organized groups to maneuver themselves into a position of bargaining power. The law enforcing agencies by tradition remain conservative. They tenaciously adhere to the atomistic philosophy of competition with the view to keeping an equitable balance in bargaining power between opposing economic groups. Liberal policies in legislation enabling producers, consumers, and workers to form mutual associations has in some respects increased the responsibilities of the law enforcing agencies. In the field of labor bargaining, for example, the authorities are often called upon to mediate differences and forestall disturbances which may arise from picketing, lock-outs, sit-down-strikes, black-listing, etc.

The right of association may be circumscribed by police, however, where the authorities suspect perversive activities against the established form of government. Failure to take action in such instances especially where the perverters threaten to use weapons would signify

the government's inability or indifference toward its spoilers.

One of the most common infringements upon the rights of assembly and association, sometimes adopted as a subterfuge, is that of taking precautionary measures in preventing the spread of pestilence, acts which endanger the morals, or unusual hazards to the lives of its citizens. Excepting measures to apprehend criminal acts and avert escape from justice, the right of free movement across state borders within our country is not to be obstructed or denied its citizens.

Market organizations thrive best in an atmosphere of peace where buyers and sellers may meet and enter into commercial transactions legally countenanced by the state. The more freely individuals intermingle and move to and from the exchange centers, the greater will be their participation. Intensified free trade will redound to the general welfare of society arising out of the consequences of a division of labor, the fructification of specialized production, and the full enjoyment of an abundant wealth.

4. The Establishment and Maintenance of an Acceptable Medium of Exchange to Facilitate Trade.

The great empires of trade which have appeared on the scene in the Christian era invariably were founded on stable and well administered currency and banking systems. In this long history of commercial intercourse no Emperor, royal potentate or popular executive ever succeeded in forming a lasting economy without sound money. The rhythm in the ebb and flow of trade has been broken and often violently disturbed by rapacious officials who betrayed the confidence of the people by debasing the coinage or otherwise destroying its value as a medium of exchange.

The full development of money as an instrumentality

was retarded primarily by man's inability to perceive its latent powers, or to coordinate its use with the growth of commercialization. After the discovery of coinage, exchange for hundreds of years was limited to the available supply of hard money in one form or another. In numerous cases the interchange was made difficult in interregional trade because of varying standards, no adequate means of assaying the value of the metals used, and no assurance of authoritative endorsements. In other instances, when credit was utilized as a means of effecting trade, it was over extended and the tempo of trade strained the people's ability to keep pace with the changes wrought.

Greek Ingenuity

The Greeks transformed their primitive state of Agrarianism to a money economy under the reform of Solon. A state policy concerning the issue and management of money and credit was instituted. In the Greek experience, crises did occur from time to time through abuses of credit or from inexperience in coping with the exigencies which arose with commercialization. The Greeks had no basic precedents to guide them in these matters. When they encountered difficulties concerning their circulating media, they appear to have been remarkably adept in formulating new policies and procedures to meet the most urgent situations.

When supremacy in the Mediterranean passed to the Italian peninsula, there was a marked contrast in fiscal policies. Whatever may be said for the achievements of the Romans, they failed to display any understanding or appreciation for a monetary system. This fact, perhaps, had more to do with the fall of the Roman Empire than the raids of the barbaric legions from across the Alps. Disentegration began with the economic crisis of the third century, and the *denarii* fell to such a low

state of esteem in the fourth century that each piece had to be individually inspected for content and weight before it could pass from hand to hand.

By the seventh century nearly all the admirable institutions which once comprised the glory of Rome had been swept away. Anarchy prevailed in the land and trade reverted almost entirely to barter consummated under the Shadow of the Sword. The vestigial remains of their coinage system appeared in the custom of passing small ingots of copper, and other objects in exchange without benefit of standardized weights and measures, legal codes, or government authority. All the precious metals had been driven out of circulation through the unconscionable debasement of coinage imposed by successive Emperors.

Byzantine Empire Trade

The Division of the Empire reasserted the Greek influence again after 500 years and with the emergence of the Byzantium civilization commerce and good money were revived and sustained for about 800 years. It is recorded that the Byzantine Empire ceased to be the trade center of the world about 1200 A.D. and its decline was initiated by Alexius Comnenus who tampered with the coinage and brought their gold piece, the *Solidus* or *bezant,* into disrepute throughout the trading centers of three continents.

In retrospect, the broad avenue of human progress is strewn with wrecked civilizations. Some of them endured for centuries, others for only a brief interlude. The survival and success of the extensive political and economic hegemonies were based in a large measure upon integrity in establishing a sound money and credit system. This fundamental concept which governs trade and finance today may vary in some details from that which prevailed when the Greek civilization flowered,

but on one important point there is no change, — monetary and banking policies must be sound and free from the capricious acts of those in authority.

The Function of a Medium of Exchange

It serves primarily as a unit of account. The tradesman is as much dependent upon money as a measure to determine economic values as he is on the yardstick, the pound weight, or the gallon. It is an objective representation and a legally authorized means of settling debts in convenient devisible units to meet the exacting needs of everyone. It derives its value from the quantitative relationship which arises between itself and these debts. One bewildering difficulty arises in connection with the use of money as a measure or unit of account. Unlike the invariable foot rule or the pound weight, units of money vary in value themselves. Most people fail to recognize this capricious characteristic in money except in periods when the rate of decline or appreciation is accentuated.

Money, in another view, is valued for its own inherent qualities, and as such it may comprise a store of value. This subjective view favors the use of precious metals for their intrinic value. Gold still commands the respect and energies of most of the common people, and they have endured untold hardships for the sake of its possession.

Money serves still another function — one which is so important to our interpretation of trade that it may well become the dominant feature of a medium of exchange. This function is that of serving as *a standard of future payments.* Much of the business transacted today is on credit. The current medium of exchange — representative money — is itself merely a promise to be exchangeable for bullion of a given quantity and quality. In like manner, contracts which are formed calling

for the future delivery of goods or their equivalent in money forms the standard of value on which deferred settlements will be made. Through this means, notions of present and future values are correlated and the net effect is to project stability of prices into the immediate future insofar as futures contracts rule the trade. In former times, the management of a medium of exchange involved details relative to coinage and to problems concerning circulation both in quantity and number of denominations to clear the trade of an area. Today, the chief aspects of the money function turn on the extent and growth of forward transactions, maintenance of reserves, control of the volume of issue, and the regulation of interest and rediscount rates. An obligation of the highest magnitude is vested in the government to administer monetary policies in a manner to facilitate trade and protect the interests of its citizens who repose their confidence in the substantive quality and security of their legal tender. The role of media of exchanges is treated more fully elsewhere in this text. The reader is referred to Chapter 4 for further consideration of the functions of money and their influence on market valuation.

5. The Privilege of Contract

In a status society no contracts exist. Each individual is enthralled by the fetishes of superstition and the customs of the clan. He submissively settles in an appointed niche to fulfill an assigned role, bowing to the authority of the chief or the elders. Before men could indulge in the making of contracts, tradition had to be broken; for contracts are cut from the fabric of individual self-determination. The privilege of free choice is grounded upon a free will and unrestrained action. It involves the right to give, to take, to pledge, to bargain, and to perform. This new found liberty, at the outset, para-

doxically slipped from the grasp of some gullible men while they sought easy riches. Thus, they lost the very rights they brought into play in forming the contracts which deprived them of their freedom to make future choices.

To obviate this prodigality the founders of democratic states designated certain rights of men as eminent and inalienable for the preservation of freedom. In the development of the law of contracts our liberties have been further safeguarded by the principle of mutuality. The long, uncertain period of man's transition from status to contract reveals that the power to change one's station in life was begrudgingly surrendered by degrees. Evidence of this evolution is found in the substantive content of contracts as they were perceived by their principals in the different periods of history.

A One-Way Transaction

The unilateral contract eloquently reflects the vestigial characteristics of status between master and servant by its one-way directional flow of benefits with no element of consideration. It was made valid by strict observation to form. Covenants between men in the "raw ages" were small in number, and there was a poverty of contracts even in the early Christian era among the trade empires of the Mediterranean. The sealing of agreements between persons of different social spheres was first culminated by a handclasp. If one Roman informally loaned another some material supplies, the act was known as *nexum*. It represented an unilateral deal pregnant with serious intentions. Terrible were the consequences when the promisor failed to fulfill his obligations. To impress this fact indelibly in the minds of the contractors, they contrived a ritualistic ceremony — a sort of side-show performance to attract witnesses to the compact in the making.

Some Serious Sanctions

When the principals — equipped with bronze and balance — pledged one another in the presence of five or more witnesses, they elevated *nexum* into a formal innominate contract. If the obligor failed to comply with the solemn terms of his agreement, he could be seized and held in bondage.

The Twelve Tables entitled the creditor, if his claims were not satisfied, "to lead his debtor home in bondage, though not in slavery, and to bind him with cords or with shackles of not less than 15 pounds weight. Meanwhile the law assumed that the debtor would prefer to live upon his own resources . . . If, however, the debtor was really a ruined man and could not afford to support himself, the law bade the creditor to feed him on the barest diet by giving him a pound of corn a day, or more at the creditor's option."[4]

Now after 60 days, if a compromise had not been reached, the creditor may lead the debtor forth "on three successive *nundinaeor* market days (to the) *comitium* before the *praetor* and there the amount of his debt was publicly proclaimed . . . . At last on the third day . . . . (or after) sixty days, the full measure of punishment was meted out to the unfortunate delinquent: he was *addictus* by the *praetor* to his creditor, and thus passed from temporary detention to permanent slavery."[5]

It devolved on the recipient or his friends to enforce the terms of covenants, and if compliance could not be secured by guile or threat, it was often enforced with a big stick. Promises in olden times were not considered transferable, and only the promisee could exact his dues from the promisor since a third party had no

[4] Buckler, W. H.: "Contracts in Roman Law", p. 48, C. J. Clay & Son, Ave Maria Lane, London, 1895.
[5] Ibid., p. 49.

standing in court. Rough justice in the long run proved reprehensible and inadequate. As the number of persons forming contracts increased under the impetus of trade, the need for more genteel sanctions became manifest and ceremonies were devised and consummated with the act of pouring wine, symbolizing the blood that would be spilled if the agreements were breached. In time the priests took over the function of reciting the vows and pledging the contractors in the name of Jupiter or some other favorite god. "A violation of *fides,* the sacred bond formed between the parties to an agreement, was an act of impiety which laid a burden on the conscience of the delinquent and may even have entailed religious disabilities."[6]

Another form of sanction eventually appeared which consisted of a solemn appeal to the people. To fail in one's duty before the eyes of his neighbors, the guildmasters, or the social group would heap disgrace and censure on his good name and that of his family. In this forward step of punishing the delinquents, ancient formalism approached legal procedure.

Reciprocal Agreements

In contrast to the unilateral contract, the bilateral contract implies equality between principals. To be valid, it must conform to the principle of mutuality wherein it is assumed that both parties ostensibly profit from their agreement and the covenant requires consideration to implement the exchange of promises. Strict formalism in contracts gradually disappeared. Here and there a word was dropped, and now and then an act was omitted. The tendency was ever toward streamlining the mutual agreements in order to adapt them to new uses in an expanding credit economy. The state

[6] Ibid. See Chapter III, "The Twelve Tables, especially the ritual treatment of debtors," pp. 48-49.

interceded time after time to strip the creditor of powers under old rules of formalism. Enforcement was denuded of extreme sanctions such as death, enslavement, peonage, imprisonment, usury, self-imposed liabilities and some limitations on assignments. The imposition of penalties and forfeitures of property, as means of enforcement however, have persisted to the present day.

Among businessmen it became a custom "to be as good as their word." This mutual trust enormously facilitated trade and the fair merchants created their own courts — *pie poudre,* to enforce their promises one to another. The merchant law growing out of the mores of the trading fraternity became a part and parcel of every important market in Europe under the influence of migratory merchants. The merchant-enterpreneurs simply accepted mutual assent as a binding force transmuting one promise into a consideration for another promise. These promises were held valid independently in their summary courts unless they were made expressly dependent upon each other. When the merchant law was absorbed by the common law, legal authorities had their misgivings about the principle of consideration based on the circular doctrine of mutual promises.

The idea of materializing promises into performances emanated from Roman law. "Nude pacts" were in the course of time made binding merely by mutual consent. All informal promises are not made enforceable even today, but under the rules of the *pie poudre* courts in the medieval fairs, the merchants admitted few exceptions. They finally rounded out the Roman consensual contracts making them an effective trade implement in their courts to cover trade agreements, sales, rentals, employments, partnerships and agency services.

The elements constituting a legal transaction are generally considered four in number, occurring in the following sequence:

(1) *An Agreement* — The buyers and sellers strike a bargain in which the seller offers to deliver goods and the buyer accepts the offer agreeing to give in exchange other goods or remit money to the seller.

(2) *The Transfer* — Action is taken to physically deliver both goods and titles from vendor to vendee.

(3) *The Payment* — The payment is a counter-action in which other goods, money, or titles are delivered in hand by the buyer to the seller as compensation for the latter's services or endowments.

(4) *The Warranty* — The warranty is a mutual exchange of assurances that the goods or titles given in the exchange will be in full measure, pure, and of as good workmanship as they were represented to be at the time of the transaction. Without this element of assurance to buyers and sellers, it would be almost impossible to make forward commitments in the form of future contracts.

Future Contracts

The innovation of contracting to sell goods which one does not own and which may have not yet come into existence accentuates the mutual exchange of promises as a means of stimulating commercial activity. The extensive use of contracts for projecting market services into the future represents the most significant forward step in the technique of marketing since the introduction of a medium of exchange. This is true because the use of contracts has resulted in the creation of a substrative market which functions concurrently as a sustaining institution to the commodity markets. In effect, it im-

parts a third dimensional attribute to the conventional spot markets in that it elongates transactions over a period of time extending them indefinitely into the future. Moreover, it has the effect of widening as well as deepening the material markets, since they are characteristically limited both in depth and breadth by the physical features of the goods offered for sale at any zero point of time in the instant present.

The use of contracts extends the powers of individuals for self-determination. This means of expression further makes it possible for buyers and sellers to formulate plans individualizing their needs. As a consequence, the suppliers in the market are given a greater latitude in producing goods whenever possible on the purchasers' specifications, a procedure which makes for economy as well as a greater measure of usefulness to the ultimate consumers.

A futures sale is in fact only a promise to deliver something in the future, or failing this performance, to compensate the vendee for the inconvenience and expense caused by the default. The courts interpret this kind of a transaction not as a transfer of title of ownership but merely a contract to complete a transfer sometime in the future. In courts of equity, these futures contracts are construed not to pass legal title. They merely convey an equitable interest in the goods. The buyer of the equitable interest nonetheless takes precedence over all other claimants with one exception. An uninformed third party may inadvertently intercept delivery in good faith for valuable consideration. His title to the goods under these circumstances rests inviolate against the claims of the equitable interest holder. Then the purchaser of the future contract must recover from the one who breached the contract.

6. The Ability to Create Credit and the Corollary Power of Incurring and Extinguishing Debts

Credit — Men of trade pulled on their seven league boots when they conceived credit as a means of facilitating transactions, and when they put the innovation to use, their strides of progress in breaking away from the past were long and irrefragable. Exchange by means of pairing physical goods had been at best cumbersome and circumscribed by impediments. The use of money as a medium of exchange did much to liberate trade from the narrow bounds of barter, but it was not complete unto itself. The extension of credit as a complement of money was destined to permeate all economic activity infusing it with dynamic powers for streamlined performance. Now, the wheels of industry and trade are driven by the motive power of these two instruments and nearly every transaction involves the use of credit in some form as a means of payment.

From its inception the institution of credit has entailed an extraordinary effort in breaking down barriers of prejudice and overcoming the inertia of custom. Among primitive peoples, credit was inhibited by the barbaric penalty of death for failure to meet an obligation. In ancient times it was fettered by the right of the creditor to seize the person of the debtor and reduce him to the status of slavery. In the middle ages, credit was blighted by fear of imprisonment. Today, we have advanced to the stage where the borrowers run the risk of foreclosure and attachment of their properties should they fail to meet their obligations. In some respects, ours is an age of economic peonage in which the masses strive desperately to remain solvent against a schedule of fixed payments in an economy of booms and busts. It is estimated that twenty-five to thirty per cent of all business in the United States is done on some de-

ferred payment basis. In one expansive study of metropolitan retailing in the United States some years ago, it was learned that forty-seven percent of retail purchases were on open account. The Federal Reserve Bank reported consumer's expenditures in 1952 exceeded 216 billion dollars. The total consumer credit outstanding varied monthly from 19.5 to 24 billion dollars, including automobile loans. From one-half to two-thirds of all new car purchases are financed on a time payment basis. On January 1st 1953 consumer credit was at an all time high. Of this sum 69 percent represented installment credit and 31 percent open accounts or single payment loans. The moral character of a people determines in a large measure the extent to which credit will be granted. Creditors like to bask in the rays of confidence and integrity radiated by willing and able debtors. Credit is a mighty useful devise in skilled hands, but it bears the seeds of poverty for the inept. One of the militant civilians of yesteryear, Jacob Coxey, dramatizes the cycle of credit with these words: "Rags make paper; paper makes money; money makes banks; banks make loans; loans make poverty; poverty makes rags."

Dealing in credits and debts is the irksome business of the bankers, requited only by lush profits. In a central banking system any member bank may create credit to the extent of ten times its capital reserves. This discovery was made by the goldsmiths of the middle ages when they began issuing receipts and notes against the precious metals entrusted to them for safekeeping. They observed that the bailors seldom demanded more than a small proportion of the total deposits of gold and silver left in their care. Then it occurred to them that they could issue notes and receipts in excess of the gold and silver deposits without an abnormal risk of insolvency. The notes and receipts not issued against precious metals

were secured by real estate mortgages and other valuable properties. Since the goldsmiths received a customary fee for their services as bailees, these charges were carried over to the paper they issued on other securities, and their income was augmented appreciably. The transition from bailee to banker was inconspicuous, simple, and direct. The goldsmiths' notes eventually circulated freely throughout the community as a medium of exchange, and their use quickened the pulse of trade and industry. Thus were all the fundamental functions of modern banking evolved by these astute pioneers in the field of finance.

Debts — A debt is an obligation due from one person to another. It is usually canceled by an equivalent payment in the form of money, goods, or services. The restitution is ordinarily made in the same species of things borrowed, but not necessarily so. The concept of debt is linked with the prerequisite right of owning property. When one receives an advance of purchasing power, the credit creates a debit and the sum of the debit generally increases as time lapses. Debt is a dominant relationship in all economic societies today, but it has not been accorded much space even in our most comprehensive treatises on economic affairs. The colossal indebtedness incurred by the various waring nations during this century is an arresting phenomenon whether the obligations are internal or external. The public debt in the United States snowballed to the unprecedented figure of 279 billion dollars in February 1946. This debt was primarily an obligation of our government to its own people, and at that time was equal to over $7,000 per family. It was reduced to 252 billion or $6,300 per family in 1948, but since the outbreak of the Korean conflict it rose again to 260 billion or $6,500 per family 1952.

Many of the other nations of the world suffering extensive war damages are burdened with crushing debts both national and international to a state of insolvency — a condition which will remain chronic for years to come for those countries which choose to honor their obligations.

In the past, many foreign governments have culminated periods of excessive governmental expenditures by repudiation in one form or another. It is probable that we can manage our stupendous national debts in a manner avoiding the most serious dislocations in trade and industry. In order to achieve this feat, however, with a reasonable degree of internal stability, the price level may be maintained on a higher plane than at any previous period in our history. The purchasing power of the United States dollar has shrunk measurably from the golden age of parity — 1914. It fell to half its former worth in the postwar year of 1920, and now in 1953 its purchasing power has been clipped to 38 per cent of its base value. In the intervening period when deflation reached its maximum limits — 1933 — the dollar rose to only 78 per cent of its value in 1914.

Postwar inflation is rampant in some of the European and Asiatic countries. Prices in some oriental countries are fantastic in relation to the exchange rate for the pound or the dollar. Decrees issued by some tottering governments are suppressing prices to the point where enterprise is paralyzed. In any instance, the rights of individuals in these countries are being severely checked or completely reined into submission. Some of the government measures which induce stagnation of industry and the decay of commerce are: nationalization of key industries, heavy taxation of venture capital, administrative or authoritative pricing, and arbitrary allocations of supplies and services. The influence of lavish government expenditures upon the total economy is of utmost

importance to trade and industry is some other respects too. In effect, the government is thrown into business competition with many private enterprisers and price levels are often seriously disturbed.

Much depends upon who acquires the ownership of government securities issued as evidence of the public debt. The accumulation of government bonds by banks can be made an inflationary influence particularly during periods when there is a relative dearth of goods on the market because it increases the total money supply. The amount of currency in circulation at the beginning of 1940 was 7.6 billion dollars and the supply has steadily increased since then. It was 30.4 billion at the beginning of 1953. In the meantime both adjusted demand deposits and time deposits in commercial banks rose from 29 to 131 billion dollars. By contrast the supply of money during the forties increased much more rapidly than the corollary increase in the national income. It jumped from 50 percent of the national income early in 1940 to about 56 percent at the beginning of 1953.[7] In the United States under normal economic conditions the money supply should be increased at the rate of four billion dollars annually at the very minimum to accommodate the needs of a growing population and an expanding economy. If it should fall below this figure, prices may decline sharply. A centralized credit system, such as that of the Federal Reserve Bank, can influence economic trends to some extent by floating government bonds into the hands of private investors during times of prosperity and by acquiring government securities for their portfolios when business activity slumps.

[7] Committee on Public Debt Policy "Our National Debt". Series #2, pp. 8-11, 26 Liberty Street, New York 5, New York, 1947, and "Federal Reserve Bulletin," February, 1953, pp. 142-143. Board of Governor's Federal Reserve System, Washington, D. C.

In a period when markets become saturated with both consumer and producer goods, most of the dynamic forces impelling inflation are dissipated. Interest rates may also be affected when banks acquire a major interest in the public debt. Sound governments obtain money at a lower rate of interest than most borrowers. In periods when governments need much credit, the rate in effect is pegged and this rate exerts a depressive influence on all other sources of money. Easy money at low interest rates is conducive to the growth of commerce and industry, but it lessens the incentive to save. If less money is saved, it tends to reduce the supply available for investment. A reduced supply will in time cause the interest rates to rise again in a dynamic economy.

Agriculture is an industry which has large capital requirements. Farmers are proverbially in debt. On a long term basis they demand financing services for the acquisition of land, buildings, and capital equipment. On a seasonal basis, they need money to finance crop and livestock production. In the lean and hungry thirties many farmers became hopelessly enmeshed in debt. They not only became delinquent in meeting the schedule of payments on the principal, but they failed to meet interest obligations and even current living costs. Moreover, in those blighted years, they found it difficult to retain their working capital, and they failed to maintain the fertility of the soil at the same high standard prevailing before 1930. Farm machines wore out; barn floors disintegrated; roofs weathered away; seeds for leguminous crops could not be purchased; livestock was slaughtered for want of foodstuffs; fences fell down, and the weeds reclaimed dominion. This condition in our agriculture seemed to approach a similar plight described of the ancient Greeks 2,000 years ago.

"The crisis which produced the final collapse originated in the agricultural depression. The greater part of the peasants' land had come under mortgage, the evidences of which were stone pillars erected on the land inscribed with the name of the lender, the amount, the rate, and the maturity of the loan. Household finance had come in for its share of the farmer's income, the security for these loans being the person of the farmer or members of his family. These chattels, on default of the loan, could under Athenian law, be sold off into slavery, and such was the extent of the existing credit structure that the greater part of the agricultural population was in danger of being converted into actual instead of nominal slavery."

The situation on the American scene became so desperate that it was necessary for local, state, and federal authorities to intervene. Appeals were directed to creditors to scale down their claim and forego interest payments. Foreclosures were thwarted with pitchforks manned by the aroused occupants. They resisted eviction and demanded a debt moratorium. Appraisal committees were formed to re-evaluate the contractural agreements which were formed under more auspicious circumstances. In the brief span of a few years, miraculous changes were wrought in the economic status of agriculturists. During the recent war years, most of the farmers of the world waxed prosperous. Even in the battle zones, with some exceptions, the agrarians fared better than any other class of society because foodstuffs and other products of the soil were in such strong demand they commanded premium prices. Part of their gains are reflected in higher land values. In this country land values increased 156 percent in the twelve-year period from 1940 to 1947. In the same period the mortgage debt was decreased about 4 percent. This two-way gain has buoyed up farmers to a new status of inde-

pendence. The indebtedness on their land was only two-thirds as much in 1952 as it was in 1930. Another indication of their well being is reflected in the decline of tenancy in the country. In 20 years tenancy fell from 42 percent — 1930 to slightly less than 27 percent — 1952.

7. Opportunity to Protect One's Rights and Proprietary Interests by Recourse to Law and Justice Maintained by Orderly Government

The Anglo-American tradition in legal matters places great emphasis on the rights of individuals. This passion for personal freedom of action results in placing a high value on human life and its concomitant which we, for want of a better term, call rights. There are some writers who contend that our legal practitioners are overzealous in their concern over these rights of the individual. They might properly give more thought to the collective rights of the whole society in contradistinction to those of the individual. And in recent years, there is reflected in some quarters a growing manifestation of social consciousness in judicial circles. This transition in thinking, however, is probably an evolutionary phase in the birth of society in a new environment such as in the Americas.

The rights under this heading, however, are of a specialized nature related to activities of exchange. Their origin is to be found in positive laws which are in some respects variable from one locality to another and between states. These laws which create certain rights for the convenience of trade should be just and impartial and in harmony with the natural laws which supplement those of the state for the dignity of man. There can be no real liberty without a framework of laws, and the government which evokes such acts can only derive its powers by the free assent of those governed. "Lex

should be rex", in a truly democratic state, "not rex, lex."

All free men are entitled to protection of their persons and their property while engaged in any legitimate business. No one should be permitted to deprive them of these rights through violence, fraud, coercion or intimidation. Moreover, none shall deem it their privilege to malign, slander, misrepresent, injure, or distress other fellowmen for the purpose of discrediting their labors or depriving them of necessary income to sustain themselves and their dependents.

Further, all persons shall have access to any lawful occupation or to any market overt where they may compete under the law on a basis of equality. They shall have freedom of movement and no infringement upon their personal rights without a prompt and fair trial. Except in events of great national peril, each shall have the right to openly buy, sell, or contract to buy and sell all manner of goods, properties, and services (without discriminatory restrictions) which emerge from industry and contribute to the commonweal.

No special distinction shall be made for the purpose of infringing the rights of legally constituted associations which comply with just laws governing their conduct. Administrative authority should be granted for informative services, extending assistance, and guidance to those who band together in corporations to gain the advantage of pooling capital and more fully utilizing plants, machines, and raw materials.

It is the function of every good government to create the necessary administrative facilities and a judiciary system that will permit every citizen recourse in proper channels to protect these beneficient rights. The end of law is not to abrogate or restrict economic activity, but to shield, nurture, and preserve honest endeavor for the common good of the community.

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4

STAGES IN THE TECHNIQUE OF MARKET VALUATION

THE technique of market valuation has passed through at least twelve stages of development when one considers the full range of its evolution from its inception to the present time.

Successive Stages of Primitive Market Valuation

A. *Subjective Valuations*

Primitive people manifest little interest in exchange for profit. They engage in gift giving, bartering, and trading to get the things they need for immediate personal satisfaction. It is assumed that action is confined to closed associations of individuals such as family, tribe, and fellowship groups.

1. *Personal favors and friendship services are extended out of esteem and love for the recipients.* These favors of pure gifts are given primarily to those descending from a common progenitor, and the transfer is unilateral in character.
2. *Gift giving for prestige, honor, and social standing* — a form of transfer limited mainly to tribal and intratribal groups and executed by ceremonial rites.

3. *Gifts presented in exchange for anticipated gifts.* These exchanges are made on the basis of ability to give, or according to the needs of the recipient. It interjects, for the first time, the idea of reciprocity, implying a bilateral exchange. The action need not be and usually is not simultaneous.
4. *Gifts offered for gifts.* In this exchange a vague notion of equivalence of value (physical) is introduced and acceptance of the offer obligates the recipient to deliver something comparable in return. It is in this stage that the sphere of exchange may be extended to strangers and even enemies. It also constitutes the basis for barter transactions developed at a later time. At this juncture in the evolution of the primitive market, the participants may also venture beyond their own confines to pursue their acquisitive drives.
5. *Goods or services offered in trade for either goods or services* — (barter). Here the exchange is based on the idea of equivalence of value, and the action is generally simultaneous. Value in the sense of the term as applied here implies individual judgment based on usefulness because each transaction may be only slightly influenced by other deals since they are isolated in the negotiational process.
6. *Goods offered in exchange for goods.* The exchanges which occur at this point in the development of trade are slightly more complex because the principals become sophisticated. The exchange is rationalized on some basis of collective evaluation introducing the notion of mutual advantage or even individual gains from successive exchanges of a particular good.

7. *Goods offered and accepted for some commodity mediums of exchange.* The primitive traders stalled in making progress at this point for a long time. The barrier separating subjective and objective valuations was a difficult one to hurdle because the individual had not been emancipated from ritual, customs, taboos, and the tyranny of group approval. So even though the transition was made by exchanging particularized items for generalized commodities (e.g. pigs, fish, and salt) which served the purpose of a modified medium of exchange, the savage still adhered tenaciously to the superannuated notion of subjectivity in his every day relationship to the things he used and consumed.

An Intermediate Stage

B. *Modified Objective Valuations*

8. *Goods offered in exchange for crude money* — (shell currency). In this instance, objectification is limited again by the primitive propensity to circumscribe the use of precious objects. They could not conceive the idea of universality in a medium of exchange until they were taught its application by contact with some intruders from the outside. Exchange was thus limited by common consent, so the shell money might be used only for the purchase of brides and wergild. Moreover, only certain kinds of shell money of purely fanciful distinction might be used for payment in acquiring particular chattels, and this right again might be reserved exclusively for a select class or sex.

Stages of Market Valuation in the Commercial and Industrial Era

C. *Objective Valuation*

From the use of shell currency exchange was eventually conceived possible by means of a common denominator — metal coins. As this new medium was perfected, utility ceased to be the sole criterion of the worth of things, and a measure of value was adopted and exchange evolved into a more complex procedure involving three or more transfers. Finally, the use of currency authorized and controlled by strong central governments induced the traders to accept the medium of exchange generally, thus translating values into prices as common jargon of the markets.

9. *Goods offered in exchange for specie.* The transition from subjective to objective exchange has taken 27 centuries and still much trade is affected by attitudes of subjectivity especially in frontier communities and in the ravaged war zones where barter often serves as the only means of regenerating trade. In most areas of the world exchange was facilitated at first by adopting some good in universal demand as a "unit of account," such as cattle in the temperate zones. Then bullion, metals by weight, came into common use.

   Finally around 700 B. C. coinage was invented, probably evolved from the *ox* unit of Eurasia. This gradual evolution in the media of exchange provided a basis for objective valuation, and standards of value could be expressed in terms of a common denominator. Up to the middle ages, however, most users of the units of value prized them principally for their intrinsic value. In effect, the

use of specie under these circumstances was only another form of barter where two or more exchanges had to be completed to attain one's objective, i.e. direct versus indirect barter. When the rivulets of trade swelled into relatively great streams of commerce through the medieval fairs, merchants perfected their methods of exchange and specie became conventionalized. Gradually the habits of suspicion and caution were spent and the merchants accepted the monies in circulation at customary exchange rates because originally the face value of specie was kept at least equal to the value of the metallic content. Later the ruling potentates conceived the idea of reducing metallic content in relation to face value in an amount equal to the mintage costs. While this was a sound economic practice, it opened the door to the debasement of precious coins by sovereign scoundrels who lived and ruled beyond their means. Pilfering the coin of the realm destroyed its value and made it inconvertible with other perfect coins of similar issue or with currencies of other countries. This debasement did much to slow up the currents of commerce and increase the risks of trading.

In the fair courts coined money acquired two spectacular attributes which were later perfected by the law courts. One was negotiability and the other the right to cancel debts. Negotiability means the incontestable power to pass title to the transferee. The transferee's rights are then inviolate against all claimants because they are not prejudiced by any defect or flaw in the title of prior holders. Thieves

as well as honest men were thus enabled to pass good title to any coined money in their possession. The second attribute of coined money is that of legal tender. This quality entitled the holder to tender payment in fulfillment of contracts and other obligations, and creditors are obligated to receive such payments cancelling claims against their debtors. With the passing of the centuries, the use of specie was perfected and those who followed trade for a livelihood conventionally accepted coins as a means of trade. But specie never wholly diverted itself from the secondary consideration — that of its intrinsic value in relation to other similar as well as dissimilar circulating media.

10. *Goods offered in exchange for convertible paper.* Paper money is a medium of exchange which the issuer stands ready to redeem at any time equal to its face value in bullion or coins of gold, silver, or other acceptable metals. From 1879 to 1933 all Federal issues of paper money were convertible in the United States.

The roots of this form of exchange extend deep into the past anchored to the venerable custom of caching treasures at strategic points of trade. Merchants and traders traveled long distances at their peril throughout the dark ages. Often it was judicious to leave their limited stores of precious metals in the custody of the pagan priests or the *Gjaedkeri* who provided sanctuaries for the safety of persons and wealth in sacrosanct places. Refer to Chapter 13 p. 292. When this form of banking became so common that the memory of individuals needed a prop, the notched stick

was invented as a means of recording deposits. Eventually the traders adopted the notched stick as a means of accounting. Credits and debits were made convertible to gold, silver, or other precious metals by splitting the sticks lengthwise to permit the matching of the notches at a time when the traders met again to settle their accounts. The general idea of using a substitute media of exchange for specie except for settling small sums became more prevalent as time passed until much of the trade of the world was carried on by means of paper currency, convertibility of this media determined in a large measure the scope and the intensity of commercial activity. On an international basis the rate at which one nation's currency exchanges for other currencies can provide a powerful stimulus for initiating trade on a multilateral basis. If importers are seeking sources and outlets for goods, business will likely be brisk. An outstanding example of this policy in action is that followed by Belgium since 1945. Nearly all prewar trade connections in Europe had been disrupted by the war. Bases for trade between the countries had to be formulated anew. These agreements were fraught with economic and political significance which required much negotiation and time for completion.

At the risk of inducing domestic unemployment the Belgians devalued their money to a realistic level in order to provide a basis for reciprocal free trade with other nations. The resurgence of trade following this action stand out in sharp relief with that of its neighboring

commonwealths particularly in providing an abundance of consumers' goods for the Belgian people. The gains from such trade easily counterbalance any losses that may have been experienced from temporary unemployment. In the long run such a program may provide a better structure for full employment possibly than a national regulatory system which limits trade either to a unilateral exchange or within a group of countries tied to a particular currency system sustained at an independent valuation level. Uncoordinated controls are almost certain to generate intense rivalry, pitting the pound, the franc, the ruble, or the dollar one against the other driving trade over to an antiquated barter system similar to that imposed by Germany during the thirties.

11. *Goods offered in exchange for fiat money.* Most monies of the world, including coins, are now inconvertible. The insolvency of most nations following the two great world wars of this century provides a most effective means for hastening the transition from subjective to objective attitudes toward exchange. It is the contention of some monetary theorists that all monies in the modern world should be held inconvertible. They believe that the functions of money should be limited to serving as a unit of account and a standard of value. When money can be "salted away" for its intrinsic value as a store of wealth, it fails to perform its primary functions. The practice of hoarding, common in India and China, often causes capricious variations in the quantity of money in circulation which in turn may induce erratic price movements solely as a phenomenon of the circulating media.

While the United States dollar is presently inconvertible, the resources back of our paper standard are so great, including about three-fifths of the world's total gold supply and huge amounts of silver, that the whole world with few exceptions desires this currency in preference to their own. This is true mainly because other major currencies are still overvalued (1953) in relation to the dollar. When dollar exchange can be acquired to buy American goods, these goods are in strong demand everywhere both from the standpoint of price and quality.

Some of the inherent dangers of inconvertible currencies are:

1) Lack of confidence in the issue.
2) The temptation to use the printing press when the sale of government securities and taxes fail to cover current expenditures.
3) The integrity of the government in power.
4) Danger of flight of capital from the country.
5) Repudiation, et cetera.

The role of the economist is accentuated in societies using inconvertible media of exchange. Its effective use calls for analyses of the extent and character of the national income. A forecast must be made of the potential revenues to the state from taxes, the sale of securities, and other sources. Expenditures of various kinds need to be estimated and classified; in short, the procedure calls for judicious planning and expert manipulation of the various controls which will assure the

circulation of the right amount of currency to perform the dual functions of serving as a standard of value, and as a unit of account. This kind of administration is known to the bankers and economists as a "managed currency".

Now most of the nations of the world cannot afford the luxury of restricting the issue of money to their supplies of precious metals in order to give each unit intrinsic value in the form of precious physical commodities such as gold and silver in amounts equal to the stated face values. They are being gradually reconciled to the use of media which is almost wholly objectively used as a means to an end — exchange. In times of stress they fall back on physical commodities of commerce such as cigarettes, chocolates, and cameras. This mental conditioning is preparing the world of trade for what is destined to be the next major stage of market valuation — the universal use of credit.

12. *Credit offered in exchange for credit.* When men of trade reach this advanced position in commercial intercourse, all trading is based on agreements or contracts for future performance. The parties to the transaction intend and agree to transfer to one another certain rights to expected future incomes. Physical transfers are incidental to the act and purely perfunctory. The agreement involves a right and a corresponding duty on the part of each participant creating two pair of creditor-debtor transfers in each transaction as it is described much more fully in Chapter 7.

5

MODERN EXCHANGES – THEIR STRUCTURE AND PURPOSE

THE pattern for modern exchanges was formed in the medieval fairs of Europe and from certain discoveries of convenience among early traders of the Levant. Its evolution and full application to futures transactions, however, may be considered distinctly an American variation. Forward trading in one form or another has been a dominant technique in grain marketing since the middle of the 19th century and presently it has been adapted to the selling of other commodities in futures markets of the United States.

In tracing the evolution of futures trading it is difficult to fix the exact date when changes in practices or methods of operation occurred. The initiatory period for such economic development in a pioneering environment is generally one of untrammeled innovation and adjustment. This is true in the founding of new market organizations because the principals exercise a wide latitude of choices in their attempts to discover the most effective means of meeting a particular need which will yield the maximum gain with the minimum effort. Consequently, in this arena of action, changes are diffused and blended one into another until some procedure is conceded to be clearly superior to others. From these experimental efforts the trading fraternity in time formalizes its rules and regulations without precluding sub-

sequent changes, and the new market creation assumes its characteristic features.

The critical impulses which motivate changes in technology and forms of organization are featured in this chapter. The mere descriptive account of marketing procedures and elemental features of market organizations presented in earlier texts omits consideration of the conflict of interests which impelled men to devise new forms of organization to serve their purpose. These distinguished literati streamlined the subject holding close to the task of faithfully recounting the various stages and transformations of a product from the producer to the consumer. It seems unnecessary to consider this phase of the subject again. What does seem worth while, however, is to note the eventful milestones considered indispensable to the institutional approach for imparting to the reader a more comprehensive explanation of the whys and wherefores of eminent changes emerging in a society of conflicting interests. These changes like captured spirits are often enigmatic unless one is apprized of their origins. Moreover, they are generally transient and dynamic, so the one who desires to become expert in this field of specialization undertakes a life commitment of unremitting study.

Commodity Exchanges

No market operation better exemplifies the interrelationship of the three branches of study, economic history, institutional economics, and law, than spot sales and futures transactions which are integrated on the commodity exchanges. One way to make this clearly apparent is to trace the evolutionary development of a representative commodity exchange and point out like phenomena in other organizations designed to perform similar services. This procedure is predicated on the

assumption that market organizations are generally evolved to meet a specific need.[1] It is the function of the economic historian to ferret out, interpret, relate, and report any major changes which have occurred to absorb the energies of man in his wealth-getting and wealth-using activities.

These historical accounts provide the economists with factual data from which they may extract their theories and formulate programs and policies to achieve certain objectives. Legal precedent arises from another source of social experience. It is chiefly comprised of judgments formed in eliminating frictions which are generated in a society of conflicting interests as they are revealed at the bar of justice. This process of rationalization on the part of businessmen, their advisers, and the judiciary tends to crystallize into certain patterns of conduct. Some of these forms are ephemeral, and others withstand the vicissitudes of time. The survival forms become institutionalized. The pattern of conduct relating to the business of exchange forms the market institution.

The Great Primary Markets

The settlement on the fenlands adjacent to Fort Dearborn was augmented so quickly by invading frontiersmen coming around the south end of Lake Michigan that it took only five brief years for the transformation of the community from the status of a stockade to a city.[2] The great epoch of commerce for this waterway

[1] Several studies could be cited to illustrate this point. A few of these are: Goldstein, Benjamin F., Marketing, "A Farmer's Problem." The Macmillan Co., N. Y., 1928; Irwin, Harold S., "The Evolution of Organized trading in Butter and Egg Futures," an unpublished monograph; Marsh, Arthur R., "Cotton Exchanges and their Economic Function," American Academy of Political and Social Science, Volume XXXVIII, No. 2, pages 253-280, September 1911; Usher, A. P., "History of the Grain Trade in France 1400-1700." Harvard University Press, Cambridge, Massachusetts, 1913.

[2] Chicago was incorporated as a village in 1833 and as a city in 1837 with a population of 4,170.

terminus began as early as 1832 with export shipments of beef and pork.[3] An ox load of grain consisting of 78 bushels was brought to Chicago in 1838, and in the following year arrangements were made to ship 1,678 bushels of wheat by boat to Black Rock, New York.[4]

As the production of grains and meat products increased on the fertile plains, it became more and more difficult for the farmers to find satisfactory market outlets. As long as distribution remained strictly on the local level, prices were generally unsatisfactory and quite erratic. More serious still there was no assurance of a market at any price. In those pioneering days it was important to settle near a port or a navigable river because grains and other farm produce were moved to market by boat or barge. In time, storage grainaries were built along the banks of these waterways to hold grains in readiness for shipment to market just as had been done in France 300 years earlier.[5]

After the founding of the city of Chicago, it was not long before the settlers took definite steps to improve transportation facilities. They laid plank roads, dug a canal to connect Lake Michigan with the Mississippi River, and built railroads radiating out in all directions from this focal point tapping the whole mid-continent basin — the richest agricultural area in North America. The strategic location of Chicago at the south shore of Lake Michigan was destined to become the greatest primary grain market of the world. At the time the

[3] Andreas, Alfred T., "The History of Chicago from the earliest period to the present time." Vol. II p. 330, A. T. Andreas Co., Chicago 1884-1886.

[4] Taylor, Charles H., "History of the Board of Trade of the City of Chicago." Vol. I pp. 101-104. Robert O. Law Co., Chicago, 1914.

[5] Usher, A. P., "The History of the Grain Trade in France 1400-1700," p. 29, Harvard University Press, Cambridge, Massachusetts, 1913. Also see Larson, H. M., "The Wheat Market and the Farmer in Minnesota 1858-1900," p. 19, Columbia University, New York, 1926.

Civil War began wheat from the prairie states was being shipped abroad.

The Westward Migration

The lure of free lands in the West proved irresistible to thousands upon thousands of home seekers from Europe and the Atlantic states. The dramatic extension of railway systems, canals, and river transportation contributed to the rapid agrarian development in the Mississippi River Valley. The building of railroads was spurred by Federal land grants, the raising of state, municipal, private investment funds, and preferential franchises. From 1850 to 1875 the various railway corporations were granted a land acreage almost equal to the total area of the four states — Iowa, Minnesota, North Dakota, and Wisconsin.

The Need for more Efficient Market Organization

This internal expansion of the Western states made it imperative to organize a more efficient market system for moving grain, livestock, and other material resources eastward to the manufacturing and consuming centers of the country because the old methods were clearly inadequate to those engaged in the business of serving as middlemen. The farmers concurred in this conviction as evidenced by their caustic criticisms and protests against the evils of uncertain markets, poor facilities, erratic prices, and high service costs.

Responding to this need for greater efficiency in distribution, the dealers and merchants in several cities formed clubs to provide a common meeting place, to promulgate rules and regulations, create administrative and judicial procedures, arrange for the publication of current prices, and disseminate other forms of market information.

The Origin of the Grain Exchanges

The merchants of St. Louis claim the distinction of being the first to form a grain exchange. In the summer of 1836, twenty-five merchants formed what they called the St. Louis Chamber of Commerce. While the statement of purposes for this organization was broad, the initial activities of the organization were limited primarily to discussion of needs and possible means of unifying, coordinating, and improving their services. It did not immediately provide effective facilities for meeting and transacting business. For a while, the group convened after business hours once a month and the organization functioned only spasmodically during the next twelve years. In 1848, the need for a more effective organization became apparent again and the group began meeting regularly at an appointed place where news services and market quotations from other cities were made available.

In the meantime, St. Louis became one of the most important milling centers in the country. Early in 1849 the millers formed an association for their own advancement and convenience. The principals of this organization invited the grain merchants to display samples of grain for inspection at a central meeting place where purchase and sales agreements might be arranged. This interrelationship between the organized millers and merchants was so mutually beneficial, they decided to merge the two groups. In January 1950, the St. Louis Merchants Exchange was formed with 200 members. It operated successfully until 1862 when it was disrupted by internal dissention over issues of the Civil War. The St. Louis Exchange, under more auspicious circumstances, might have developed into the premier Exchange of the nation since its location was centrally strategic to the vast production of the plains states. It

was a great milling center as well as a point of converging transportation systems. Among other causes the St. Louis merchants probably lost their position of advantage to Chicago because they were tardy in adopting new technological developments in receiving, weighing, grading, and warehousing grain.

"In 1780, an endless belt with buckets attached had been invented for carrying wheat and flour in mills. From 1843 to 1848 this device operated by horsepower, was worked in Buffalo and other ports, inside a long movable 'leg' which could be lowered directly into the vessel hold."[6]

"One of the principal reasons for the rapid growth of the grain trade in Chicago during the first decade of the existence of the Board of Trade, was the fact that almost from the time of the first arrivals by canal and railroad, Chicago warehouses were forced to find a method of handling grain in bulk and by machinery, and that by this method and by their system of weighing instead of measuring, they reduced the terminal charges to about one-fourth of what the grain would have to stand if consigned to St. Louis, or the markets where the antiquated system of sacking prevailed. In other words, the terminal charges at St. Louis included the expense of sacks, amounting to seven or eight cents a bushel, against about two cents in Chicago."[7]

The merchants in the city of Buffalo similarly organized a grain dealers association as early as 1844 which they named the Buffalo Corn Exchange to facilitate terminal sales and the forwarding of shipments to the Eastern seaboard and foreign ports.

[6] The Grain Trade U.S.D.A., Vol. II, p. 184.

[7] Taylor, Charles, H., "History of the Board of Trade of the City of Chicago." Vol. II, p. 236, Robert O. Law Co., Chicago, 1914.

The Evolution of the Chicago Board of Trade

In the year of 1848, a group of Chicago tradesmen formed a voluntary association of 82 members and called their commercial club "The Board of Trade of the City of Chicago". At first they were concerned mainly with ways and means of promoting Chicago as a business center and to deal with matters of general concern to the group. The Chicagoans experienced the same difficulties as the St. Louis Chamber of Commerce in holding the group intact and maintaining an interest in their program. Contrary to the general impression adrift, the Board of Trade during its first several years of existence definitely was not a market exchange.

About 1856 the organization was instrumental in initiating some innovations in the methods of physically handling grain. It worked out and applied a system of standard grades for wheat, and in 1857 these grades were made effective by the inauguration of an inspection and weighing system. Up until 1854 grain was sold by the measured bushel. Since then it has been weighed and a minimum weight test is specified. Concurrent with these changes the Board of Trade began receiving market information from other grain trade centers, and it disseminated like reports as well as price quotations prevailing on the Chicago market. See Appendix C for list of other commodity Exchanges formed in this country.

In 1859, the Illinois legislature granted a special charter to the Board of Trade empowering it to appoint and instruct specially trained personnel to measure, gauge, weigh, and inspect grain. Simultaneous with these changes in handling grain the services of warehousing no longer remained purely incidental to the business of forwarding shipments. Corporations were formed exclusively for the function of warehousing.

Spot Trading

Open trading on the streets or in market squares was a transplanted custom from the old world, and it was common in most frontier villages of America. The wheat market in Chicago was no exception to this custom during the forties. It was not uncommon in curb trading for groups of buyers and sellers to meet at three or four different places during the course of the day and even late into the evening. As production increased in the outlying areas, it became apparent that other facilities adapted to the trade had to be made available. The merchants resolved this problem by providing a convenient meeting place under the auspices of the Board of Trade where buyers and sellers could expeditiously arrange for deliveries and payments within a brief period following their transactions. At times there was a seasonal glut of grain on the market, and at other times, when either the roads or the weather were unfavorable, there might be a dearth of farm products in relation to the demand. The Chicago merchants were among the first to adopt a technique which had been first evolved by the Genoese merchants six centuries earlier in connection with marine commerce.

"To Arrive" Contracts

Sometime during the fifties, the Chicago merchants began making contracts with sellers to deliver a specified amount of grain within a given number of days at some designated place such as a warehouse, mill, or ship. This procedure made it possible for the merchants to adjust their outgoing shipments to the variable schedule of sailing vessels or to the requirements of certain processors with a limited milling capacity. These agreements became known as "to arrive" contracts, and they extended delivery date from a few days up to as much as two months. The "to arrive" contract represents an inter-

mediate link between cash and futures contracts. Title technically passes immediately and it assures the delivery of a specific grade of a commodity sometimes sold on the basis of samples. Yet the use of such contracts permits a lapse of time between date of agreement and its performance, giving it an aspect of futurity because the buyer or seller may in turn contract to transfer their obligations in the transaction. For this reason the traders favored time contracts over spot trades because it added flexibility to transactions, and it enabled them to take either a long or short position in a semi-physical market. Moreover, trades in time contracts with the use of warehouse receipts were found to be more convenient for those who assumed a speculative position in trading since the use of the receipts obviated the necessity of receiving or delivering physical grain if the buyer should choose to offset his commitment.

The "to arrive" contracts were in all probability the predecessor of the futures contracts which were first used in this country in the sixties during the Civil War when advance government purchases of grain were made to meet the needs of the Union army. The basis for trading in futures was established even before the war when the Board of Trade defined grades and enforced them with an inspection system.

The Warehouse Receipt and Negotiable Documents of Title. — These measures made it possible to issue warehouse receipts against stored grain. The receipts were later used much like paper currency in the trade. The issue of these credit instruments made possible speculative short sales in the following manner. The shorts arranged to borrow warehouse receipts through their brokers or commission firms in the amount of their sales, which were then delivered to the buyers of the cash contracts in lieu of actual wheat. When the shorts covered, they accepted warehouse receipts in lieu of

physical wheat on their contracts. Then they promptly returned the receipts to replace the ones borrowed. The great stimulus to trade in grains induced by the "to arrive" contracts implemented by warehouse receipts made it necessary finally in 1865 to define the type of trade that had thus come into existence; and to establish rules concerning margins, sanctions, and the means of settling differences which might arise in the course of trade. Up to this time warehousemen submitted to the regulations of the board, but as volume increased making Chicago the greatest primary grain market in the world, the carriers and warehousemen became less amenable to the instruction of the Board of Trade. The fault in this case was attributed as much to the limited vision of the Board officials as it was to the growing independence of the warehousemen. The Board of Trade had not kept pace in maintaining administrative procedures adequate to cope with the growing business.

The agrarian element rose to the occasion by demanding state control through legislative action. The first warehouse law in Illinois was enacted in 1851. It provided that no receipt should be issued for grain not in storage. Moreover, a second receipt should not be issued while the first receipt was outstanding, and finally, no goods in storage should be transferred without the consent of the owner of the receipt.

The Carrier Acts. — No other legislation similar to the warehouse act designed to protect the public interest was passed until 1865. Then the legislature imposed a measure of control upon railroads effecting the movement of grain in and out of Chicago. This measure required every common carrier within the limits of their capacity to receive and forward all consignments of grain in the order in which the same were delivered or offered for transportation. Failure to comply with this rule would entitle the consignee to a forfeiture of $100 for each offense.

Another act directed at the carriers was that of 1869 which required them to transfer grain at intersection points, to provide grain cars impartially to all warehouse owners, to remove therefrom all loaded cars when instructed to do so by the shipper, and to permit cars from other connecting roads the use of their tracks for a reasonable charge.

The Warehouse Acts, 1865-1869

In the special charters granted warehousemen, the state reserved the right to regulate and limit warehousemen's control over the movement of grain to and from Chicago. The legislature prohibited them from entering into collusion through contracts with railroads to deliver grain to their Chicago warehouses when the grain was consigned elsewhere. The warehousemen were obliged under the terms of their charter to accept all grain offered if storage space was available.

In the act of 1867, it was unlawful to charge variable rates for grain received by rail irrespective of the road it came over. In order to fulfill these service requirements, the warehousemen could exercise the right of eminent domain in projecting spur tracks to their warehouses or they could demand permission to use streets and byways for expediting the movement of grain in and out of storage. Each warehouseman under this act was required to issue warehouse receipts stating the grade, kind, and quantity of grain he received for storage. The warehouse receipts bore numbers and were currently negotiable. Storage services were classified as private and public. Grain stored in private warehouses was kept in separate bins and not intermixed. The public warehouses made no attempt to retain ownership identity — the grain was intermixed. The services of the private warehouses were usually too costly. Those of the public warehouse were fraught with abuses. Some

of the limitations of public warehouses were: excessive storage rates, inaccurate reports of holdings in storage, unauthorized sale of damaged grain which had been stored more than 12 months, and improper grading and mixing of grain.

The Granger Uprising

The growth of the business of handling grain exceeded the capacity of the administrative machinery which had been created to regulate and control the industry. Discriminations and abuses pervaded the agencies entrusted to render the essential services of moving grain from points of production to the processors. The farmers organized to eliminate these weaknesses in handling their production. Their chief complaints concerned six points of grievances:

(1) They objected to the monopoly elements that had invaded the field. The farmers were critical of railroad rates, and the apparent unwillingness of common carriers to compete with one another. They objected to the consolidated holdings of warehouse space, and they looked with suspicion on the practices of the Board of Trade.

(2) The grain growers felt that the inspection services were wanting in accuracy and reliability.

(3) They protested the senseless dissention which prevailed among the service agencies. It was an open fact that the Board of Trade was waging a battle against the encroachments of the warehousemen and the common carriers.

(4) Much mischief was being created by loose regulations concerning the issue and cancellation of warehouse receipts.

(5) False information was frequently disseminated relative to the condition of grain in storage covered by receipts. These receipts were normally

in wide circulation, and their value and negotiability was at times seriously affected by erroneous reports intentionally released.

(6) The grain growers suffered heavy losses of grain in transit because no regulation existed compelling the common carriers to weigh or measure the grain loaded at the point of origin of the shipment and to check this weight at the end of the journey assuming liability for any discrepancy in the amount received and that delivered.

These aggravating circumstances coupled with an ever increasing expansion of agricultural production, falling prices, increasing taxation, and losses from railway investments irked the farmers. They agitated for broad programs of reform through political channels and by means of creating economic pressure groups. They focused their attack on the abuses of the railroads and the storage monopolies that had come into being. The grand result of this unrest manifested itself in a constitutional convention in Illinois in which the people drafted and approved by popular vote a new Article XIII for their Constitution. Other states such as Iowa, Minnesota, and Wisconsin stressed the enactment of restrictive laws similar in nature but more easily changed either by amendment or repeal if later circumstances justified modifications.

Munn vs. Illinois

The Illinois legislative act of 1871 implementing Article 13 of the state constitution provided that all class (A) warehousemen must be licensed and maximum charges were established for storing grain. The administration of this act was entrusted to a state commission for the regulation of railroads and warehousemen in handling grain. The warehousemen of the state at first refused to submit to regulation on the grounds that their

business, like any other private enterprise, was not based on franchise or special privilege of the state, and therefore, the act deprived them the free use of their property for profit.

The state brought action against Ira Y. Munn and George L. Scott for refusal to take out a license and file a bond recognizing the jurisdiction of the commission. The Munn suit became a test case, for there were 30 persons in the state who operated class (A) warehouses and none of them complied with the requirements of the act. The Circuit Court of Cook County decided in favor of the state. This decision was later sustained by the State Supreme Court and upheld finally by the United States Supreme Court.[8]

The Munn case definitely established the state's right to regulate businesses "clothed with a public interest", thus extending governmental control in the field of economics. The legal doctrine conceived in this case paved the way for socially necessary regulation of market organizations — a right which the courts have had occasion to exercise repeatedly in reviewing the operations of various commodity and stock exchanges and their corollary facilities. It might be pointed out here, however, that presumably the decisions of the courts in this and subsequent cases based on this reasoning eventually affected the whole business of storing and selling grain adversely at the Chicago terminal.

Speculators and Elevator Operators Vie for Control

The acceptance of futures trading as a regular market practice involved a sharp internal struggle between grainmen before some indefinite issues were settled. There was a contest between the specialists for control of the business. Warehouse receipts became so important

[8] Munn vs. Illinois, 94 U.S. 113, also 69 Ill. 80.

as a means of dealing in forward contracts that those who dealt in time contracts prevailed upon the state to impose regulations concerning the manner in which they were issued. This move was presumably made to protect buyers and sellers against fraudulent issues. Those who were specialized in the business of storing grain resented state control as interference with a legitimate private business, and they retaliated by inducing the Illinois legislature to declare futures contracts illegal as a form of gambling. Shortly, it became apparent that this act seriously interfered with the sale and movement of grain and probably was not strictly enforced. The legislature repealed this provision of the act at their next biannual sitting. In the meantime, the Board of Trade had formulated rules and by-laws which devised futures trading as a regular procedure based on warehouse receipts. Thus this type of trading became a distinct market practice.

The crux of this strife between the speculators and storers came into sharper relief later as the volume of grain flowing through the Chicago market increased as the total capacity of elevators was increased. The elevator operators, with some public support, prevailed upon the legislature to amend the act of 1871 giving to them the right to store grain for their own account, to mix like grades of grain received from other clients, and to issue warehouse receipts. These rights, however, were to be exercised in a non-discriminatory manner and subject to the approval of the chief grain inspector. At the time the amendment was passed, nine legal actions were pending against elevator operators for violation of the 1871 warehouse act.[9]

[9] See Central Elevator Co. vs. People, 174 Ill. 203.

Warehousemen, — Public Servants or Private Enterprisers

The court adjudged the amendment of 1897 unconstitutional and this decision was upheld by the Supreme Court of Illinois.[10] The reasoning followed in this case was that a licensed public warehouseman is committed under the original act to serve the public exclusively. That permission to do otherwise might prejudice operations in their own favor. There was evidence to show that public warehousemen had profited greatly in handling, mixing, and financing grain for their own account in conjunction with the business of receiving and storing grain as a public warehouseman.

Another evil arose from the practice of jointly holding grain in the same elevator for public account and for private use. The elevator operators became dominant as traders on the Board by virtue of having command over huge stores of grain and control over storage rates in their own elevators. They held a marked advantage over the other traders who simply engaged in dealing in cash grain or in future contracts. The court perceived in this operation the opportunity for public elevator operators to manipulate storage charges. In this practice they could discriminate against the traders who had no elevator affiliations. Furthermore they could either sell grain on sample from specific lots to meet millers' requirements or they could mix various lots to produce "skin grades" for delivery on futures contracts. This position was in the eyes of the court tantamount to a monopoly privilege which might be used to demoralize the whole grain trade.

Another angle relative to elevator services concerned terminal charges and allowances. One common carrier, for example, entered into a contract with a line elevator

[10] Hannah vs. People, 198 Ill. 77.

company to elevate and store grain either in transit or at the terminus of the line. Other handlers caused a complaint to be lodged against this sort of agreement with the Interstate Commerce Commission on the grounds that it was preferential and unfair to rival agencies.

On the basis of a report and recommendations from the Commission in 1905, Congress passed the Hepburn Act the next year. This act construed the services of elevating grain into terminal elevators and arranging transfers of grain from one carrier to another, a proper function to be performed by any railroad upon reasonable request. When such services were provided, the carriers might make a charge for them providing they were entered on a separate schedule and providing they were reasonable in amount.

The Interstate Commerce Commission in a subsequent ruling to test this act was sustained by the courts but only with respect to its delegated power of determining the reasonableness of rates, rebates, and discriminatory acts, if any. The court balked at permitting the Commission control over the use of property. In this ruling it was clearly outside its jurisdiction. The enterprisers who had invested venture capital for handling and shipping grain had every reason to expect that they be permitted to carry on in this type of business without inordinate interference from the state.

Doctrines of Public Policy in the Grain Business

Public policy pertaining to grain storage and transportation was variable and at times contradictory in the different states. The extent of public pressure from growers and handlers had affected the legislatures, courts, and commissioners in different ways. Some decisions exerted a considerable influence either in yielding positions of advantage to some specialized groups over others, or their judgment resulted in shifts in the industry.

Concepts of state control finally settled on certain principles which may be condensed in three terse statements:

Equal rates and services be given to all persons handling and dealing in grain to forestall any form of discrimination.

These rates must be reasonable to avoid monopoly rights.

All persons who find occasion to employ the services of public utilities in transporting, handling, and selling grain owe an obligation to these functionnaries to reward them liberally enough to make a fair return on their investment. In this way private property can be attracted to the public service.

In the early Illinois cases the interpretation of the courts assumed the attitude that the public warehousemen could either accept the Commissioner's rulings and abide by them, or withdraw from the business of serving the public. This harsh alternative was abandoned by the courts at the turn of the century for the fair return doctrine. Then, in 1920, the transportation act pushed the precept one step farther toward retaining private property in the public service by prohibiting shifts from public to private use.

Unrestrained individualism was running its course during the last quarter of the 19th century. Speculation in futures markets was characterized by periodic raids on the market for the purpose of cornering and squeezing the shorts. These manipulative practices produced considerable mischief among the traders and the exactions of the predacious were not salutary to the business. These spectacular forays attracted wide public notice through the press. They often caused marked price derangements, and they created unfavorable public impressions of the functions and purposes of commodity exchanges. The public's memory concerning

such things is often long and the excesses of this era still plague the commodity exchanges. Fears of exploitation form the basis for unprovoked attacks now on this form of market organization.

The piratical elements in these markets were usually in the minority. In the course of time, the men interested in the exchange for its continuous services essential to all factors in the trade asserted their authority. If they were not alert in correcting the evils of their organization, the government interceded in the public interest by passing restrictive and regulatory acts either by statute or Commissioner's rulings. As the commodity exchanges grew in number as well as volume of trade, remedial measures were applied internally by the members who desired to elevate their organizations to the maximum point of usefulness. A few of the significant changes that were instituted after the initial years of experimentation are arrayed here to illustrate the manner in which such market institutions are evolved.

A Transition in Contract Forms

The futures contract was conceived to afford greater flexibility in trading than was permissable under its prototype agreement — the "to arrive" contracts. Formerly the trade in futures contracts gave both the buyers and sellers the option of determining date of execution of the contract. Trade was generally confined to the first or second succeeding month at the inception of these agreements, and futures in wheat were bought and sold for maturity in every month of the year. Three limitations became apparent in these agreements:

It was not necessary to offer futures contracts for every month of the year.

It was desirable to project these agreements over a longer period of time, and

The whole arrangement worked better when the option rights were limited to the vendor.

Accordingly, trade was limited in wheat futures to five months of the calendar year — March, May, July, September, and December. May is regarded by the trade as the "clean up" month when the boards are cleared for most of the old crop commitments. In July the new winter wheat crop harvested in the Mason-Dixon belt moves into market channels. In September the spring wheat from the north border states flows from the grain fields. December is an important month because navigation on the Great Lakes closes and the grain is accumulated in terminal elevators for storage. The March future is the least important of the five.

Under the five-futures system, commitments are made for several months in advance of anticipated deliveries, and these are made continuous by shifting from one future to another. The maximum period of outstanding commitments at any given time is about eleven months.

The arrangement permitting either the buyer or seller the right to determine the delivery date proved awkward, so after a trial period, it was decided to limit the right exclusively to the seller. Later this right was extended to include the seller's right to determine which grade of wheat would be delivered under any particular contract. This right is limited to any commercially acceptable grade of wheat to be delivered. This option was given the seller in order to increase the volume of deliverable supplies. The multigrade contract is effective only insofar as grades are made definitive and limited in number to those readily salable. Differential values between grades must also be fairly accurately ascertainable to make possible the necessary financial adjustment on delivery from the base-grade.

One of the incentives which spurred internal reform in the grain and cotton exchanges was a hostile agri-

culture. In many states, the organized farmers pressed for restrictive laws and succeeded in passing a number of laws aimed at curbing sharp practices and culpable actions. Several of these bills were introduced in state legislatures which, if passed, would have declared futures trading illegal as a form of gambling.

Members of Congress were influenced to some extent by the tide of popular prejudice against exchange dealings. Bills were introduced in the House of Representatives and the Senate which proposed to make futures transactions illegal. One of the first bills to be presented was the Butterworth anti-option bill of 1890 which never came to a vote in the House. In 1892 three different anti-option bills were offered and referred to a committee. After some debate the Hatch Bill was selected in lieu of the three bills since it incorporated the main ideas expressed in the other bills. In the meantime, two similar bills by Washburn and Feffer were presented in the Senate. The Hatch Bill passed the House and the Senate but was defeated on a move to suspend the rules after it had been referred to the House. The Hatch Bill was re-introduced in 1894 and approved in the House, but it never came out of committee in the Senate.[11]

Another House Bill was proposed to prohibit the use of the mails for conducting the business of futures trading. From 1884 to March 1953 at least 330 bills have been introduced in congress designed to regulate, investigate, or prohibit trading in futures contracts. In the postwar years of the twenties, the Federal administration launched a broad legislative program intended to help the farmers of the nation help themselves. A

[11] Refer to a Brief entitled, "The Grain Trade" prepared for the President's agricultural Commission by the Grain Dealers National Association, January 22, 1925. This pamphlet contains a chronological listing of 30 governmental investigations 1890-1924, pp. 2-7.

number of acts, later mentioned herein, were passed relating to problems of distribution. These statutes determine the mode of operation and they closely scrutinize the structure of commodity exchanges for defects and limitations. Nearly all the well-managed exchanges in the country have stipulated rules against raiding the market, forming corners, and otherwise manipulating prices. Some of the groups have set up machinery to check any irregular deals by its members, to classify the kinds of transactions, and to determine the volume of trade in each category.

In order to increase deliverable supplies, a major problem in most futures markets, railroad receipts with grade certificates attached were finally made tenderable for grain on futures contracts during the last three days of the option month.

What is a Commodity Exchange?

A commodity exchange per se is an association of persons acting either as agents or principals in market overt. The various exchanges now in operation may vary in some details of organization and in composition of membership, but on one point they are all alike. Every exchange in this country operates as a non-profit agency. Its chief function is to provide the necessary facilities to accommodate its members, their patrons, and other interested parties in the business of marketing.

The members of the exchange are in business for economic gain and service. They may be regarded as specialists in negotiating purchases and sales of rights and titles to diverse commodities. These individuals render the essential services of creating a focal point of trade, providing a continuous market, pricing products and transferring rights to products, shifting risks, disseminating information, recording transactions, facilitating settlements, maintaining ethical standards, and sustaining justice in commerce.

The Chicago Board of Trade is described briefly as an example of the American Commodity exchanges. The association was formed originally in 1848, but its charter was not granted by the Illinois legislature until 1859. Membership on the Board is a personal privilege and corporations and partnerships are no longer admitted as members. It began with 82 members, and each member was assessed an annual fee of $5. The present membership is 1,422, and the annual dues are $300. Membership is acquired only by the purchase of a place on the exchange from another member or his estate. The new member must be a male, 21 years of age with an unassailable moral and financial record. He is not admitted to membership until he is formally accepted by the association.

The functioning body of the exchange is centered in a board of 15 directors and 4 nonmember appointees including an administrative secretary and an executive vice president. Members of the Board are elected for terms of three years. They select from their number a president and two vice presidents annually.

The Board of Trade is departmentalized and the affairs of each department are supervised by one or more committees. The department divisions cover: transportation, sampling, weighing and custody, provisions, public relations, quotations, cotton, and security. Other committee appointments relate to business conduct and to arbitration and appeals. These two committees are probably considered the most important ones by the association since they are elected from the general active membership. All other committee appointments are entrusted to the President of the Board, such as those concerning legal matters, finance, floor conduct, membership, cash grain transactions, and rules. The Executive Committee is elected from the Board of Directors.

The major function of the Business Conduct Committee is to prevent manipulation of prices and any other irregular dealings that may reflect on the name of the Board. It has access to the records of any member by common consent, and its decisions are final.

The principal duty of the Arbitration and Appeals Committee is to expeditiously settle all disputes between members or between members and nonmember patrons. This mediation committee has been outstandingly successful in settling differences and suggesting adjustments in transactions involving controversy. Very rarely are cases carried over to the civil courts from this committee's rulings.

The vitality of the association is reflected in its rules governing the conduct of the members toward one another, their respect for existing laws, execution of their contracts, observation of exchange rules, and their attitude toward customers and the public in general. If members deliberately violate their agreements, circulate false or erroneous reports on prices and other matters concerning market affairs, rig the market, raid it for the purpose of cornering available deliverable supplies, fail to execute orders of customers in the manner directed, trade with or for the account of one who is not privileged to trade on the Board, cause spurious market conditions, or act dishonorably in any way which may be inimical to the interests of the association, such actions will provide grounds for fine, suspension, or expulsion from the exchange.

For more than 90 years, now, controversy has raged around and about the efficaciousness of stock and commodity exchanges, the system of trade, and the intent and conduct of its members. These attacks have ranged from mild rebukes for short-comings to caustic condemnations. Too often the red flames of prejudice have been fanned by the demagogic denunciations of self-

styled leaders seeking public favor. On the other side of the issue, the champions of the exchanges have been guilty of loquacious and misleading statements which only served to intensify suspicions. They have condoned abuses and defended ill-considered practices which served the entrenched interests. They have likewise arrogantly resisted reforms and have poured resources into propaganda with the idea of disconcerting their critics.[12]

The crux of this dissention is, does speculation in futures contracts affect prices unfavorably both to producers and to consumers? There is no simple answer to this question. If there were, the issue would have been settled long ago. In all probability the arguments on both sides of the polemics have merit. Some of them will be considered more fully in the next chapter.

The Clearing House

The hundreds of transactions on the floor of the exchange assume a very complex pattern involving enumerable cross transfers in various quantities at different prices. Formerly, trading members were required to search out the opposite party to the trades for the day and arrange all settlements or adjustments on outstanding contracts by simple cancellation called "washes". To expedite the work of striking balances in their accounts the traders usually retired to a room where they could freely move around and meet their fellow Board members collectively called the "ring" for the purpose of determining offsets, and differences due one another.

Clearing Houses of other grain Exchanges. The Clearing Corporation — At Minneapolis and Kansas City — and at all other important

[12] Refer to a critique of the New York Stock Exchange by Samuel Untermyer — "Speculation on the Stock Exchanges and Public Regulation of the Exchanges," American Economic Review, Vol. V No. 1 Supplement pp. 22-111, 1915.

markets trading in grain futures — the method of clearing obligation between commission houses on future trades is much further developed and simpler than at Chicago. It will be convenient to refer to this method hereafter as the complete clearing house system. Minneapolis organized this system in 1891, being the first to use this method of clearing. Members or commission houses dealing in futures have formed corporations which take the place of the other party on the "street" to each trade. Membership is obtained by the purchase of stock with the approval of the directors of the clearing association. Thus the commission merchant needs to deal only with the clearing house in making settlements, putting up margins, etc. This corporation, though under the auspices of the exchange, is not structurally a part of the organization, and is thus unlike the Chicago clearing house in this perhaps somewhat unessential respect. Its functional importance is so great, however, that it may be assumed that all members trading to any great extent in future will be members of the clearing house and will put all their trades through it, though not compelled to do so by the rules of exchange. In fact, it is especially provided by the rules of these clearing houses that members of the clearing association may, by agreement, settle trades otherwise than with the clearing house.[18]

This procedure often required hours of work after each active trading session. Eventually, a Clearing House was formed to facilitate cancelling out long and short commitments and arrive at a net credit or debit for the day's activities. The principle of clearing transactions through a central agency had already been well established by central banking systems. The Board of Trade Clearing Corporation in many respects is similar in methods of operation except this agency guarantees performance of all agreements among its members and between them and the public. It is an independent self-supporting entity owned and controlled by a limited number of members of the exchange. Traders who are not members of the exchange are required to clear their trades through those who are. All contracts made in the pit must be shuttled through the Clearing House, and such contracts when accepted are treated as a proprietary right of the Clearing House. In other words, the Clearing House fortified with guarantee deposits from its

[18] Report of the Federal Trade Commission on the Grain Trade, 1920, Washington, D. C., Vol. V: "Future Trading Operations in Grain" pp. 227-228. Section 5.

members acts as an intermediate buyer or seller for them technically releasing all other parties from any further negotiations or arrangements on contracts.

Another major accomplishment of the Clearing House is that it consolidates the margin requirements to protect each contract against changes in price levels. It requires a sufficient variation margin based on previous trading records. When trade is dynamic, the accounts of members are scrutinized hourly to ascertain whether sufficient capital is on deposit to cover the anticipated net position of all trades by each member for any given trading session. The Clearing House reserves the right to call for additional margins at any time the tempo of trading appears to warrant such a call. This arrangement obviates the cumbersome *modus operandi* of posting margin requirements separately covering each contract.

Intraorganizational Control

Various investigations have revealed imperfections in organization and in procedures on different exchanges. In the evolution of these organizations the merchant members first obeyed the law of self-preservation. Their first legislation concerned rules of the game protecting their own interests. Under these rules, however, conflict soon occurred among themselves. Thus, the second line of defense had to be formed which required rules and modes of conduct to establish and delineate the business relationships one to another. Their preoccupation in forming associations which would provide opportunities for economic gain became self-centered.

The formation of Boards create esoteric groups primarily interested in making profits. Public service was a strong secondary consideration insofar as it served to attract patronage. Imitative of the medieval merchants, these exchanges not only made their own rules, they

formed their own judiciary to arbitrate differences and eliminate internal frictions. In this technique they became a law unto themselves. Formerly, the decisions of some of the exchanges admitted no judicial review. The members by prior agreement deprived themselves of the right of appeal. In this manner the exchanges "washed their own dirty linen", and the public was none the wiser.

It is a patent fact, historically, that these exchanges in general were slow to recognize that they owed any obligations to the public. The associations they had created were in their opinion private clubs. Under the impetus of drastic price declines for agricultural products the real drive on grain exchanges began in the depression of the early nineties and throughout the first decade of this century. The cause was taken up again with renewed interest following World War I. Congress passed a Futures Trading Act in 1921 which was declared unconstitutional by the Supreme Court.[14]

This set-back only refreshed the law maker's determination to delve further into the problem of regulation and control of forward selling on organized exchanges. They passed the Grain Futures Act in 1922 designed to pacify agrarian interests. This act was amended in 1936 and renamed the Commodity Exchange Act, an abridged text is given in Appendix A. Statute law, like the common law in many instances, has in a generous measure adopted the merchants' codes evolved under practical experience. The transition imparts to them the weight of state prestige and access to any authorized judiciary.

No attempt will be made to describe trading procedures on the exchanges for two reasons. Firstly, no theoretical considerations are involved and, secondly,

[14] Hill vs. Wallace, 259 U.S. 44 (1922).

there are numerous pamphlets and texts which describe and illustrate the operations of an exchange in meticulous detail.[15]

Advantages Derived from Futures Trading

In Chapter 1 it was postulated that contemporary market organizations can be found in all stages of development owing to the uneven degrees of socio-economic development in the universe whether that be the world or some great geographic area. A cross-section view of these enterprises, it was stated, would reveal progressive gradations of advancement. This premise applies especially well to modern exchanges since many of them have undergone a rather complete transmutation within a relatively short period of time. The modern exchange is an indispensable medium in a free industrial society. Without its facilities and techniques of consummating forward transactions all business endeavor would be retarded and industry semi-paralyzed. It is an efficient means of attracting capital investment and providing specialized risk bearing services.

Some of the advantages claimed for futures markets are:

1. Delineates production from marketing and enhances the utility of economic goods.
2. Creates a distinct competitive group of marketing specialists who deal almost exclusively in forward commitments.
3. Provides a continuous market.

[15] The reader is referred to the following publications for brief explanations: "Marketing Grain Through a Grain Exchange," University of Illinois and Chicago Board of Trade, 1950; "Hedging, An Insurance Medium in the Marketing of Agricultural Products," Chicago Board of Trade, 1949; "Rules and Regulations of the Board of Trade of the City of Chicago," 1949. More comprehensive reports are given in: "Grain and its Marketing" — a mimeographed text used by the Grain Exchange Institute for in service training; Baer and Saxon, "Commodity Exchanges and Futures Trading," Harper and Bros., N. Y., 1949.

4. Atomizes risks and diffuses them among persons trained in appraising and forecasting market trends.
5. Attracts necessary capital to functions of distribution.
6. Increases the efficiency of marketing services in relating cash and futures sales.
7. Enables producers to reapportion the factors of production.
8. Permits advance planning in production through hedging.
9. Promotes price stability and shortens the amplitude of price variations.
10. Yields greater returns to the producer by facilitating transfers on a broad national scale.
11. Forms a grid of the various futures markets through the practice of arbitrage.
12. Releases market quotations regularly and disseminates news and other valuable information.
13. Assures all growers and handlers accurate grades and weights which are maintained through close supervision as a necessary adjunct to futures trading.
14. Facilitates forwarding shipments in export trade.
15. Establishes a means by which deficit areas may through competitive bidding be assured of their share of supplies to meet market demand.

The bane of the commodity exchanges in an unsettled world is the constant threat of government price controls, allocations, procedural interference, and government acquisitions. Many of the exchanges in foreign lands have been closed during the last decade and displaced by government commissions.

A Tempest in the White House

To illustrate the delicate situation which arises at times when price movements are strong, the American

exchanges were subjected to an ignominous censure by high government officials a few years ago. President Truman expressed his views about futures trading in a radio message on October 5, 1947, as cited in part herewith:

> "Another factor that contributes to high prices of food is gambling in grain. Grain prices naturally respond to the law of supply and demand, but they should not be subject to the greed of speculators who gamble on what may lie ahead in our commodity markets.
>
> "There is a place for legitimate trading in futures and for hedging transactions. But 90 per cent of all accounts in a recent corn futures market were found to be speculative. Trading in wheat futures rose 75 per cent in September compared with August. Normal trading in wheat at Chicago should amount to 3 or 4 million bushels a day. In this past September, however, trading averaged almost 30 million bushels a day. In a single month, on one exchange, almost half the year's crop was traded.
>
> "I am instructing the commodity exchange commission which consists of the Attorney General and the Secretaries of Agriculture and Commerce to demand of the grain exchanges that they increase their margin requirements to at least 33 1/3 per cent. If the grain exchanges refuse, the government may find it necessary to limit the amount of trading.
>
> "I say this because the cost of living in this country must not be a football to be kicked about by gamblers in grain."[16]

As a consequence of this tirade the United States Department of Agriculture released a long list containing several thousand names of private persons who held long or short positions in the market during the years of 1946

[16] Time Magazine, October 13, 1947, p. 22, Vol. 50, part 2.

and 1947, as well as the names of public officials and exchange personnel with large commitments in futures contracts.[17]

Are Futures Contracts Circumscribed?

Most of the authorities seem to be in agreement on one point. They contend that the technique of selling futures contracts is circumscribed in its application to a limited number of commodities. The reasons given in support of this view were presumably derived by some process of rationalization rather than by experiment. Subsequently, a number of commodities have broken into the esoteric circle of futures selling with varying degrees of success after they had been excluded either specifically or by inference. The most common reasons given in support of the thesis limiting the number of commodities which may be sold for future delivery are briefly listed herewith:

The commodity must not be perishable.

It must be one for which the price fluctuates frequently and with a wide amplitude.

Units of the good must be homogeneous and fungible.

The products must be measurable both quantitatively and qualitatively either by weight or cubic content.

It must be a product that can be accurately graded.

The supply must not be controlled by monopoly interest.

Nearly all manufactured articles, especially stylized ones, are unsuited for futures transactions.

[17] N. Y. Times, p. 1, December 23, 1947.

It should be relatively free from governmental regulation or state trading.

A broad market should exist for the good, possibly a world market.

It must be a basic commodity.

Finally, it should be a product that is salable at all times for liquidity.

A number of these reasons do not apply with any degree of precision in present day trading. The periods of acmatic quality for eggs, butter, and potatoes are quite brief, indeed, and yet these products have been sold in futures markets for the past 20 to 30 years. Advancement in the science of preserving food products has broadened the area in which futures markets may operate because it facilitates grading, standardization, and deliveries over a longer period of time for a number of staple products which were not well adapted to futures market operations previously.

To specify variability of price as a prerequisite is a contradiction in itself. One of the strong arguments in favor of a futures exchange is that it stabilizes prices and lessens the amplitude of price variations. Consequently, the organization of a futures exchange which will result in the stabilization of prices in effect contains the seeds of its own destruction. A more logical deduction is that any commodity of considerable volume with normal price gyrations may attract and hold speculative interests sufficiently broad to assume the risks involved in directing its flow into market channels.

Technically, probably no commodity is strictly fungible. The problem is to evolve a grading system which will permit the intermixing or commingling of products of like characteristics so they may be freely interchanged for purpose of delivery on futures con-

tracts. Variations from the "basis grade" may be tendered at the seller's option on futures contracts. A schedule of value deferentials will determine the financial adjustment to be made between the parties to the transaction. Such a schedule of value differentials has been worked out and applied successfully by many exchanges. E.g. — The Chicago Board of Trade prescribes the following differentials for wheat:[18]

No. 1 dark hard winter wheat No. 1 dark northern spring wheat heavy	at 1½¢ per bushel over contract price
No. 1 hard winter wheat No. 1 red winter wheat No. 1 yellow hard winter wheat No. 1 northern spring wheat heavy	at 1¢ per bushel over contract price
No. 2 dark hard winter wheat No. 1 dark northern spring wheat	at ½¢ per bushel over contract price
Basis grade	
No. 2 hard winter wheat No. 2 red winter wheat No. 2 yellow hard winter wheat No. 1 northern spring wheat	at contract price

The intrusion of monopolistic interests is inevitable in a number of commodities. An open, free market attracts the prodigal and the parsimonious alike. There will always be a minority, even in the best managed markets, who will attempt to corner the supply and exact tribute from the shorts if the time appears propitious. Second-quarter 1950, a group of wealthy Chinese Nationalists operating through a number of accounts from Hong Kong raided the soy bean futures market increasing their holdings from less than a million to

[18] Similar schedules are set up for corn, oats, rye, barley, and soy beans. Refer to Rule 291, p. 68 of the Chicago Board of Trade.

nearly seven million bushels. This accumulation with actual deliveries under July contracts gave them control over more than 50 per cent of all deliverable supplies in this country. The result of this near corner made prices jump from $2.20 to $3.45 per bushel. Through skillful maneuvers these operators could, if they chose, glean a few million dollars profit by concerted action in selling their long accounts, and the Business Conduct Committee and the Commodity Exchange Authority would probably be hard pressed to prove ulterior motives in this instance.

A few of the better managed exchanges attempted long ago to empower themselves against the inroads of monopoly cliques by governing the extent of fluctuations in prices on any given day. This rule is a strategical one in that it authorizes a delaying action designed to give those who may assume the opposite side of transactions time to muster their forces. Rule 81 of the Chicago Board of Trade provides: "The Board at any time, upon ten hours' notice by regulation, may provide that there shall be no trading during any day in any grain provisions, or cottonseed oil for delivery in any specified month at prices more than a fixed limit above or below the average closing price of the preceding business day." (p. 21, Rules of the Chicago Board of Trade). This rule was amended five times between June 1, 1933 and December 31, 1938. Rule 1823 proved further that: "Trading is prohibited during any day in futures contracts of wheat, rye, barley, oats, corn, soybeans, lard, or dry salt meats at a price higher or lower than the closing price for such grain or provision on the previous day plus or minus as the case may be, the following sum with respect to such commodities:

Wheat, barley, rye, and soybeans	10 cents per bushel
Corn	8 cents per bushel

Oats	6 cents per bushel
Lard	$2.00 per cwt. lbs.
Dry salt meats	$1.00 per cwt. lbs."

This rule was amended five times between October 1, 1935 and August 31, 1948, and it was set aside once and readopted in this period. Chicago Board of Trade Rules and Regulations, p. 235.

The main objection to manufactured products, especially stylized ones, is that the supply is controlled by a limited number of processors or manufacturers. It might be pointed out, however, that since the beginning of World War II, a considerable volume of business in all types of manufactured goods has been consummated on a type of futures contract similar to the original "to arrive" contract. These "on order" deals could in time be evolved into futures contracts with proper organization and some adaptation to futures trading. It would not be beyond the realm of possibility for various canned goods' manufacturers to standardize their outputs on a national basis.

The evaporated milk companies have achieved this status substantially and so have other firms. They could conceivably elect to sell their output on organized exchanges if it appeared advantageous to do so. It is already being done for semi-finished goods such as butter, mill feeds, molasses, and vegetable oils.

It might be noted in passing that the United States Government at times does a considerable volume of business in commodities which are ruled by the futures markets. State business, a necessity in most economies, is not in itself objectionable anymore than other large accounts. It is the usurpation of the rights of the exchanges such as those imposed by the Canadian Wheat Board which arouses the resentment of those who favor free enterprise.

It is not the breadth of a market which serves as the criterion for the existence of futures trading. It is con-

ceivable that it might be a relatively narrow market in which a limited number of people specialize to a high degree. The real test is whether the depth of speculative interests is sufficient to absorb the risks of price changes which may occur while the products flow from areas of production to points of consumption. This depth may be formed by a limited number of principals possessed of lush resources who play the market to the hilt, or it may come from a large number of persons many of whom are only casual traders risking nominal sums sometimes for the pleasure or thrill of the diversion. If speculative interest is thin, futures sales may only total three or four times the physical volume delivered, but if it is profuse, it may exceed spot sales ten fold.

The stipulated requirement of limiting futures trading exclusively to basic commodities is open to question. Those who place this restriction on the market have failed to elucidate what they mean by the term "basic". As new scientific discoveries are made, our appraisal of the primary nature of products must be periodically revised. What may have been previously considered secondary to the prime necessities are now often regarded as absolutely essential for the full enjoyment of health.

Finally, it is not necessary to deal in a product that is readily and equally salable at all times. Every product offered on exchanges now involves some factors of seasonality either from the demand or the supply side, and all futures markets alternately have their ups and downs and their periods of animation and lethargy.

One may conclude from this analysis of limitations that some of them are more imaginary than real and most of them are largely fictional based on too few observations of a technique not yet fully evolved. The mode of evaluating future expectations by use of executory contracts in a free market may still be considered in its primacy.

The exchanges have been rather consistently subjected to desultory outburts of criticism from various quarters since their inception. These disclaimers have, no doubt, exerted a salutary affect in quickening the evolution of the exchanges. They have forced the issues for certain reforms, and their impact tended to perfect organization and functions, however, vexatious the ordeal may have been to the principals involved. These provocations too frequently were occasioned by the penurious acts of individual members of the association which precipitated merited censure either from its patrons or the public. The administrators authorized to govern the affairs of the exchanges were sometimes at fault too, in that they failed to recognize how delicate is the function of price making in a free economy. They apparently were unaware of the assuasive powers which flow from cultivating good public relations to cushion their associations against the shock of external attacks.

With all its shortcomings, this writer is convinced that the futures market operations are destined to become the dominant procedure either directly or indirectly for most agricultural products. It may also be adapted for the output of manufactured items whether they be capital or consumer goods. The full realization of this development in marketing may take another century or more, but it appears inevitable for all peoples who succeed in maintaining a free state both political and economic. Such a status may be achieved when a majority of the buyers and sellers acquire the habit of thinking about values objectively. To cast off the bonds of subjectivity will require much educational effort based not on propaganda or emotions as it has in the past, but on a prodigious amount of research work for a full understanding of this market mechanism in all of its ramifications.

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6

THE LEGALITY OF FUTURES TRADING

THE system of trading in "to arrive" and "futures" contracts since their inception has been plagued by a rather full complement of critics representing all phases of commercial activity. Some of the critics are chronic in voicing their complaints while others are desultory. The provocations which incite criticisms of one kind or another have in some instances been based upon some invasions of buyers' or sellers' intuitive sense of justice. More often, however, accusations have been leveled at this form of trading in a frantic attempt to find the underlying cause for disruptive changes in the economic order or for panic in the financial and trade centers of the world. The number of malcontents who voice their displeasures increases appreciably if the price gyrations are sharp and erratic. When prices rise steeply, protests emanate from consumers; when prices fall precipitously, the husbandmen and the handlers grumble. The lawmakers and government authorities have often interceded in the public interest to curb or regulate those who are held suspect of influencing the frequency, the range, and the pattern of price fluctuations whether they be up or down.

In medieval times, kings and clerics decreed measures against unjust prices and unfair trade practices. The

three transgressions against trade then were known as forestalling, engrossing, and regrating.[1] Forestalling the market consisted of buying or contracting for goods or provisions enroute to market with the view of selling them again at higher prices or of turning goods away from a particular market or inducing vendors to demand a greater price than they had originally intended to ask. The act of engrossing was committed when a person entered a market and bought up large quantities or the entire supply for the purpose of enhancing the price as a monopolist. Regrating was an offense in which one purchased goods with the intention of selling the same again in the identical market or elsewhere within the area tributary to such market at a higher price.[2]

It will be noted that medieval authorities were concerned principally with the problem of preventing speculation for a rise in prices. The practice of taking orders for future delivery was not wholly unknown to the fair merchants, but their agreements were made with full intent to make delivery. The idea of selling the market short had not occurred to the merchants of that era as a practical means of realizing gains. The technique had not yet been evolved for settling the differences between contract and market prices by means of a cash payment in lieu of actual delivery of goods.

The Age of Intolerance Against Short Selling

The merits of the fair merchants' "to arrive" agreements were never lost sight of by the succeeding generations of traders. A prototype of these agreements be-

[1] Usher, A. P., "History of the Grain Trade of France" — 1400-1700. Gras, N.S.B. "The evolution of the English corn market" Harvard University Press.

[2] Gras, N.S.B., refers to these market practices a number of times in his book, "The Evolution of the English Corn Market," 12th-18th centuries, Economic Studies, Harvard University Press, 1915, Cambridge, Mass.

came an instrumentality of major concern to producers and consumers late in the 17th century and throughout the 18th and most of the 19th centuries. The Dutch people passed laws in 1610 and 1689 designed to control speculation by imposing a tax on the profits realized from selling shares short. These laws were subsequently repealed as unworkable. In 1697 the British Parliament attacked the practice of stock jobbing by statute. The number of licensed brokers was limited to 100, and they were not permitted to deal in securities for their own account. Ten years later this law was permitted to lapse. The business of stock jobbing was destined to reach new heights in the grandiose scheme known as the South Sea Bubble. Its promoters assumed a large part of the national debt of Great Britain in exchange for exclusive rights to all trade with the South Seas. The prospective profits of the South Sea Company led to wild speculation driving share values up as much as $5,000. The crash followed and share values fell to less than $450. In the wake of this episode, 1733, Parliament passed the Sir John Barnard's Act to curb the notorious practice of stock jobbing, i.e., selling shares short. The British courts recognized the validity of the act but ruled that it was applicable only to domestic shares. As time passed, it became evident that the act served more and more as a bottleneck to the expanding economy of England. On the insistence of the London Stock Exchange and the bankers, the act was repealed in 1860. Subsequently, 1867, Parliament mistakenly imposed another restrictive measure on the securities market — the Leeman Act. This measure was pressed through Parliament as a direct consequence of the 1866 panic. It was later discovered, however, that poor banking administration rather than short selling caused the mischief. Changes in the methods of dealing in bank

shares devitalized the act, and since 1878 it has been ignored but never removed from the statutes.

Sometime later, 1724, the French attempted by decree to forbid term dealings restricting transactions to actual transfers of securities for cash. This restrictive order was a direct consequence of the bursting of the Mississippi Bubble, a colonization scheme promoted by John Law. This decree was reaffirmed in 1785 by another Royal decree suppressing short sales. After the French Revolution, popular demand called for stringent regulation of the Bourse. In 1802 its membership was limited to 60 members and short selling was circumscribed. In 1824 the French courts held that a short sale was comparable to a wager, and brokers had no recourse against their clients who refused to either make payments or deliveries of securities. This right of nonperformance was abrogated in 1856.

Slow but certain progress was made in France in 1885 when the government recognized all term dealings of the Paris curb market as legal. This precedent paved the way in 1898 to the acceptance of short selling on the Bourse and extended to it discretionary powers to limit trading among its members for future delivery in critical periods.

The German Experiment

To the Germans go the credit for graceless meddling with the exchanges in Europe during the 19th century. Low prices for grain and other products had prevailed throughout the middle 90's and German agrarian interests pressed for governmental action against the traders on the "Bourse."

In 1896 the Reichstag amended a bill pertaining to the operation of produce exchanges in a manner prohibiting futures transactions in grain, mill products, mining, and industrial shares from being consummated

upon the exchange. The law became effective January 1, 1897. This experiment ran for a period of over 3 years before the provision relating to trading in futures according to exchange procedure was repealed early in 1900. Later amendments 1904-1911 liberated exchange almost completely. This legislation provided an experiment on a grand scale to test the efficacy of spot trades versus futures transactions in grains.

It was an experiment of wide interest to the statisticians and economists of that day, and many studies were made of its effects on the price for grain sold in Germany. One author summarized these studies in the following words:

"The result of our investigation may be summed up in a single sentence. The conditions existent at Berlin during the suspension of the produce exchange, while causing great hindrance to the trade, have not induced a rise in the prices of grain, and they have not imparted greater stability to those prices if, indeed, they have not exercised a deleterious effect in both these directions."[3]

The main reasons supporting this conclusion appear to be centered in the methods of trading adopted by the dealers after futures transactions were in effect abolished. The major factors in the business of assembling, storing, importing, and milling grain in Germany chose not to violate the law. Since no official prices could be quoted on either spot or futures contracts, the dealers limited their trading to an esoteric circle of self-disciplined merchants. Most of their trades were negotiated within the walls of their private offices, and they circumspectly mediated their differences among themselves rather than submit any evidence of their operations in the courts of the land for judicial review.

[3] Hooker, M. A., "The Suspension of the Berlin Produce Exchange and its Effect Upon Corn Prices," Royal Statistical Society, London, December 17, 1901, Vol. 64, page 574.

Restrictive Measures in the United States

In the United States similar measures of restriction were advocated, but our legislative bodies on the whole acted more prudently than did the European lawmakers. One of the first measures to ban forward sales in this country was passed by Congress in 1864. Toward the close of the Civil War, the price of gold rose spectacularly and some authorities attributed this inflationary development to speculative dealings in forward sales of precious metals and of foreign exchange. After the act was passed, however, gold jumped 25 per cent in value and the act was forthwith repealed. Some states passed restrictive measures under pressure of agrarian protests, but a number of these acts were ineffectual. Some of them were later modified by amendment or repealed.[4] At the congressional level, consideration was given to short selling in the Butterworth Bill in 1890 and three different bills in 1892, notably the Hatch Bill. None of these proposals became law. In 1913 a full scale investigation was launched by the House of Representatives under the direction of Congressman Arsene Pujo. The gist of the Pujo report called for regulation of speculative dealing rather than nullification. No law was formulated on the basis of this investigation. The matter of futures transactions in stocks and other securities was considered again in 1914 and 1917 by the Senate and the House respectively with no tangible results.

The sharp recession in agricultural prices which occurred in the post-World War I period stimulated new interest in activities on commodity and stock exchanges in the United States and in Canada. The Federal Trade Commission launched an exhaustive survey of specu-

[4] Refer to Chapter V, pp. 107-117.

lative dealings on commodity exchanges. In the furor Congress became intent on curbing privilege trading.[5]

Other federal laws concerned with the operation and regulation of commodity exchanges in recent years have been described in the preceding chapter.[6]

Privileged Merchants and the Free Traders

As the power of the manorial lords and the guild merchants waned in the post-feudalistic period, restrictions upon trade were either lifted by Royal decree or honored more in breach than in observance by common consent. It was not in the interests of workers or entrepreneurs who formed the new industrial society to stand idly by and permit the surfeited land owners and the merchant princes to monopolize trade under favors of the crown. They challenged the established order and asserted their rights to produce and to trade in a greater market outside the sphere of the guild merchants. Albeit, the transition was incredibly slow. Tradition is an obstinate force even in the face of necessity. The spectre of prescriptive prerogatives continued to haunt the avenues of trade long after they had been superseded by other means in the industrial revolution. Incursions were made upon the rights of exclusive professionals operating in closed markets toward the later middle ages. The rulers in Europe began to withdraw privileges, issue ordinances, and formulate laws favoring greater freedom of industrial activity in consideration for the

[5] This form of trading includes "put" and "call" contracts which were regarded essentially as gambling transactions. A "put" entitles the holder to either deliver or sell to the maker a specified quantity or lot of bushels or shares at a particular price previously named. The "put" is acquired by one who expects the price of certain grain or stocks to decline. A "call" is the counterpart of a "put". One who holds a "call" has the privilege of calling on the giver to purchase a particular number of units or lots of the goods at an agreed price within the time fixed in the "call" option. These contracts were negotiable.

[6] See Chapter 5, pp. 112, 116-117, and 123, also appendix A for an abridged text of the Commodity Exchange Act.

general welfare of the people.[7] In 1358, Charles VI attempted reform in France. Similar efforts were made in Austria, Germany, and elsewhere throughout the 15th, 16th, and 17th centuries. Notable among these were the French reforms of 1776 and abolition of the guilds in 1791. The *coup de grace* in England occurred late — the laws of 1814 and 1835 finally swept away the remaining vestiges of prerogatives that had been in force for centuries.

During the long struggle between the privileged merchants and the free traders, the use of contracts became quite common. To facilitate contractual negotiations, the busy traders fell into the habit of simply making verbal agreements. The convenience of this procedure was readily apparent and it stimulated commercial activity. These exchanges of verbal promises became known as parol contracts and their use was augmented by the legal assumption that each party to the transaction intended to fulfill his part of the agreement to the last syllable. At first such agreements were presumably limited to small trading and nominal sums, but eventually their use was extended to include commitments in the organized stock and commodity exchanges.

The parol contract was not an effective instrument for selling goods which had not yet come into existence or which the seller did not possess. It was necessary to make them freely negotiable and impersonal. These qualities were imparted to them during the 17th century. After the contracts became assignable and the debts therewith negotiable, new difficulties arose to restrict transfers of property rights. The courts were still subjective minded in their concept of marketing. They could visualize the necessity of buying and selling commodities already in existence for future delivery. The

[7] Price, William H., "The English Patents of Monopoly," Economic Studies, Houghton Mifflin & Co., Cambridge, Massachusetts, 1906.

incidence of seasonal production was clear, and it seemed logical that one might wish to run the risk of holding physical goods for higher prices. The counterpart of such transaction, however, — selling the market short for a fall in prices — was not permissive for the greater part of two centuries as pointed out above. The lawmen failed to perceive any advantages which might accrue to society from this form of exchange and, indeed, it is still a bone of contention in some quarters.

Gambling

The difficulty arose in distinguishing this form of exchange from that of a wager. Gambling has been defined as an agreement between two parties whereby the transfer of something of value is made wholly dependent upon chance in such a way that the entire gain of one party is the entire loss of the other. Its practice has been generally considered inimical to the interests of society in most countries where high ethical standards are maintained. Gaming is abhorred by the authorities because it accentuates the element of chance in human affairs. Artificial risks are superimposed upon natural risks and no social gain is achieved. The impulse to gamble is a form of contagion that many persons find difficult to resist. They ignore the just systems of property distribution and they take leave of their better judgment in a mad desire to gain something for nothing. Its effects on the losers are often enervating not wholly compensated by the edification it brings to the winners. The most objectionable feature of this nefarious practice, however, is the harm it precipitates on so many innocent people. Most civilized states have adopted strong measures to inhibit the practice.

Its evolution in Britain is quite characteristic of the course followed in other Western nations. Although the

English courts of common law recognized debts arising out of wagers, certain exceptions were eventually made to unbridled gaming through legislation. One of the first laws against gambling was passed in 1477 in order to prevent persons from becoming impoverished by their own intemperate acts of betting.[8] Later the onus was shifted to the keepers of gaming establishments. In an attempt to get at the root of the evil, the maintainance of gaming houses was prohibited.[9] The next attack came in 1664. Parliament passed a law to curb cheating at gaming and it made void any wager in excess of £100.[10] This act was later buttressed by another making all bills, notes, mortgages and other securities offered in payment for gambling debts void. Under this law, the loser could recover all stakes in excess of £10.[11] As a national policy, state lotteries were authorized in 1782 and revoked in 1823.[12] Even petty gaming was finally abolished in 1845 when all wagering contracts were declared void.

The 1951 televised proceedings of the Senate Crime Investigating Committee exposing the sordid details of multi-million dollar betting syndicates and their corollary criminal activities aroused the American public interest to a fever pitch. One of the direct results of these hearings materialized in the new revenue measure passed in October, 1951, imposing a 10 per cent Federal tax on gross receipts. To aid the Internal Revenue Bureau proprietors of gaming establishments and their agents must register with the Bureau and secure a license

[8] 17 Edward IV, C. 3.

[9] 33 Henry VIII C. 9 (1541-2).

[10] 16 Charles II C. 7.

[11] 9 Anne, C. 19. (1710).

[12] 22 George III, C. 47 and 4 George IV, C. 60.

at a cost of $50 in order to operate as bookies or tipsters. Names of the licensees are made public. Ironically, compliance with the Federal law exposes all registrants to arrest in the various states which have passed anti-gambling laws.

The Role of Speculation

There are inherent risks in all legitimate economic enterprise. Someone must assume these risks. If not, business will cease and the whole economy will revert to a self-sufficient stage of culture. In a complex society, the function of assuming natural risks is specialized and in many instances made calculable on some scientific basis such as the mortality tables adopted by life insurance companies. Various theories have been developed in an attempt to reduce the function of pricing to a scientific basis such as the Dow Theory and others. To perform this function of risk bearing, a number of persons with capital form organizations and create institutions for the purpose of legitimately transferring such inherent risks from those who cannot run the chance or from those who do not choose to carry them to those who are trained and equipped to assume them. This function takes the form of a bilateral contract in which the seller agrees to deliver and the buyer to receive certain property rights in exchange for a specific consideration.[18] Subsequent to the organization of modern exchanges, contracts are not limited to sales for immediate delivery. Agreements are freely made in nearly all of the commodity exchanges to buy and sell contracts for future delivery. Those who wish to assume the minimum risk of price changes hedge their position by means of these contracts. In this manner, commitments in growing, holding, assembling, and processing

[18] For a more detailed discussion of the bargaining transactions, refer to Chapter 7, pp. 178-186.

commodities may be almost completely limited and refined to the actual function performed. Risk is atomized and the consequence of erratic price fluctuations is diffused. The whole procedure expedites production and distribution and paves the way for lower unit costs of operation. Many writers on the subject of futures trading have categorically stated that the principal economic function of commodity exchanges is to provide a means for hedging transactions.[14] The tendency is to overstress this feature of futures trading rather than the main function of risk assumption. The principals engaged in dealing in futures contracts have been reviled so often in the past that they have become wary of public censure. Emphasis on the insurance feature of forward trading offers a strategic line of defense against critics because the concept of insurance is now accepted as a venerable institution, and its extension to this area of business should be respected not only as a right but it should be recognized as a commendable achievement.

Net Possession Utility

This writer, however, entertains another view. The major function of those operating on the stock and commodity exchanges is that of pricing and transferring legal rights and titles to the things bought and sold. The act of hedging sets one transaction off in apposition to another with the net result of zero ownership. Those who take either a negative or positive position in the market — the speculators — are the ones who create net possession utility. Hedging is incidental to this market service. Everyone who acts as an intermediary between

[14] Baer, Julius, B. and Olin G. Saxon, "Commodity Exchanges and Futures Trading," Harpers & Bros., New York, 1949. Also, Lesar, James C., "Hedging, an Insurance Medium in Marketing Agricultural Commodities, Chicago Board of Trade, Chicago, 1950.

the primary producer and the ultimate consumer in creating possession utility must anticipate supply and demand in the future. On the basis of their judgment they make commitments which ultimately result in either a gain or a loss excepting the break-even trades. In following this line of reasoning, then, the primary service is risk assumption, and those who render this service are called speculators.

Commodity Exchange Authority Analysis of Futures Trading

The Commodity Exchange Authority has made several surveys in different markets in recent years to ascertain the nature of transactions. On June 30, 1947, a total of 4351 traders participated in the corn futures market on the Chicago Board of Trade. A review of their transactions showed that over 90 per cent of the trades in open contracts were speculative. Three-fourths of the speculators were on the long side of the market commanding rights to 43,406,000 bushels, and two-thirds of the speculators had sold 38,846,000 bushels short.[15]

A previous check on the market, September 29, 1934, revealed that 88 per cent of the accounts were speculative and 75 per cent of the open accounts were long in wheat and 74 per cent were long in corn.[16]

Another study of the characteristics of futures trading was made covering the period from October 1, 1948 to June 5, 1950 relative to open contracts in soybeans. All trades consummated on March 27, 1950, were scrutinized and tabulated to ascertain the number of speculative and hedging accounts. It was learned that 87 per cent

[15] U.S.D.A. Commodity Exchange Authority, "Commitments in Corn Futures on the Chicago Board of Trade." August, 1947 (a mimeographed report).

[16] U.S.D.A. Grain Futures Administration, Analysis of Open Commitments in Wheat and Corn Futures on the Chicago Board of Trade, September 29, 1934. Circular 397, May, 1936.

or 3,096 of the transactions were speculative. Moreover, the speculators held the bulk of the commitments on both sides of the market with a net balance on the long side. The hedgers again constituted a minority as holders of open contracts.[17]

The Problem of Sequence in Transactions

The hardheaded businessmen of the 19th century insistently pressed a query upon the makers and interpreters of laws governing trade. This issue was one of sequence in the bargaining transaction. "Why was it legal to buy and then sell and not legal to sell first and then buy?" Under the common law wagering contracts were not void per se.[18] In fact, they were upheld if not *contra bonos mores.* No rules of morality and public decency were to be violated. Moreover, they were not to pervade the interests of third parties or violate any recognized principle of sound public policy or public duty. Whether this liberal view could be extended to agreements for the future transfer of unspecified lots of goods was at one time questioned.[19]

One decision which affirmed this view was handed down in an English court early in the 19th century. It attracted considerable attention for its breadth of view on an issue that was destined to plague the lawmen for the next hundred years. The decision by the court of Exchequer was: "A contract for the sale of goods, to be delivered at a future day, is not invalidated by the circumstances that at the time of the contract, the vendor

[17] U.S.D.A. Commodity Exchange Authority, "Futures Trading in Soybeans," 1950 (a mimeographed report).
U.S.D.A. Report of the Administrator of the Commodity Exchange Authority, 1951. This report represents an excellent review of the activities of this officer for the year 1951.

[18] Jones v. Randall, 1 comp. 37 (1774).

[19] Lorymer v. Smith, 1 B. and C. 1, 3 (1822) and Bryan v. Lewis, Ryan and Moody 386 (1826).

neither has the goods in his possession, nor has entered into any contract to buy them, nor has any reasonable expectation of becoming possessed of them by the time appointed for delivering them otherwise than by purchasing them after making the contract."[20] In this case, counsel argued that if this type of transaction was declared illegal, "It would put an end to half the contracts made in the course of trade." It should be noted that the court apparently assumed that both parties in the Hibblewhite v. M'Morine case fully intended at the time the agreement was made to comply with its terms in every detail. A contemporary decision in an American court blocked out the *bete noire* from agreements to make deferred deliveries. It held that a contract is valid even though the seller does not own the thing he sells at the time the agreement is made.[21]

The Intent Test

The volume of trade carried on by means of agreements around the middle of the 19th century was on the increase both at home and abroad. In form, these agreements were above judicial reproach, but the growing practice of waiving deliveries and settling differences in market values by simple cash payments imparted a new meaning to them in the eyes of the law. They became wagers in disguise. Since such contracts could no longer be accepted on face value, it was deemed necessary to judicially analyze the motives of those who entered into such agreements to determine their validity. To implement this procedure an English court evolved the famous test of "intent of the parties to deliver the

[20] Hibblewhite v. M'Morine — Meeson and Welsby Reports of cases argued before courts of Exchequer, Vol. 5, pp. 462-466 (1838).

[21] Dodge v. Van Lear, Fed. Cas. #3956 D. C. 1837.

goods."[22] This test becomes much more explicit in the words of Justice Matthews:

". . . a contract for the sale of goods to be delivered at a future day is valid . . . when the parties really intend and agree that the goods are to be delivered by the seller and the price to be paid by the buyer; and, if under guise of such a contract, the real intent be merely to speculate in the rise and fall of prices, and the goods are not to be delivered, but one party is to pay to the other the difference between the contract price and the market price of the goods at the date fixed for executing the contract, then the whole transaction constitutes nothing more than a wager, and is null and void."[23]

The "intent test" became the cynosure of all lawmen concerned with the problem of divining the difference between true and spurious contracts of trade. It conformed perfectly with common law doctrine and during the formative years when legislation governing commerce was being written it was encompassed in the statute law of many states. The rule undoubtedly has some merit for determining the legality of bilateral contracts used in concluding exchanges on physical markets conducted on the medieval pattern. Conversely it has been proven to be totally inadequate and unreal as a guide for judging the validity of commercial transactions on our modern futures markets.[24]

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[22] Grizewood v. Blane, 11C. B. 526 (1852).

[23] Irwin v. Williar 110 U. S. 499 (1884).
Noyes v. Spaulding 27 Vt. 420 (1855).
Pickering v. Cease 79 Ill. 328 (1875).
Rumsey v. Berry 65 Me. 570 (1876).
Barnard v. Backhaus 52 Wis. 593 (1881).
Justh v. Holliday 2 Mackey 346 (1883).

[24] Taylor Telford, "Trading in Commodity Futures — a New Standard of Legality?" Yale Law Review, Vol. 43, pp. 63-106, 1933, New Haven, Conn.

A strict interpretation of this rule at first required mutuality of intent under all written time contracts. The vendor was actually required to deliver and the vendee to actually receive and pay for the objects traded in when the time for delivery arrived.[25] It had been earlier established that such time contracts were not invalidated by the circumstances that at the time the contract was made the vendor had no agreement to acquire or no possession of the goods sold. After 1885 this strict subjective attitude was abandoned because it was apparent that rigid adherance to the mutuality of intent rule was unfair if one of the parties to the transaction acted in good faith and really intended to fulfill his part of the agreement. In order to judge time contracts as a wagering proposition then it was held that both parties must mutually agree not to deliver or to receive the thing sold according to the terms of the agreement. If it can be shown that they merely desired to speculate on the rise and fall of prices with the understanding that differences between the contract price and the market price at the time the agreement terminated would be settled for cash, then the contract is void.[26]

The Right of Substitution

From the very inception of futures contracts, the parties to the transaction reserved the right to close out the deal by transfer to a third party. The substitution of parties was a feature of convenience and necessity to uninterrupted trade, and it is to be distinguished from

[25] Barnard v. Backhaus 52 Wis. 593.
Kirkpatrick v. Bousall 72 Past 155.
Roundtree v. Smith, 108 U. S. 269, 276 (1883).

[26] Bomeisler v. M. Jacobson and Sons Trust 314 U.S. 630.
Burke Grain Co. v. St. Paul Mercury Indemnity Co. of St. Paul, 58 S Ct 765; 303 U.S. 611; 82 Led. 1120.

mere assignment. If, after a contract has been properly formed, should either party find it expedient to change their mind and settle the difference by a cash settlement it will not invalidate the agreement.[27]

In nearly every transaction the element of gain or loss is present and the courts are confronted with the onerous task of winnowing the spurious from the valid speculative contracts.[28] It is undoubtedly quite evident to the lawmen that great numbers of people go in for making speculative contracts who obviously neither grow nor use the things they buy and sell. In like manner, it is equally apparent that a considerable number of the principals engaged in trading on organized exchanges are specialized risk takers who have no interest in gaining possession of the physical commodity they trade in. Moreover, the intent of hedgers in entering the market is unequivocal. They come to the market to slough their risks. This they achieve by offsetting one transaction with another. They hold no intention to either deliver or receive on the future contracts they make because the whole purpose of their trading operations would be defeated. If under these contracts they were forced to deliver or receive, their risks would be doubled instead of being cancelled out. The commodity exchange authorities report that 65 to 90 per cent of the transactions on the organized commodity exchanges, as was pointed out above, may be classified as speculative which does not necessarily entail deliveries of physical commodities. It is a well known fact that generally less than one per cent of the futures contracts are terminated by actual deliveries. The pit traders and scalpers who follow the practice of trading for small fluctuations in price and ending each day neither in a long nor short position

[27] Wilhite v. Houston, 200 Fed. 390 (CCA 8th, 1912) and Nash-Wright Co. v. Wright, 156 Ill. App. 243 (1910).
[28] Farmers Milling & Grain Co. v. Urner 151 Md. 43.

usually have no intention to receive or make physical deliveries on their contracts.[29]

The Multiplicity of Contracts Involved in Completing a Speculative Deal

Normally, three different contracts are formed for each customer's order in our modern exchanges. The first contract is between client and agent at the broker's field office. The second contract between principal and principal on the floor of the exchange in compliance with exchange rules.[30] The third contract is executed between members of the exchange and the clearinghouse where balances are struck to facilitate settlements and to expedite the operations of futures markets. This tertiary contractural relationship becomes complex as contracts are grouped for efficient execution on the floor of the exchange and transmitted to a third principal for clearance. It is almost impossible for the courts to determine mutuality of intent unless it can be clearly shown who the principals are to the transaction. Under present operating procedures when an order runs the gamut from customer to broker to clearinghouse, the real difficulty arises in identifying the principal who takes the opposite side of the transaction in the maze of deals and cross deals on a futures exchange.

Occasionally brokers are sued by their clients to recover advances, commissions, or other sums entrusted to them when transactions go awry. The usual complaint presented in these cases is that the transaction was illegal on the grounds that the broker acted in the capacity of

[29] The volume of this sort of trading is considerable on the various commodity exchanges. It has been reported to exceed 50 per cent of the trading in grain futures.

[30] See Chicago Board of Trade Rules and Regulations, Rule 16, paragraph 1.

a principal rather than an agent. It is contended that the broker had no intention of either making deliveries or receiving the commodity under futures contracts even though orders are transmitted to and executed on a central exchange. Thus the contract is construed as one of wager and in reality no distinction exists between agreements formed in bucket shops and on organized exchanges.[31]

This line of attack may be successful only under special circumstances where the broker has been overzealous, incompetent or negligent in performing his work. An action based on the contention that the broker is a principal rather than an agent is quite illogical. Two principals cannot take the same side of a contract in the same transaction. One must be the buyer if the other is the seller. The broker merely assumes the position of a principal on the exchange as a deputy of his client in order to complete the transaction. The complainant must search further for the other principal to the transaction.[32] Such effort, however, is practically futile since the contracts are freely assignable and it has been held that contracts which were valid in origin do not become invalid if parties to it subsequently agree to make a cash settlement of differences.[33] Contrariwise, a contract which may have been invalid in origin may be validated if the parties later agree to actually deliver and receive according to its terms.[34]

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[31] U. S. Dayton Bread Co. v. Montana Flour Mills Co., CCA Ohio 126 F 2d 257. Uhlman Grain Co. v. Dickson 288 U.S. 188. Burke Grain Co. v. St. Paul Mercury-Indemnity Co. of St. Paul 58 S. Ct. 765, 303 U.S. 661, 82 L. Ed. 1120.

[32] Scandinavian Import-Export Co. v. Bachman 195 App. Div. 297, 186 N.Y. Supp. 860 (1st Dept. 1921).

[33] Sprunt v. Hurst-Streator Co., 180 Fed. 782 (CCDSC 1910).

[34] Anthony v. Unangst 174 Pa. 10, 34 Atl. 284 (1896).

What Constitutes Delivery?

The mercurial nature of futures trading requires an expeditious system operating at high velocity in transferring legal rights and titles. These contracts are not only made readily negotiable, they are consolidated and reformed into substitute contracts by process of cancellation in the clearinghouse operations. This device tends to blur any distinctions between disclosed and undisclosed intentions of the parties to the contract and it makes effete the subtle agreements or understandings concerning any particular deal. All that remains of consequence is that either party may materialize the original contract by simply waiting until the time arrives for performance. But even this is not essential for brokers. Contravening the common law rule, the Supreme Court has ruled that mere substitution by "ringing out" or "setting off" in the clearance of contracts constitutes delivery. Thus every broker may speculate for his own account or for his customer's with positive assurance that he will rarely if ever be called on to receive or make physical delivery of the goods bought or sold.[85] One writer pointed out that the "intent test" would have been devitalized completely if parol evidence had been declared inadmissable to prove the illegal intent of parties to a written contract fair on it face.[86] In one case the court heeded the parol evidence rule, but like the old English proverb, "one swallow does not make a summer," one suit at law may not establish a precedent.[87]

[85] Board of Trade v. Christie Grain and Stock Co., 198 U.S. 236 (1905)
Sawyer, Wallace & Co., v. Taggart 14 Bush 727 (Ky. 1879).
United States v. New York Coffee and Sugar Exchange 263 U. S. 611, 619, 44 Sup. Ct. 225 (1924).
Board of Trade v. Olsen 262 U.S. 1, 39, (1923).

[86] Goldstein, Benjamin F., "Marketing, a Farmer's Problem," pp. 124 and 467. The Macmillan Co., N. Y., 1928.

[87] Porter v. Viets Fed. Cas. #11291, D C N.D. Ill. (1857).

Props to Support the Tottering "Intent Test"

The successive decisions cited above have riddled the inner consistency of the "intent test" to the point where lawmen were forced to indulge in chimerical observations which were too often fatal to their premises. More recently, they attempted to fortify the test by enlarging its scope to embrace "particular circumstances." That is, the court reserved the right of introspection by examining the jargon of the trade, inquiring into the traditional relationships between traders, ascertaining their economic competency, determining their vocation, enumerating the facilities they possess for compliance, and a number of other qualitative factors that might temper the explicit terms of the agreement. One concept which emerged from this obliquity was the so-called "contemplated delivery" function. The emphasis under this doctrine is shifted in that all contracts consummated on organized exchanges are in effect legal even though the parties originally intended to settle on differences rather than to submit to the inconveniences of making or receiving physical deliveries. The only condition attached to such agreements is, are the participants in any manner barred from making physical delivery of the goods in the event they so wish?

Futures Trading is in the Public Interest

Legislation in the states will undoubtedly be modulated to the federal pattern. Several states have ostensibly recognized the inadequacy of the common law rule and its limitations upon legitimate trade. Statutes have been revised which remove "hedging" from the pale of illegal transactions. Federal legislation such as the Cotton Futures Act, 1916, the Grain Futures Act, 1922, the Commodity Exchange Act, 1936, and other corollary acts governing trade on organized stock and commodity

exchanges has bestowed upon futures contracts a rank in eminence approaching that of the more orthodox contractural relations. Section 3 of the Commodity Exchange Act places a great responsibility upon members of organized exchanges and admonishes them to serve well a serious public trust.

"SEC. 3. Transaction in commodities involving the sale thereof for future delivery as commonly conducted on boards of trade and known as 'futures' are affected with a national public interest; that such transactions are carried on in large volume by the public generally and by persons engaged in the business of buying and selling commodities and the products and by-products thereof in interstate commerce; that the prices involved in such transactions are generally quoted and disseminated throughout the United States and in foreign countries as a basis for determining the prices to the producer and the consumer of commodities and the products and by-products thereof and to facilitate the movements thereof in interstate commerce; that such transactions are utilized by shippers, dealers, millers, and others engaged in handling commodities and the products and by-products thereof in interstate commerce as a means of hedging themselves against possible loss through fluctuations in price; that the transactions and prices of commodities on such boards of trade are susceptible to speculation, manipulation, and control, and sudden or unreasonable fluctuations in the prices thereof frequently occur as a result of such speculation, manipulation, or control, which are detrimental to the producer or the consumer and the persons handling commodities and products and by-products thereof in interstate commerce, and that such fluctuations in prices are an obstruction to and a burden upon interstate commerce in commodities and the products and by-products thereof and render regulation imperative for the protection of

such commerce and the national public interest therein."

In a number of states the criminal code made futures trading illegal if the principal had no serious intention of making delivery or receiving the commodity and such knowledge was imparted to his broker. An Illinois court, however, held that dealing in grain futures was no longer contrary to public policy. When such transactions are cleared through regulated exchanges the contracts must be considered valid.[38] There have been a few instances in which the "shorts" defaulted by failing to make deliveries. In most cases the court imposes a penalty reimbursing the "longs" for losses suffered as a result of non-performance.[39]

An Achievement of Concord

The number of transactions completed on organized exchanges runs into the millions each year and nearly all of them are concluded without discord. Members of the exchange agree, as a condition of membership, to arbitrate all disputes relating to their trading on the exchange. The decisions of the arbitration committees are final. Appeals are sometimes granted either as a regular procedure or by special arrangement. The exchange may refer the case to a court of law on suggestion of the disputants. This quiet means of resolving differences is inexpensive, expeditious and effective. It is practically devoid of publicity such as that which attends a long, drawn out contest in a court of law.

The dissidents who have carried their contentions to the courts in the United States to test the legality of futures trading have not been numerous over the years considering the volume of trade, the variety of trans-

[38] Albers v. Lamson 380, Ill. 35 (1942).

[39] Lewis Mears Co. v. Chicago Mercantile Exchange 1 Fed. (2d) 281 (1924).

actions, and the number of persons engaged in this type of trade.

In the hundred year period 1850-1950 there were 616 law suits on record involving transactions which are classified as speculative dealings, sales for future delivery, options, payment agreements, and wagers on the rise and fall of prices. Only 48 of these were brought into the federal courts. Eight states claim the distinction of never having tried a major suit of law involving futures trading and related dealings. When these cases are arrayed on the basis of commodities involved, they show that 57 per cent concern some one of the grains, 31 per cent related to stocks or securities, and only 12 percent are attributable to all other goods and commodities. A further breakdown of this litigation indicates that about 70 per cent of the cases are waged between individuals, 20 per cent between individuals and brokers, 3 per cent between firms of brokers. The remaining 7 per cent covered all other types of enterprises such as banks, partnerships, exchanges and sundry associations which sought recourse in courts of law to settle their transactional difficulties.

Another tabulation of the suits reveals a marked decline in the number of cases instituted in state courts during the last quarter century. There were only about 90 cases in this period. Eleven of these were begun in federal courts and a single major decision was handed down from the United States Supreme Court.[40] Certiorari was denied litigants in three other cases.[41]

In the decade 1926-1935, 61 suits were instituted in state and federal courts. The majority of these suits involved dealings in either grain, cotton, or securities. During these years the doctrines of law relating to fu-

[40] Uhlman Grain Co. v. Dickson 287 US 581.

[41] Bomeisler v. Jacobsen & Son Trust 314 US 630; Burke Grain Co. v. St. Paul Mercury Indemnity Co.; 303 U.S. 611.

tures transactions were being assayed anew in the litigation that was initiated to test the fallibility of regulatory acts (both federal and state). It was a period of great disparities and adversities which caused many persons to resort to legal recourse in an attempt to protect their economic interests.[42]

During the next 10 years, 1936-1945, only 38 citations are recorded. The litigation of this decade is much more diverse than formerly because various exchanges authorized contract trading in a number of commodities never previously offered in futures. A number of cases in this period involved other property right issues as an outgrowth of changes in transactional commitments.[43] The number of cases brought before the bar from 1936 to 1945 were less in number too, since it was relatively a prosperous period in which prices rose rather consistently toward higher levels. Moreover, the war interrupted normal business operations after 1941 and necessitated the imposition of price controls on a national basis which anesthetized the commodity exchanges.

Bases for a New Legal Concept of Futures Trading

The judicial attitude will be slow to change even after new doctrines have been pronounced or a new formula evolved effecting futures contracts because it is in the nature of the judiciary to move slowly and cautiously. Moreover, there will be a time lag between the development of new concepts and decisions resulting therefrom. It is encouraging to note that an occasional article appears in the scientific journals pointing out the razzle-dazzle logic used by some courts in an attempt to reconcile the business of exchange in the physical mar-

[42] Refer to Vol. 15, 4th Decennial Digest (1926-1936) American Digest System, West Publishing Co., St. Paul, Minnesota.

[43] See Vol. 22 — 5th Decennial Digest (1936-1946) American Digest System, West Publishing Co., St. Paul, Minnesota.

kets with transactions in the futures markets. So obvious are the limitations of these decisions that it has become a matter of major concern to those who are interested in the techniques, procedures, and validity of modern futures transactions."

The problem rests upon the relationship that should exist between cash and futures markets. Undoubtedly cash markets will always exist in which buyers and sellers may negotiate for specific lots of a commodity. This type of market institution is invariably strongly influenced by terrestrial conditions effecting the production and utilization of commodities. The cash or spot markets are patronized in the main by producers, processors, and consumers. The things which are bought and sold in these markets, nevertheless, are rights and titles giving ownership and control to specific units of goods. The sellers impart and the buyers receive possession of the goods immediately or shortly after the transaction. The prevalence of this form of trade interlinking the transfer of rights to the physical delivery of the good creates a subjective attitude toward all transactions which has pervaded the legal view in the form of "intent to deliver." But the doctrine of "intent to deliver" has become archaic in recent years because technological changes have been speedily evolved to meet the needs for a more positive and expeditious system of marketing. Evidence of this change has been traced through the numerous court decisions cited above, particularly the cases referred to in footnote 35. The account balances which result from trading in time contracts are much more acceptably settled with cash than with the actual product. Residual settlements by delivery of the physical commodity may result in a net disutility to one or both parties to the transaction or at least it entails

" Harvard Law Review, Vol. 45, pages 912-925 (1931-32).

an inconvenience most traders wish to avoid. The legal fiction that has plagued the courts is that the cash and futures markets are actually tied to one another by the fact that physical delivery is mandatory if the contracts are not offset by opposite transactions.

This slender strand which ostensibly causes the two markets to move in a horizontal parallax approaching the termination date was unobtrusively severed in 1905 when it was held that the intent of brokers to close out their contracts by "setting off" or "ringing out" did not invalidate their contracts.[45] This significant decision may be construed to be applicable to trades in the pit as well as in the clearinghouse since the contracts are merely transferred to the clearinghouse to expedite cash settlements and clearance by cancelling out opposite trades. The court left the status of trade in futures between brokers and customers hanging in the balance. This is the gossamer that ostensibly links the two markets and causes them to function in a harmonious relationship within reasonable limits. It is argued that it also serves as a point of distinction between a bucket shop and a legitimate futures market.

What curious line of reasoning could be offered to invalidate transactions between brokers and their customers where intent to "off-set" is clear, since the courts have held that brokers may indulge in such transactions with impunity? Brokers do trade for their own account as well as for their customers. The fact remains that delivery is, as Irwin maintains, "a minor function."[46] As futures markets develop, this function is destined to become less and less important. Nearly all hedgers enter into futures transactions with the intent of off-

[45] See Board of Trade v. Christie Grain and Stock Co., Supra note 35.

[46] Irwin, H. S., "Legal Status of Trading in Futures," Illinois Law Review, pages 156-157, Vol. XXXII, No. 2, June 1937.

setting one contract with another. Thus, as Irwin further points out, "a strict construction of the 'intent test' would include a number of them as gamblers." Another disadvantage of the "test" is that it, "would bestow its blessing upon a manipulator who was 'squeezing' the shorts in spite of the damage which results from such an operation, simply because he was engaged in receiving the commodity upon his contracts."[47]

Two Specialized Markets

The difficulty arises from confusing the functions of the two markets. Those who are interested in "delivery" should go into the cash market where rights to specific lots may be purchased to fulfill definite requirements. Failure to make delivery in these instances might result in a real economic loss and cause considerable inconvenience to the principals who intend to deliver and receive the physical commodity. Buyers and sellers normally enter this market with the clear purpose of acquisition or disposal of rights associated with particular goods which may not be fungible or duplicated in kind, degree, or quality. A breach of such contract should entitle the aggrieved to specific performance or adequate compensation to obviate an economic loss which may in some instances exceed the actual value of the original goods.

The function of the futures market can be sharply delineated from that of the cash market. Its primary role is that of determining prices for the present and projecting them into the future. A relatively new element has been interjected into the price making process by these futures markets. It is the presence of a body of speculative experts whose collective judgment in market overt is backed up with their own capital under

[47] Ibid, pages 162-63.

the supervision of government authority. Other countries are contemporaneously pursuing a different course of action. They have closed many of their futures exchanges or anesthetized their operations to the point of ineffectiveness. As a substitute for the free market, a corps of official statisticians are entrusted with the task of determining, forecasting, and fixing prices. These men assume a great responsibility, but they are not required to support their collective judgment in pricing with their own cash. Which system of pricing is the superior one? The answer to this question depends in a large measure upon circumstances. In national exigencies the latter may be expedient although not necessarily superior. Wherever possible, people should organize free market institutions because they are an integral part of the democratic process.

The futures market gives direction to the whole movement of physical goods into channels of use through objective contractual commitments, and it interrelates values at different centers of trade. Secondarily, in this type of market, risks may be shifted from those who do not have the inclination, the capacity, or the resources to carry them to those who specialize in risk assumption. Moreover, the net result of this form of trade provides a continuity of market opportunities that cannot be gotten in any other way. Those who enter this market do so with the clear intention of trading in rights and titles. Rarely do they ever intend to receive the physical commodity as a result of their transactions. They fully intend to make settlements by paying differences in cash because deliveries of physical commodities on futures contracts are on the whole unsatisfactory for specific uses.

Criteria for the Formulation of Another Test of Validity

The criteria which a court should use in determining the validity of contracts in the futures market are as follows:

(1) Is there a natural or inherent risk which must be borne by someone in the market process?
(2) Does this type of market render necessary economic services?
(3) Is it in the public interest?
(4) Are third party interests jeopardized by its existence in a commercial society?

The contracts which are made in "bucket shops" represent unregulated, isolated transactions between the operators of such shops and would-be speculators. The contracts thus formed are usually based on quotations surreptitiously obtained from organized exchanges operating in market overt. The spurious transactions of the bucket shops are generally not published and they play no part in price determination. Consequently, no desirable economic service is rendered, and since these shops divert business from legitimate exchanges, they are not conducted in the public interest.

If the courts will recognize the division in the classification of market institutions with cash or spot markets on one side and futures markets on the other, then a firm basis is established for creating a new doctrine of law validating contracts in futures markets. The above criteria do not postulate a physical interrelationship between the two markets. They are conceived as two separate and independent market institutions each organized to perform a specialized function. For any given commodity or related commodities the futures markets and their corollary cash markets seek their own price plane, but they are influenced by similar forces within their universe. These chief motivating forces

are the factors of demand and supply which may vary only slightly with reference to each series of rights and titles; consequently, the two markets closely resemble one another in the values they establish as they course through time.

Is there great jeopardy in severing the Gordian knot (the right of physical delivery) which now ostensibly binds the two markets together in an indissolvable bond? If, indeed, it is the slender reed upon which so much is at stake, the courts have been remiss in their custodianship of such a precious vinculum. Brokers and agents are permitted to settle their contracts by paying the differences in cash. Less than one per cent of the trades are consummated by physical delivery on the great exchanges. Admittedly, it is quite impossible to apply the doctrine of "intent to deliver" in modern exchange transactions because of their complexity. Since the original concept of strict adherence to "intent to deliver" on the part of either principal to a transaction, successive decisions have cut away the underprops of the doctrine making it effete.

While the cash and futures markets have in a large sense reached a point of specialized services and some degree of independence in operations, one has become dependent upon the other in price leadership. The futures markets, because of their scope of operations, the number of active participants, the volume of business, and their facilities has become the dominant one in forecasting market trends and prices. The operators in the cash market usually base their offers and make their acceptances with an eye on futures quotations. These markets have been thus related for many years, but they do not always maintain a normal spread as measured by the expense of storage and other costs to date of delivery. If either market should gyrate errat-

ically from the normal relationship for some reason which seems illogical to the traders in the other market, they may pursue an independent course in pricing and in performing other market services until the two markets again assume a characteristic cash-future spread.

When this occurs it sometimes creates the problem of inverse carrying charges, and hedges become more imperfect.[48] The possibility of being forced to make or receive physical deliveries on futures contracts is of little restraining influence in price determinations now. Far more important are the regulations and requirements of the Commodity Exchange Authority in curbing piratal raids, price manipulation and other predatory acts which may transcend the ordinary forces of supply and demand.[49] Partly on their own initiative and partly in response to outside critics, the traders have over long years of experience formulated rules and sanctions in the internal government of futures markets which are designed to curb such predatory acts as manipulation, corners, and false rumors by unscrupulous members. This has been done in order that their organization may become a more perfect market institution for serving all who are engaged in the business of bearing necessary risks and projecting market values into the future.[50]

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[48] Working, Holbrook, "Theory of the Inverse Carrying Charge in Futures Markets," Journal of Farm Economics, Vol. XXX, No. 1 (February 1948) page 3.

[49] U.S.D.A., Commodity Exchange Authority Report Supra note 17.

[50] Under the Cotton Futures Act, for example, hedging has been made a more perfect form of insurance by a requirement that differences in price between the various grades deliverable on futures contracts be determined by actual cash differences as gauged on spot markets. A tax of two cents per pound of cotton is imposed if trading is not conducted in conformity to the rules of the exchange. All contracts must be in writing according to paragraph 4 of the act.

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7

THE CONCEPT OF FUTURITY

IF one turns to the sages for words of wisdom about time, he will discover no unanimity of opinion among them. In fact, they appear to be utterly confounded in their divergent views, concerning either the past, the present, or the future. Some appraise the past as the harbinger of the future while others regard it as burnt embers. There are those who hold that the present is all that counts, the past is dead, and the future is uncertain. The exponents of the future declare it infinite in the good it holds and the opportunities it affords for greater happiness and well-being. An American proverb gives expression to this sentiment in words of action, "Hats off to the past, coats off to the future."

In the economic science, one of the most elusive concepts is that of time. It evades the firm grasp, and it defies encirclement. It is an abstract idea freighted with relative values for which no bench mark exists. Economic analysis applied to problems of exchange has generally followed lines of deductive reasoning. The orthodox approach to the future has simulated crawfish locomotion with rear to the front and eyes on the past guided by the landmarks of anteriority. As a consequence, the classicists, the mercantilists, and the hedonists drew no sharp distinction between the existence of

material things — corporeal properties and their ownership. To them, objects of use constituted wealth, and ownership simply meant possession of such wealth.

To the institutionalists goes the credit for discerning the basic significance in the series of dichotomies: production and exchange, efficiency and scarcity, and wealth and ownership which provide new means for the economic interpretation of values.

The Power of Future Expectations

All ownership extends from the instant present on into the future. It connotes legal control, and legal control gives one dominion over objects of desire which may be transferred to others or withheld from them at the possessor's discretion. Without this essential right obtained through some form of market action, neither production nor consumption can occur. No transactions would take place if the participants were not motivated by future expectations. A person can only appreciate the attributes of a thing as they come toward him from out of the future, and one may hope that the fountain of munificence will not run dry before it serves the intended purpose.

The core of the subject of marketing is the transaction. Transactions are essential to attain ownership which in a civil society assumes a multiple significance bearing on the usefulness, the quantity, the future use, and the legal control of the thing which is being transferred. It is in essence a legal-economic-ethical relationship formed between man and man in their effort to acquire rights to scarce goods which they believe will have a future value. Even though the present supply of some particular perishable or seasonable good were so abundant it could virtually be considered a free good, it is almost certain to command a present price for future delivery to fulfill anticipated needs.

Actual possession of physical goods is an arresting fact which commands forbearance from those who respect law and order. "Possession is nine points of the law."[1] Primitive peoples are singularly impressed by adverse possession based on the principle of "might is right." This phase in the evolution of property rights, as outlined under origins of private property in Chapter 2 and described further as an institutional development among the aborigines in Chapter 12, emphasizes the subjective attitude of the untutored man toward nature and its stimulating effects upon his being. This same attitude toward material goods carried over generally to the medieval traders, although they improvised certain means of trade which revealed some of the basic elements in commercial relationships.

Beliefs in immortality and its influence upon economic affairs — For many centuries following the introduction of monotheism in the world notably the Christian concept, people appear to have expended much of their mental resources upon the idea of their relationship to deity and other cosmic speculations. Scholasticism which dominated thinking in the Western world for nearly eight centuries (800-1600) was eminently preoccupied with a controversy between the adherents of a mystical and intuitional philosophical tradition on the one hand, and intellectualism on the other. This schismatic argument between the nominalists and the rationalists may not have completely monopolized thought during this long period, but it obscured pragmatism to the point where it was ineffective. At least the milieu of that period was one that could not be considered conducive to the development of an economic science. The influence of this protracted period of philosophico-religious thought cast its long shadows over the new era

[1] An English proverb of the seventeenth century.

of industrial revolution. For nearly two centuries the economists of the traditional school of thought were off on a cold trail misguided by a series of hypothesis which were later found to be inapplicable. The spell of man's relationship with God is reflected in Smith's devine abundance theory handed down to him from Locke through Hutcheson. In their view, a certain harmony prevails between man who is inherently good and his creator making of earth a sort of paradise. In this paradise they believed man would enjoy devine abundance, — cornucopia would never cease to pour forth fruits of a bounteous harvest.

The Principal Actor in a Natural World

When Hume established scarcity as a precept of inescapable reality for economic science, the philosophers cast about for other anchorage to which they might attach their new found discipline. Under the full import of Darwinism, they abandoned the original premise that the science should reflect devine munificence to man for ideal conduct in his acquisitive activities. They concluded from circumstantial evidence that the new relationship was one between man and nature. The eternal struggle to sustain life by wresting a living from a niggardly nature dramatized the idea of the "survival of the fittest" and justified it, however harsh its implications, as the new basis of economics. From this theory of "tooth and claw" we inherited the dictums, "competition is the life of trade"; Gournay's "laissez faire, laissez passer"[2]; LaSalle's "Iron Law of Wages," and Ricardo's theory of marginality as it applied to rent for the use of land. The classicists and their protogonists labored

[2] An expression which presumably originated with a French merchant named Legendre. The idea of a "natural order" in economic affairs was prevalent among Italian economists before it became the maxim of the physiocrats of France.

under the impression that the study of economics could be formalized by a series of laws, precepts, and principles, and this continued to be the general view of many brought up in the classical tradition. Insofar as attention can be limited to phases of production subject to economic interpretation, sometimes called engineering economics, such a field of specialization can be reconciled on the premise that it involves a correlation between man and nature in the natural order. The variability of man's reaction to materialism, however, continued to be inexplicable notwithstanding the analytical possibilities of macroeconomic techniques.

Marketing Involves Objective Personal Relationships

The founding fathers of economics gave scant attention to the theoretical implications of market transactions when judged by their writings. If they had perceived that the major premise of economics rested on the primary relationship of man to man rather than man to nature, they may have become absorbed in an analysis of market organization and its evolution. Moreover, they might have attempted to formulate principles, and fathom the techniques of operation with the net result that marketing as a field of specialization, within the greater realm of economics, would have been better rounded out and more fully developed than it is today.

The early social critics of the economic order vaguely suspected an aberration in the orthodox notion of property but they failed to "pin point" their shafts of criticism on the vulnerable postulate supporting the classicist's view. If they had directed their attention to the epochal judgments and opinions prevailing in the merchant and common law courts of their time, they could have discerned a cogent new idea relative to property which had been worked out by the legalists long before the economists dipped their pens in ink.

First of all they might have noted that prices and values are in every instance an expression of human judgment because values are exclusively created in the human mind. Next, that these expressions of price and value are variable and always relative since they merely represent one man's judgment against the judgments of all other persons concerned with any particular economic good.

After judgments have been formed concerning the value of things, then and only then, can action be initiated to acquire objects of desire. This action assumes a relationship of one individual to another. Even in a primitive society this relationship assumes complex forms bearing on economic conditions, ethical standards, and on the status of the individual. In the more advanced stages of societal organization, this relationship is formalized by a series of rules and regulations finally crystallized into laws signifying general mutual consent. Thus, when law and order are established among men, their relationship one to another assumes the form of recognized legal rights. These legal rights are designed to govern their conduct in the ordinary pursuits of working and living together. Where conflicts arise in the incessant pursuit of a livelihood, the principals are expected to arbitrate their differences in a peaceful manner through advisory counsel in which they tacitly recognize dependence upon one another anticipating future dealings. In more extenuating circumstances they may resort to a court of law wherein they manifest their faith in an orderly authoritative procedure in resolving their differences.

In each and every instance, the relationship is one of man to man, and the contributing stimuli affecting economic activities are not material stuff as so many laymen believe; it is the right to the future use of economic goods. Objects need not be corporeal to have a price. They attain a price often before they come into

existence because it is the abstract rights to a thing which impart value to the traders in the market place.

The Time Element in Marketing

No one can use a thing in the past — that's a logical impossibility. The water which has turned the mill wheel has transmitted its gravitational power, and the millstones will cease to grind the grist when the stream fails to flow. MacLeod pioneered the idea of injecting the time element into economics. His contemporaries, the classicists, were apparently oblivious to this unexplored area fraught with implications relating to the origin of values. Like other explorers without benefit of compass, he momentarily lost his bearing and became confused by the undulations of theory and practice in the rough terraine of legal practice applied to the early industrial era. He observed that the landlords, bankers, and industrialists capitalized their future income. This practice, however, was ostensibly limited to one year. The banker discounted a loan by the sum of its annual interest rate. The landlords collected their rent in advance, and the industrialists demanded advance payments before they would undertake the fulfillment of certain contracts. It was this phenomenon which inspired MacLeod to formulate a discount policy for the Bank of England to control the flow of gold in and out of its coffers.

The Finite Present and the Infinite Past and Future

In attempting to square this practice with the theory, MacLeod stretched the present to a measurable period limited to one year. This breach between the past and the future was a concept of convenience to rationalize the seeming practice of projecting the emoluments of corporeal property over an annual span of time.[8] There

[8] MacLeod, H. D., "The Elements of Economics," Vol. I., pp. 156-157.

was a serious oversight in MacLeod's classification of time periods in economics, but his prosecutors charged him with the wrong crime. He did not overlap the past with the future, but he counted the future twice. He extended the present one year into the future without creating some attribute of property as its counterpart that could be distinguished from corporeal or tangible things of the past as against the incorporeal or intangible properties of the future. Thus, he mistakenly double-counted the future as it applied only to one's own use of corporeal things for one year of the future. This confusion was not singular with MacLeod, his contemporaries had not perceived the distinction between an anticipated flow of time interrupted by transactions and the lapse of time which involves forbearance. This distinction, when finally brought into clear relief, enabled the economists to delineate profits, the return to the entrepreneur, from interest, the return for use of capital.

MacLeod's regrettable error of attempting to stretch the present into a year in order to account for the practice of discounting the future probably deprived him of enduring fame as an economic theorist. In his treatise preceding his discussion of the problem of discounts, he clearly described for economic consideration the true relationship between past, present and future. No ownership exists in the past. The present constitutes only a fleeting instant of time which is so brief that only an infinitesimal part of any right has significance. A savage may pluck a berry from a bush in passing which he immediately consumes. In this instant, a right has been appropriated, but we may ignore this minute portion for all practical purposes. In the more complex situations, a person negotiates a transaction to acquire proprietary rights primarily in expectation of future benefits. The transfer of ownership is a present trans-

action projected forward to an ever-present moving point of time. Thus, all ownership lies in the future; another way of expressing this idea is: man emerges out of the past, acts in the present, and lives in the future. His whole existence of any consequence is what lies before him; so he lives in expectation of the amenities of life.

It Takes Two or More to Trade

The subject of marketing is exclusively concerned with one particular attribute of things — their exchangeability. The economic quantity bought and sold in the markets is legal rights which have both positive and negative concomitance popularly called debts and credits. The transaction in a modern economy is the means of consummating an exchange.

The minimum conceivable number of persons involved in an exchange is two. Two brave men in a lawless society who engage in barter in defiance of tribal taboos. This mode of exchange in a primitive society, however, generally involves many participants rather than two.

Where transactions are isolated from the influence of competitive offers and bids, as they are frequently in exchanges among farmers, three persons form the minimum necessary to make the deal — a buyer, a seller, and a representative of the judiciary who stands ready to maintain law and order in the event a dispute ensues.

In organized markets the absolute minimum number of individuals necessary to complete a transaction is five, a buyer, a seller, a prespective buyer, a prospective seller, and a judge. The prospective buyers and sellers serve two functions. They provide the necessary competition to protect the economic interests of active buyers and sellers and they may serve as witnesses when disputants come before the court.

Exchange and Transaction Contrasted

In Chapter 4 the successive stages in the technique of market valuation were listed and briefly described. This array of (twelve) procedures serves primarily to show the extent to which market negotiations have been evolved through gift giving, barter, exchange, and transactions. At this point it is important for a fuller understanding of contemporary business to distinguish more clearly the transaction from its prototype known in the trade as exchange.[4] The average man thinks of exchange as a transfer of physical products. It is the Sayian ultimate concept of "things are given in exchange for things"[5] even though exchange is defiled by the use of money, hindered by delays in delivery and made turbulent by unaccountable variations in value due to imperfect competition. It is essentially a static notion of material quantities offered on the market squares of the orient and in the spot markets of the occident. The equation of exchange is focused on the possession of materials rather than on concomitant rights.

In a transaction viewed as an institutional process a price is paid to acquire the rights which ownership imparts rather than to acquire material goods because without these rights possession becomes an empty husk. It may expose the individual to risks and liabilities which far outweigh any advantages gained from illegal possession. To comprehend fully the concept of futurity it is necessary to become completely objective and to center attention on attributes of physical goods rather than on the goods per se.

One of the common items in commerce today is gasoline or "petrol" as it is called in Europe. When an

[4] In popular usage the word "exchange" is loosely interpreted as a synonym for all form of trade ranging from barter to futures transactions.
[5] Refer to Chapter 8, "The Law of the Markets".

automobile owner drives into a filling station and requests the attendant to "fill 'er up" what has he purchased? Is it gasoline or is it a right to a potential store of power? He actually acquires the future attributes of this product with the assured expectation that its power will propel his car along the streets and highways during the next few hours or days. He could not possibly utilize this liquid power in an instantaneous manner at the very moment of purchase. His main concern, then, was for future rights to the ergs of energy it could impart when injected into an engine designed to convert the power and transmit it in a desired manner. Commodities as such are of no consequence whatever to those who serve as intermediaries in the modern boards of trade and they are not properly the subject matter of the science of marketing. The commodities merely serve as vehicles of the characteristics under consideration. This idea stands out in bold relief against the idee-forces of materialism. In a dynamic society the accumulation of goods provides a force which rises against the present as a support for future action, but it never exceeds the zero instant of the present. The usefulness or the efficiency of these goods in the meantime, may either increase or diminish pending the valuation of rights of future possession.

Economic Goods Have Three Dimensions of Value

At this juncture, the relationship between the different concepts of value in economic goods may be appropriately considered to elucidate further the distinction futurity value holds in any discussion of marketing. Further comment on these value relationships may clear up some obscurities of a paradoxical nature and reconcile variations in opinions based on emphasis attributable to specialized disciplines within the field of economics.

All economic goods have three dimensions. This triad may be illustrated in the following way:

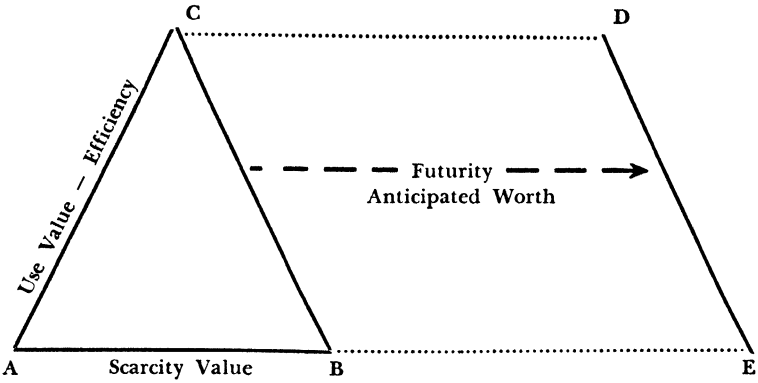

Figure 2

In triangle ABC — AB is made to represent scarcity and AC to represent use. Combined they represent any given zero instant of time in any transactional negotiation. These two physical diversions of height and width are dependent variables of the futurity function CD and BE. Time, as a function of depth is dramatized graphically by moving the triangle along a plane through space. All rights of ownership extend into the future along the broken lines CD and BE. The rights of the immediate present depicted as a flat exposed surface ABC are vendible only when made contingent upon CD and BE because only an infinitesimal part of any future right arrives at the instant present and can have no appreciable independent value of itself without reference to the future. At the very moment rights are acquired they begin to fade into the past because only by this concept of time is it possible to appreciate the nature of debts and credits and their role in the determination of market values based on expectation. Hitherto, much of the emphasis in marketing has centered on use and scarcity values because the time factor was either ignored or assumed. This attitude toward the problem of market valuation was strongly influenced by a type of economy where exchange was restricted pri-

marily to barter or to purchase and sale in which goods were visibly displayed for critical examination under the rule *caveat emptor* and were passed from hand to hand without delay.

The Bargaining Transaction

Exchangeability is the keystone in the arch of principles, laws, rules, and concepts relating to economic activities. Commons goes so far as to assert that it is the only principle with which economics has to deal. This generalization is based on the epochal discovery of a debt market by MacLeod. He perceived a dual relationship growing out of the exchange of ownership on the commodity markets and the exchange of ownership of legal obligations. This relationship brings to light the real nature of a transaction evolved through centuries of struggle between debtors and creditors. The issue was that what is fair and just in the form of rights and privileges each may exercise against the other for the best interest of commercial intercourse and for the public welfare.

The function and the role of debt in a modern society were briefly described in Chapter 3. Throughout time it has been the merchant class which formed the spearhead of attack against restrictive measures in the use of credit. In final analysis it was negotiability of debts which spurred trade on to maximum velocity. In effect, it created a new species of circulating media which capitalized the future. A transaction involves the negotiation of a transfer of rights and titles which automatically form debts and creates credits. These debts are the equivalent of an economic quantity — present legal control in exchange for expected future income. Those who assume a debt incur legal duties. The legal duties are made vendible because they may either be assigned or made negotiable in the debt market.

The structural relationships involved in a transaction may be schematically shown as follows:

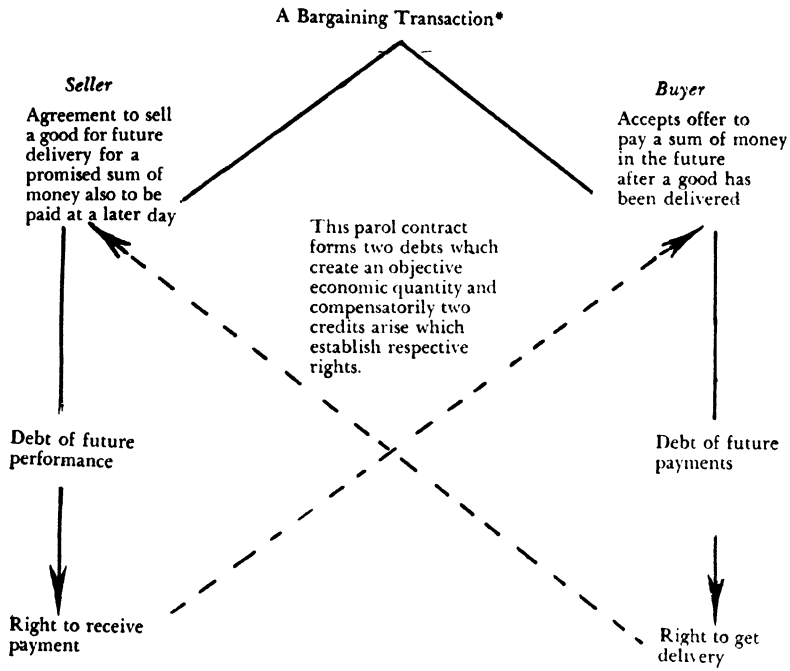

Figure 3

*This illustration describes a bilateral transfer of property rights. That is, when either party acts to conclude the agreement, the other side of the transfer is of necessity closed. A multilateral transaction is evolved by a unique device called a clearing house usually formed as a subsidiary agency of modern commodity exchanges to facilitate substitution. Then, transfers on the part of either principal to a contract are arranged without affecting the status of the other.

Other Forms of Transactions

It will be noted that in the debt market there is a lapse of time between the negotiated agreement and the consummation of the transaction. The duration of rights and duties under the contract are limited both by terms of the contract and by statutory laws. Commons distinguished three types of futures negotiations: bargaining, rationing, and managerial transactions.[6] In this era of authoritarian governments abroad and oligopolies at home the rationing and managerial transactions assume magnitudes which would recommend them for independent analysis for their effects on the markets of the world. The relationship in these transactions is one of peer to subordinate, and only three parties rather than five are all that are necessary to consummate a deal.

Corollary to the bargaining act through which persuasion, coercion, and duress are used to effect a transfer of rights or titles, there is the managerial prerogative of giving an order and expecting compliance or the rationing decree which is invoked by authorities. Those who wish to protest the latter may plead hardship and debate the relative merits of any regulation controlling distribution.

The Area of Exchangeability

Our immediate concern is that of measuring the potentials of the bargaining transaction in markets overt within the framework of a capitalistic economy. If the broad dichotomy in economic subject matter between production and marketing is granted as an accepted fact, then we may proceed to a more definitive analysis of the merchantable nature of property. Possession of economic goods can be broadly classified in three cate-

[6] Commons, John R., "Institutional Economics, Its Place in Political Economy," p. 59, The MacMillan Company, New York, 1934.

gories: corporeal, incorporeal, and intangible properties. Except for the instant present which is referred to as the zero point of time, all ownership lies to the fore and extends to infinity. With this salient point in mind, the nature of property may be made more lucid by another diagram relating the component parts of a transaction with reference to time. See Fig. 4, p. 185.

The Significance of Negotiability

Incorporeal property is represented in Figure 4 as expected income from debt payments. This form of obligation has been recognized for centuries by the merchant class but it attained a new status in the seventeenth century when debts were made negotiable. Up until the last decade of the nineteenth century, all object of future materialization were simply regarded as being incorporeal. In the gay nineties when the American Congress became conscious of the impending evils of trust, and the courts began to rationalize commercial activities, the word "liberty" as used in the fifth and fourteenth amendments of the constitution was interpreted to mean a new form of property. The courts of the land recognized transactions designed to capitalize such things as goodwill, which might be transferred from one concern to another for a price. This new economic quantity conceived in the Minnesota rate case was called intangible property to distinguish it from incorporeal property.[7]

The interpretation enlarged the freedom of individuals to bargain, to withhold, to choose opportunities, and to capitalize their reputations with reference to anticipated future earnings.

Many practitioners and not a few students of marketing categorically declare that transactions cannot

[7] See John R. Commons, "Legal Foundations of Capitalism," pp. 15, 36, referring to Chicago, Milwaukee, and St. Paul RR Co. vs. Minn., 134 U.S. 48 (1890), MacMillan Co., New York (p. 82 JRC Inst. Econ.)

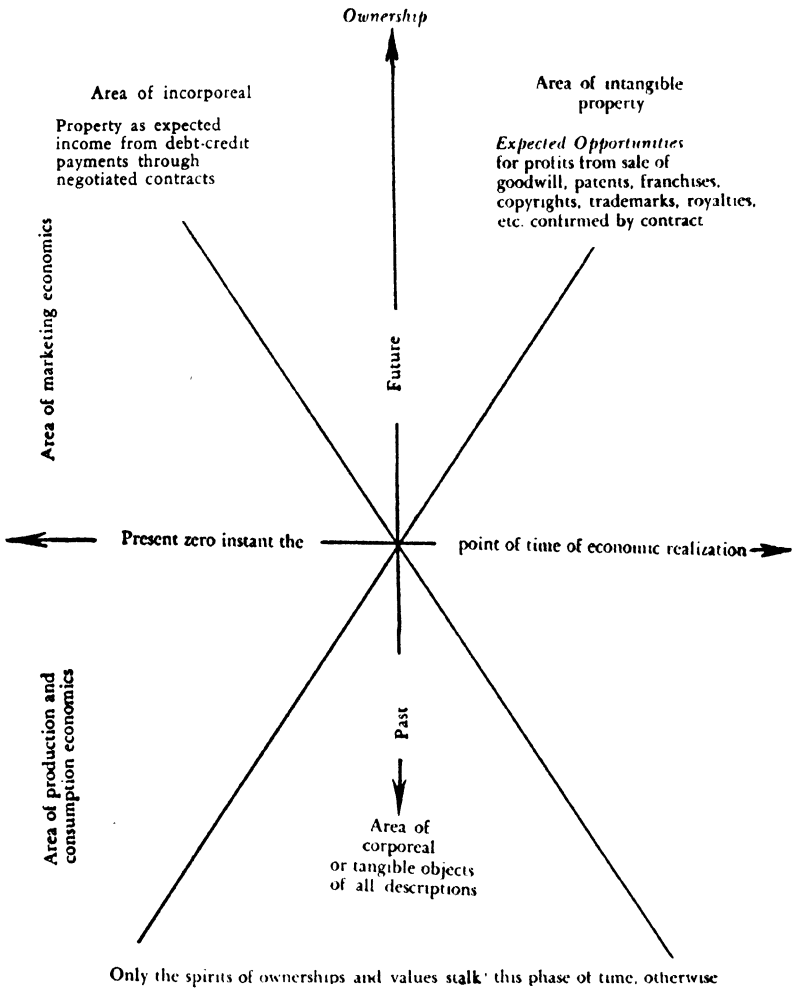
Ownership
Area of incorporeal
Property as expected income from debt-credit payments through negotiated contracts
Area of intangible property
Expected Opportunities for profits from sale of goodwill, patents, franchises, copyrights, trademarks, royalties, etc. confirmed by contract
Area of marketing economics
Future
Present zero instant the
point of time of economic realization
Area of production and consumption economics
Past
Area of corporeal or tangible objects of all descriptions
Only the spirits of ownerships and values stalk this phase of time, otherwise they have no economic existence.

Figure 4

occur independently of some physical good. The transition from a subjective predilection to an objective attitude relating to the process as of economic valuation is conceded to involve a difficult mental exercise. There are those who fail to appreciate that marketing is primarily a service and services can be rendered frequently with no outward physical manifestation. This is demonstrated in the fact that on the Chicago Board of Trade ten bushels of wheat may be sold for every bushel of actual wheat delivered. Trading on the futures markets is not predicated on actual wheat — it is based on the rights to control the ownership of potential wheat which may come into existence, but not necessarily so. Some critics of this concept of marketing go so far as to say, a transaction merely effects a change of ownership without creating in itself anything of value. This feudal notion of the function of merchants is prevalent even today among grain farmers in their attitude toward the various agencies dealing in futures. They can easily perceive the usefulness of a railroad, a miller, and an elevator operator because they understand what these agencies do in forwarding the farm product toward the consumer. The services of the risk takers in the wheat pit, however, are not clearly evident to them. Therefore, they are critical of their service and suspect as parasitic intermediaries in the industry. The wheat growers readily understand the production risks they take in the interval between sowing and harvesting, but they fail to appreciate similar services rendered by those who facilitate the transfer of ownership rights creating possession utility.

The Flow and the Lapse of Time

Another means of distiguishing incorporeal from intangible values centers in the idea of a lapse of time — the interval between two anticipated events and a flow

of time in which a succession of events may occur. This relationship is conventional in the business of finance. The contrast may be illustrated by the type of security issued for risk capital. A stockholder is induced to invest his capital in a going concern by the prospect of profits that may be realized from the succession of transactions entered into by the firm. If the enterprise is a success, the investor may gain both from dividends on stock and from capital appreciation reflected in its share values on the market. Another investor's capital is primarily attracted to the business by the anticipated income at a positive nominal rate which accrues in the interval between two dividend payment dates. He acquires bonds which may also appreciate in value on the market and provide a greater measure of security since the bondholders are given a preferred creditor's status over common stockholders in the event of bankruptcy or dissolution. Both types of investment have pragmatic significance only with reference to the future.

A parallel case can be cited applicable to an agricultural commodity again involving risk capital. A miller enters into a contract to deliver 1,000 barrels of flour some months hence to a wholesale grocer. His quotation is based normally on the present price of wheat in the spot market, but the order will be milled and delivered some time in the future. He feels competent to assume the probable risks of overhead, the costs of power, future labor, administration, and sales costs; but he is not prepared to assume the risks of price variations which may be in the months ahead quite erratic for the raw material — wheat. This risk he covers substantially by a hedge on the futures market. On the one hand, the position of the miller is analogous to the bondholder backed by the security of physical possession of the wheat or flour. If he is skilled in the management of his mill, he likely has current costs under control, and he is fairly

certain of earning a calculated margin on each unit of output. The commodity speculators, on the other hand, are in much the same position as the common stockholders. They assume a market risk in return for an anticipated profit from a succession of transactions taking a secondary position to that of the miller in the event of catastrophic changes in prices. The farmer can readily understand the position of the stockholder when he relates his risks to the ownership of his farm enterprise. He becomes dependent upon a succession of capricious events in production and marketing for anticipated profits. In this respect his position resembles that of the common stock investor. He has the option of shifting his position to one similar to that of a bondholder if he is engaged in the production of certain commodities for which a futures market exists. Then he may hedge his sales to minimize the inherent risks involved. In this case his risks are analogous to that of the milling processor.

The Quest for Security

To recapitulate briefly, marketing is an intercessory function which must precede all production and consumption in every society where property ownership rights are recognized and respected. Ownership presumes legal control, and legal control gives the individual dominion over future rights to scarce goods. Peaceful possession is usually achieved through a transaction assuming that rights and titles to ownership are vendible. Thus exchange becomes the central principle of concern to all economists who evince an interest in the related fields of marketing and the distribution of wealth.

The future is illimitable not only in space but in motion. The economic aspects of life in some respects are not separable from the great social and political movements of the times. Morse and Marconi compressed

the time element to an irreducible minimum in perfecting a means for transmitting communications. In like manner, distances from point to point on the globe have been melted down in the fiery surge of power from jet planes. These great technological sweeps bring within a lifetime events and experiences and influences which surpass the loftiest aspirations of men who "crossed the bar" only a few decades before our time. If man turns to the future from which all things flow toward him, he becomes vitally concerned with the impending events which will affect his life and his well-being.

At Valley Forge a renowned patriot penned an invidious sentence to inspirit the loyal soldiers who refused to desert a cause.[8] Each generation has its Golgotha and ours is no exception. The prospect of cataclysmic changes which may be caused by new type bombs, rocket ships, electronics, gases, and germs is awful to contemplate. They impose on us an overpowering sense of insecurity. A hazard which has ceased to be particularized. It is an inclusive danger of the total annihilation of mankind. The burden it imposes to perfect a ready defense and the means for a reluctant offense both here and abroad approximate twenty billion dollars annually. The implications of such a program affecting individual freedom are full of import in that they require taxes on the wealth we create, conscription of youth for military service, restrictions of basic freedoms, centralization of authority, and the certain end to some of our free institutions.

The Need for Social Innovators

The progress of a people in meeting these dangers to life and posterity may be judged in a large measure by their resourcefulness as innovators. Throughout the in-

[8] "These are the times that try men's souls," Thomas Paine, in "The American Crisis."

dustrial revolution in the Western World men have been outstandingly successful in perfecting machines, discovering processes, and compounding new products from the rich stores of elements found in abundance in the western hemisphere. In exploiting these newfound treasures, men have individually and collectively demonstrated a remarkable capacity for producing physical goods. The developments on the socio-economic front have been less impressive except in recent years. There is a growing realization that this phase of economic enterprise must be elevated to a level of performance comparable to the advancements in machine technology otherwise further progress in industrialization may be stymied. On an international basis the belligerent nations are technically still at war (1953) eight years after the shooting ceased because peace treaties have not been concluded. United Nations conferences are too often bedeviled by vetoes and walkouts. The institutions which the victorious nations have formed to obviate another war must await a crucial test. In the eyes of some observers they appear impotent and indecisive. The cold war is waged to test the intensity and spirit of national ideological beliefs and to evaluate the tenacity and grandeur of their objectives.

An adequate military establishment alone is not enough to guarantee security. When nations place their reliance upon great military machines, their citizens invariably surrender many of their individual freedoms because direct controls are imposed on the economy to make the military program effective. The government's allocation programs narrow the free market. It restricts the available supplies of strategic materials, costs tend to rise, and prices are regulated by decree. Rigor mortis sets in over the whole body politic.

Social organization to ease the tensions which are generated in an armament race may prove to be the

critical factor in averting disaster. Skillful diplomacy is in many cases more effective than powder and shot. It can promote a friendly feeling among nations, win their support and sympathy, and help preserve the peace. The judicious dissemination of information can allay fears and suspicion. The extension of credit and direct economic assistance is postulated on the theory that bread is more effective than bullets in quieting internal disorders and averting chaos. Such programs tend to widen markets and stimulate trade. They engender a kindred feeling among diverse peoples and create good will. This confidence in one another's national affairs will permit a freer exchange of information, and sweep aside any impervious curtains through the mutual exchanges of travelers, scholars, technicians and government representatives.

Internal Economic Activity

In the minds of many businessmen, economic security has become an anathema. They rail against its enervating effects upon initiative. Too much paternalistic coddling, they claim, will weaken the moral fiber of men and dull their faculties to cope with adversity in the event of a national catastrophy. In opposition to this view many governments have initiated social legislation to dispel the feeling of insecurity and outright fear in the event of an economic depression. The programs are conceived on a broad basis to assure men against adversity both on a collective and on an individual basis. They are made applicable to a number of situations which can arise in the course of a lifetime. Some of these remedial measures apply to unemployment, accidents, health, education, maternity and old age. In this coun-

try the widows, orphans, and other survivors are assured of future income through life insurance to the extent of 270 billion dollars. There are in addition to these major programs of security some measures of a preferential nature such as pensions, bonuses, and aids to the veterans of wars. In some states the underprivileged children receive special consideration to give them an equal opportunity in life both from the standpoint of health and training for life's work.

It is contended that these social programs add stability to an economy and in most cases return dividends on the investment in that they diminish worry and loss of efficiency on the job. The recipients tend to increase their productive capacity because surety in the future obviates the necessity of making the job last. It eliminates vicious sabotage and slowdown tactics. Improved educational facilities increase the capacity of all the people to engage in gainful pursuits. Finally the capital outlay for these various social programs is a powerful factor in sustaining purchasing power. Excess profits are drained off in the form of taxes and redistributed to those who deserve assistance by virtue of their services to their country and their community. This statement is not to be construed to mean that indolence is condoned. Precautionary measures should be taken to assure the people that only the deserving are to be rewarded with such generosity.

The Psychological Factor in Negotiating Market Values

Stability and security can be realized in a mature economy where institutional development has been well rounded out and skillfully administered through the interactions of democratic forces. The economic societies that have reached this state of perfection in combining

and coordinating its human and physical resources have been altogether too few in number. In some of the pre-capitalistic societies where self-sufficiency was maintained at a high level or where atomistic competitive influences ran rife, it is conceivable that the law of averages might smooth the course of economic affairs by counterbalancing one against the other, excesses in audacity and caution, optimism and pessimism, and sagacity and stupidity.

Our contemporary economies, however, have suffered severe convulsions from time to time because of the high degree of interdependence between rival industries and within particular fields of specialization. The business captains are more and more influenced by each other's expectations of future economic developments. It follows as a result of their propensity to interrelate operations by forming great corporations, trade associations, and cartels. They have integrated managements and unified policies in the interest of maximizing returns per unit of product output, or per unit of capital investment. In a dynamic society existing prices alone do not provide dependable criteria for future commitments; neither does the current rate of output in physical supplies furnish a reliable basis. This is true because control of the factors of production become a vested interest and demand and supply are manipulated not for the welfare of the populace or the nation, but in the interest of the business stewards and the proprietary class. Those who pyramid future rights, then, can control the factors of production. Theirs is a strategic position in determining whether or not these factors will be employed. They decide, moreover, the manner in which the factors will be combined, when they will be

utilized, and for what purpose. Specialization in money lending, control of land sites, appropriation of raw materials, and manufacturing may result in considerable higgling and bargaining among the proprietors to determine the distribution of future income. Under these circumstances it is not to be expected that the factors will always be combined in proportions which will result in the most efficient production. The seasoned business executives warily appraise contingencies and rarely launch a venture unless the outlines of success are discernible. This is one of the influences retarding recovery from a period of severe depression. When, at length, it becomes apparent that there are profits to be captured by intensifying economic activity, entrepreneurs may be induced to start the wheels of industry again and prime the markets with new goods. In nearly all business enterprises, risks and uncertainties are prevalent because there is a lapse of time between the decision to act and when the product or service is made available. Some operations require little time, and others, particularly in the round-about process of production, take months and even years to bring them to fruition. In this procedure someone must act on expectations. It may be the enterpriser, a speculator, or a potential user.

The Saga of a Basic Enterprise

On the North American continent extending from Ungava Bay to Minnesota are found scattered deposits of rich iron ore. One series of open pit ranges in the Lake Superior district alone contained more than 2 billion tons of high-grade ore. At the present rate of use, it was predicted that presently known deposits of high-

grade surface ore would be exhausted by 1965. In steel production the manufacturers must anticipate needs on a long-range basis because much capital is needed to develop facilities for mining and transporting ore as well as to build furnaces, shops, and mills in strategic locations to hold down procurement and processing costs. Spurred on by expectations of future needs, geologists from many countries have been scouring the earth's surface for new deposits. The search was not in vain, for several new deposits were discovered. In April 1947 a group of prospectors for the United States Steel Corporation found huge outcrops of iron ore on a small mountain near the Orinoco River in Venezuela 500 miles from the Gulf of Paria. Drillings on La Parida subsequently revealed that this great hill standing 2,000 feet above the surrounding savanna was a vertible mountain of iron ore containing no less than 500 million tons of high-grade ore.[9] The American company plans to invest over a billion dollars in the next 15 years to provide the necessary facilities for exploiting the ore reserves which are sufficient to supply this country's needs to the year 2000. This enormous outlay of capital is a long-time investment which might not be fulfilled were it not possible through our modern stock exchanges to break this long-term investment into short-term investments. By this modern means of financing, securities of the company may be acquired by those who have venture capital to risk in the enterprise in anticipation of a sequence of events yielding future income.

[9] LaParida has been renamed Cerro Bolivar and is held under denouncement by the U.S. Steel Corporation for the next 100 years along with 17 other adjacent area reservations containing a total ore reserve of over one billion tons.

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8

LAW OF MARKETS

UNDER the Keynesian doctrine it is within the realm of possibility for income to agglomerate without inducing a corresponding expenditure because the difference may be hoarded or reinvested. In like manner, it is possible through bank credit and savings to expend more than current income receipts. Crisis may occur before a condition of full employment has been attained and even before the effects of credit contraction or short supply are made evident by the turning point in business cycles. Economists have preoccupied themselves in a search for limiting factors, which were supposed to cause either the bottom of the valleys or the peaks of the up and down swings in the course of business activities.

The arresting effects which the "law of the markets" had upon the development of economic theory constitutes one of the most absorbing chapters in economics. The factious issues in this controversy so vital to a full understanding of transactional economics are related and interpreted in the next few pages.

The Protagonists of Market Theory

Garnier, the physiocrat, contended that it was possible to have such profusion of production that all markets would be congested with goods. This theorematic state-

ment relates primarily to agricultural commodities since land was the only economic factor, according to the physiocratic doctrine, which yielded a net surplus — *produit net* — over and above the costs of production.[1] Say challenged this idea by insisting that no general glut of markets could occur. In support of his theory he asserted that "products are given in exchange for products".[2] Substantially, this same notion of mathematical balance between demand and supply was held by Ricardo and the elder Mill.[3] Paraphrasing the law in a prefatory note to a recent publication of Say's correspondence, Harold J. Laski asserts that one-half the goods of the world are exchanged for the other half. Without qualification, this statement implies a physical quantitative relationship. Say was not entirely oblivious to the intangible elements in transactions, since he repeatedly mentions the capricious variations in prices and values that affect the ratios of exchange.[4] ". . . . In reality we do not buy articles of consumption with money, the circulating medium with which we pay for them. We must in the first instance have bought this money itself

[1] Garnier, Germain, Translation, "Wealth of the Nations" by Adam Smith, Vol. 5, pp. 290-315, Paris, 1802.

[2] Say, J. B., Traite "d economie politique", Second Edition, 1814.

[3] "No man produces but with a view to consume or sell and he never sells but with an intention to purchase some other commodity which may be useful to him or which may contribute to future production. By producing then, he necessarily becomes either the consumer of his own goods or the purchaser and consumer of the goods of some other person . . . . Productions are always bought by productions or by services; money is only the medium by which the exchange is effected."
Ricardo, David, "Principles of Political Economy", Gonner, Edition, pp. 273 and 275.
Marx emitted a caustic comment on this passage — "This is the childish babbling of a Say, but unworthy of Ricardo".*

*Marx, Karl, "Theorien Uber den Mehrwert," Vol. II, pt. 2, p. 277.

[4] Say, J. B., "Letters to Thomas Robert Malthus on Political Economy", P. V. George Harding's Bookshop Ltd., London, 1936.

by the sale of our produce .... Therefore, it is impossible for them to purchase any articles whatever to a greater amount than those they have produced, either by themselves or through the means of their capital or their land."[5] "Therefore, the total supply of products and the total demand for them must of necessity be equal, for the total demand is nothing but the whole mass of commodities which have been produced: a general congestion is consequently nothing more than absurdity."[6] As the venerable Mr. Say pondered over this great truth that he had seemingly discovered, he observed further that production precedes sales because such production immediately creates a demand for other products. "There is nothing to be got by dealing with a people that have nothing to pay."[7] As he proceeded in his argument that extended the application of the law to international commerce, he became so inbued with this fundamental truth that he exclaimed, "The theory of markets will change the whole policy of the world". As of an individual, the interest of any particular country lies in abundant production. Concomitantly other nations prosper likewise in material output so that a good basis of exchange may be established.

Pursuing his analysis further, Say recognized that the markets might be flooded with some particular commodity. He attributed such a situation to an inefficient application of the means of production or to a miscalculation of the potential demand for such a good. A glut in one commodity may be attributed to a deficit in the supply of another. These temporary inequalities in equilibrating demand and supply were of no signif-

[5] Ibid., p. 2.

[6] Op. Cit., Footnote 2.

[7] Say, J. B., "Political Economy", Book I, Chapter XV, p. 82, Translation by C. R. Prinsep, 3rd American Edition, John Griff, Philadelphia 1827.

icance in his estimation because the sum of the surpluses in any given instance must be less than the sum of the deficits. He perceived economic society to be operating in a realm of scarcity. Thus, he emphasized that no one need fear general overproduction. Moreover, he denied the essence of business crises, even though he recognized that exchange did not seem to function so well at times. He regarded these limitations as transient incidents easily eliminated by removing some of the restrictions that are imposed upon an individual's initiative to produce and exchange goods for their own selfish interests.

The Law Hobbled by too Many Assumptions

Although Say's "law of the markets" has attracted wide attention, and has been noted in countless publications, surprisingly few critics have attempted a definitive analysis of its precepts or have suggested its experimental application. It has ostensibly become the *modus operandi* nevertheless, for one type of business enterprise extant in our industrial societies — the cooperative associations that are committed to the policy of production for use.[8] A few have strafed the law as illaudable nonsense, a simple truism, or as meaningless tautology. Since this treatise is devoted to a study of the theories concerning markets and their functions, Say's pronouncements should be critically reviewed for their contribution of ideas about the evolution of markets in an early capitalistic period. In order to fully appraise Say's "law of the markets", his basic assumptions should be listed for reference as a prelude to the following pages which delve into the theoretical speculations of this eminent economist and his erudite contemporary critics.

[8] Bakken, Henry H., "Cooperation to the Finnish", Chapter 18. Mimir, Madison, Wisconsin, 1939.

LAW OF MARKETS

The original assumptions basic to Say's "law of the markets" were:

1. Consumption is coextensive with production.
2. Every transaction is consummated ultimately in barter form.
3. The time factor is not so important.
4. Money has no significance other than as an instrument or as an intermediary agent.
5. There is no concept of a normal market period, and the function of marketing is a continuous process.
6. Complete freedom of principals in both domestic and foreign trade.
7. The round-about process of production is a deterrent to trade.
8. Value created in the product at its source is not augmented by the services of middlemen.
9. Values fluctuate from time to time, but these changes create little disparity in the ratio of values between different economic goods.
10. All able bodied workers are fully employed.
11. Only things of value are intentionally produced.
12. Society is relatively static and technological changes are not abrupt.
13. The essential products are normally produced in correct proportions.
14. The more rapid the turnover of capital, the greater will be the volume of production.
15. Purchasing power crystallized in the form of money nominally cannot be dissipated in circulation.
16. The general level of intrinsic prices is a matter of indifference; it is the relationship of values one to another that is significant.
17. Complete mobility of factors.

Malthus Revises the Law

Mr. Say encountered an adverse critic in Malthus who objected to his oversimplified statement; for Malthus was of the same opinion as Garnier concerning market surpluses. He maintained that commodities are not always bartered for commodities because the greater part of commodities are directly exchanged for either productive or unproductive labor. In the interval between production and consumption, the mass of commodities may change in value in relation to the labor or money invested in them. This fluctuation would create a discrepancy between supply and demand. Say freely acknowledged that labor constituted a demand on supply, and furthermore, he admitted that even the services of capital including land might be accepted as a form of production which could be exchanged for commodities. Then Malthus observed from these modifications that Say did not fully comprehend the nature of the productive process nor the principles governing supply and demand because he went so far as to assert that the consumption of a commodity absorbs supply and thus diminishes the demand for it, while the production of a commodity proportionately increases its demand. Say's speculative labors excluded a situation in which a great increase in production could be achieved with a constant or declining number of workers because such a trend in productivity would lead unerringly to a physical output that exceeded the laborers capacity to consume. Sismondi lost patience too with Say and his theory, so he felt impelled to ask, "How is it that philosophers will not see that which is evident to every vulgar eye?" He cited the facts about world trade in the post-Napoleonic war period. There was a general glut of goods in all the markets. European goods were in excess of the demand in Italy, India, Germany, Rus-

sia, Brazil, Argentina, and Chile. Sismondi concludes, "no fact presents itself to us in a greater number of places, or under more varied shapes than the disproportion of the means of consumption with the production."

The error into which Say fell is due entirely to his false principle — that production and revenue are one and the same. The present trend in agricultural production in the Western hemisphere would no doubt have perplexed Say, even if he had overlooked the trend in the post-Napoleonic period. The overall production of agriculture in this country has increased 60 per cent between 1910 and 1945, and the production per worker has increased 100 per cent in the same period. Production has been so abundant that we could feed 50 million people in excess of our own needs with the increase in our national farm production during the decade 1937 to 1947. This large surplus is now being exported to the war-torn countries of Europe and Asia on credit. Contrary to Mr. Say's admonition, we are doing business with destitute peoples who have little to return in payment for these exports.

The author of the "law of the markets" failed to appreciate the fact that demand is always determined by value and that supply may be appraised as a physical quantity. It is the same point which Commons made in explaining the double meaning of the term marketing — use value in contradistinction to scarcity value. One is the function of efficiency, the other of scarcity.[9] Malthus pointed out that a sudden spurt in production with no corresponding increase in the number or kind of consumer wants may cause a precipitous fall in market values in apposition to an increase in use values. When this phenomenon occurs, it is difficult to retrieve the expenses of production.

[9] Commons, John R., "Institutional Economics", Chapter VIII, The MacMillan Co., New York, 1934.

Production Not Defined in the Usual Sense

Say conceded that anyone who combines the services of land, labor, and capital to manufacture or produce market items must recover the sum of the costs of production in the venture, otherwise production has been misdirected. Production, then, is not defined in the usual sense as the physical output of goods and services, but it is conceived as an operation in which market receipts must be just sufficient to recover both prime and supplementary costs. This concession of Say's almost completely destroyed the inner consistency of his law which was based on the concept of simple barter transactions and buttressed by a multitude of unreal assumptions. These transactions are now entered into an arena of scarcity values which are stirred by myriad influences and swayed by the vagaries of time and the whims of customs. In yielding ground to Malthus on the issue of use vs. exchange values, Say failed to include profits as an item of cost. In his calculation, the entrepreneur's income is apparently included simply as an opportunity wage. If the manufacturer begins with X dollars capital, and the enterprise again yields X dollars, the capital fund is considered sufficient to complete the first roundabout process of production and distribution.

". . . . For the purpose of showing the operation of industry, capital, and land, in the work of production, I personify them; and I find that each one of these persons sells his services, (which I call *productive services)* to an enterpriser who is a merchant, a manufacturer, or rather a farmer. This enterpriser having bought the services of a parcel of land, by paying a rent to the proprietor, the services of a capital by paying interest to a capitalist, and the industrious services of laborers, clerks, or agents of any kind, by paying them a salary,

consumes and annihilates all these productive services; and from this consumption, a product of a certain value emanates.

The value of the produce, provided it be equal to the costs of production, that is to say, to the price which it has been necessary to advance for all the productive services, is sufficient to pay the bills (profits) of all those who have contributed, directly or indirectly, to this production."[10]

On this point Malthus expressed apprehension. He feared a stoppage of production unless the enterprisers were assured profits over and above the direct and indirect expenses of production. Even though Say subscribed fully to the physiocratic expression, *laissez faire — laissez passer,* the battle cry of free enterprisers, he appeared to falter at critical points in accepting the full text of its creedal abstractions. Unknowingly, Say embraced one of the cardinal principles of a modified planned economy when he repudiated the necessity of those profits which Malthus regarded as indispensable.[11] Malthus looked upon profits as a reality because the accumulation of capital, flowing largely from savings, provided the means for an indolent, unproductive class in society to consume the excesses produced by the innovators. In reply to this implicit preconception of Malthus, Say believed that riches were exceedingly slow to accumulate and that what few fortunes were accumulated could serve to offset the misfortunes of others in society. Hence, there is no danger of destroying or overthrowing industry through rapid capital accumulation by a few persons.

The idea of overthrowing industry by excess pro-

[10] Op. Cit. Footnote 3, p. 13.

[11] The principle alluded to is "services at cost" or "business without profit", which is generally adhered to by the agricultural cooperative sales associations here and abroad.

duction was pursued further in the running controversy between Malthus and Say. Malthus inquired what the consequence would be if every kind of consumption were suspended for six months except that of a jail diet of bread and water? He observed that according to Say's "law of the markets", there would be accumulated a prodigious market demand. To this shaft of criticism, Say responded that the learned professor had totally mistaken the meaning of the word "accumulation". "An accumulation is not a nonconsumption, it is the substitution of a reproductive for an unproductive consumption".[13] Moreover, he had never claimed that a saved product opens a market outlet. It is the creation of a product that provides the demand for other products, whether it is used productively or unproductively.

Malthus, one of the best adverse critics among the classicists, might have pushed his inquiry into the nature of demand to a point of great usefulness as an analytical tool of political economy if he had received some encouragement and assistance from his contemporary fellow economists in England. Ricardo's unqualified acceptance of the law supported by Mill apparently provided the authoritative cover which smothered Malthus' intuitive doubts.

However, Malthus persisted in maintaining that certain classes in society render services simply by consuming without producing. Say refused to accept this hypothesis on the grounds that each non-producer limits the supply. If one does not create things, he fails to generate demand. Any interference with production which limits output, such as tax levies, directly or indirectly results in limiting demand. Even on this point, the two adversaries clashed; Malthus, on the one hand, contended it would be a misfortune if the English na-

[13] Op. Cit., Footnote 3.

tional debt were substantially reduced. The English consuls and other revenues served to support a particular class of people who Malthus believed served a useful function simply as consumers. England has always treasured its nobility, a "kept class" which fulfills a fustian function. About one-half of one per cent of the people on the island (many titled) own 40 per cent of the property in the country. Say, on the other hand, looked with favor upon the reduction of the national debt. He believed that the release of 40 million sterling funds into creditor's hands would stimulate production, activate the market, intensify the flow of goods, reduce prices, and generally improve the moral tone of society. It would assure the English people "sustenance and apparel instead of sabre cuts from the constabulary".

The Heritage of Logic

The elixir quality of Say's mental concoction filtered down through the classicists to the neo-classsicists as a sort of an intellectual heirloom. The notion which persisted was that people who acquired money by fair means or foul must also spend money in one way or another. A given change in output immediately set in motion a corresponding change in the requirements so as to absorb the newly created output. Evidence of the acceptance of this idea, either implicit or explicit, permeates the whole literature on economics down to the very present.

"Those who think so cannot have considered what it is which constitutes the means of payment for commodities. It is simply commodities. Each person's means of paying for the productions of other people consist of those which he himself possesses. All sellers are inevitably, and *ex vi termini,* buyers. Could we suddenly double the productive powers of the country, we should double the supply of commodities in every market; but

we should, by the same stroke, double the purchasing power. Everybody would bring a double demand as well as supply; everybody would be able to buy twice as much, because everyone would have twice as much to offer in exchange."[13]

A corollary idea was expounded by Marshall:

"The whole of a man's income is expended in the purchase of services and of commodities. It is indeed commonly said that a man spends some portion of his income and saves another. But it is a familiar economic axiom that a man purchases labor and commodities with that portion of his income which he saves just as much as he does with that he is said to spend. He is said to spend when he seeks to obtain present enjoyment from the services and commodities which he purchases. He is said to save when he causes the labor and the commodities which he purchases to be devoted to the production of wealth from which he expects to derive the means of enjoyment in the future."[14]

In his later works Marshall was more guarded in his statements, but the same doctrine of oneness in sales and purchases runs through his theory as it does through the theories of Pigou and Hawtry. They assumed that when output rises or falls it induced a similar rise or fall in effective demand. Market activity is, in every case, directly geared to the wheels of industry. The volume of trade rises and falls concomitantly with the volume of production from the fields and the factories.

An Evaluation of Say's Law

The import of Say's so-called "law of the markets — products are given in exchange for products" should be

[13] Mill, J. S., "Principles of Political Economy", Book III, Chapter XIV, Para. 2, pp. 557-558, Ed. by W. J. Ashley, Longmans Green and Co., London, 1921.

[14] Marshall, Alfred, "Pure Theory of Domestic Values", p. 34. London School of Economics and Political Science, Univ. of London, (1949).

appraised in the light of the long series of assumptions he used to prop up the thesis, because these assumptions mark the outside limits of its usefulness and applicability as a theoretical tool. A critical review of these assumptions at this remote point makes it appear that Say was driven to extreme measures to salvage something from the "law of the markets" which held so much promise at its inception. Taken at its face value, the aphorism is nothing more than a simple statement of the manner of barter. His retreat before the attacks of his classical contemporaries deprives it of any claim to the rank of a basic economic law which might govern such an expansive field of economic activities as our markets. Its limitations are obvious when an attempt is made to apply its precepts to modern market institutions, which deal in futures contracts, intangible services, incorporeal properties, unstable mediums of exchange, elaborate systems of financing business, savings in the form of capital reserves, and competitive and monopolistic techniques of withholding economic power from other rivals. This brainchild of Say's was primarily an observation of promise perceived in those early days of provincial produce markets ubiquitous to the town squares of an agrarian France.

In the days when Say speculated about the social affairs of mankind, he was impressed by the Malthusian theory of population. Gloom pervaded the atmosphere everywhere, and the outlook on life was rather drab. Considering the war-torn countries and the undeveloped regions of the world today, one might easily conclude that no appreciable progress has been made since the neolithic stage of culture. In these areas, the Sayian formula still applies — the sum of the surpluses is less than the sum of the deficits. In fact, the want of food, raiment, and shelter is so great it dominates the life and thought of whole nations.

At other places in this atomic age, there is a high note of optimism with each step of advancement in nuclear physics. Man, perhaps, is coming of age and perhaps he will, in his maturity, be able to banish poverty and scarcity forever simply by tapping the latent energy that is embodied in a few minute particles of material. With the aid of modern machines and power, it is conceivable that men may produce in excess of their demand. Part proof of this progress may be found in the shorter working day and the rising standard of living. Apparently, the magnitudes have been transposed in the Sayian formula so that the sum of the surpluses will exceed the sum of reasonable needs. If this hypothesis is accepted, it becomes clear that the maxim, "products are given in exchange for products" is only a partial truth. In an economy of abundance other considerations also form the basis for exchange.

The increasing use of a medium of exchange to facilitate commercial transactions in the United States in the course of one century dramatizes the transition from a barter to a money economy. In 1840 it is estimated that only 10% of the commerce was accomplished by the use of money. By 1900 the percentage jumped to 55, 1940 it reached 85, and since 1946 about 95% of all trade involved the use of various forms of money and credit instruments serving the purposes of a medium of exchange.

Tangibles and Intangibles in Exchange

Legal rights may be given in exchange for products. In contradistinction to physical goods used to effect exchange in a barter deal, it was pointed out in Chapters 1 and 7 that our most modern markets are chiefly concerned with the transfer of legal rights and titles to ownership.

Promises may be given in exchange for products. The

great bulk of our exports in this postwar period (1945-52) for the reconstruction of war-ravaged countries come under the head of indefinite promises. The debt will be repaid ostensibly with goods at some future time, if the debtor nation is capable, and if its political leaders feel such action would be good policy. This assumes, of course, that the creditors are willing to receive payments in kind for the type and form of goods visible or invisible which they chose to offer for repayment.

Good will may be given in exchange for products. In corporate America it has become a common practice to sell incorporeal or intangible properties such as good will, exclusive sales privileges, trade names, and customer lists. This may in some degree duplicate the sale of legal rights, but it is more often a transaction parallel to legal rights, since it may be concluded informally and without written evidence of the agreement. Under this same head, one may go so far as to assert that love and affection constitute a magnitude of the transaction equation, in instances where human relations are most intimate.

Unproductive labor services may command a price in the form of economic goods as Say admitted. There are many instances of mismanagement and miscalculation in a complex industrial society. If mistakes are made, they are charged up to overhead or to experience without prejudice to the wage contract with the worker.

Productive labor services given in exchange for products need no illustration since a large proportion of our working population carries home a pay envelope with periodic regularity.

Protection may be given in exchange for economic goods. This transaction has a wide range of application. It does not refer to police protection, but rather to insurance, to the screening off of difficulties and risks, and at the extreme marginal limit it involves forbearance.

Racketeers operate either in the twilight zone or in the area beyond the metes and bounds of the law. This is a familiar pattern of transactions common to large metropolitan areas that are under corrupt governments in different parts of the world.

Only a portion of one's output may be exchanged for the simplest necessities. We allude to the status of slaves, or to those who are presumably free agents but who are burdened with an unfortunate obligation from which they are unable to extricate themselves. To confirm this statement one only needs to scan the headlines of metropolitan newspapers for an illustration. At the moment this paragraph was being written the author recalled seeing a story about an unusual form of servitude common in Japan. The attractive daughters of some unfortunate Japanese families are leased out into involuntary servitude as apprentice geishas for sums ranging from 10,000 to 15,000 yen ($200 to $300). The girl continues to be a chattel until she or her friends manage in some way to repay the original sum advanced for her services. Failing this, she endures in the status of a chattel for the remainder of her natural life.[15]

Business Cycles and the Law of the Markets

Say's apothegm describing the manner of barter contains the latent power of suggestion that inspired other writers to pursue a course of inquiry into the subject of market functions: namely, the causes which generate recurrent business cycles. His belief in productivism was not shaken by Sismondi's assault nor by the succession of business crisis in the Napoleonic postwar period. He held firm to the idea that demand and supply are so closely correlated that there would never be a con-

[15] Chapman, Ralph, "Geisha Girls Still Sold", The Chicago Sun and Times, Jan. 25, p. 12, Vol. I, #17 1948.

gestion of goods on the market, if the management of our business enterprises was reasonably competent in arranging the factors of production and in anticipating market requirements.

Moreover, the long line of neo-classicists who tacitly accepted Say's doctrine were unimpressed by Marx's unqualified repudiation of the law concerning the nature of demand on the grounds of pure logic.

"Nothing could be more *absurd* than the dogma that because every sale is a purchase, and every purchase a sale, therefore, the circulation of commodities necessarily implies an equilibrium of sales and purchases. . . . No one can sell unless someone else purchases. But no one is forthwith bound to purchase because he has just sold . . . . If the split between the sale and the purchase becomes too pronounced, the intimate connection between them . . . . asserts itself by producing — a crisis."[16]

In his analysis by mathematical formula he bares the apparent paradox that total output must be the same as the total revenues, while, in particular concerns, receipts generally must exceed incomes by at least as much as the depreciation of capital. According to his line of reasoning, there is ever present the danger of disequilibrium.

Let us cite a situation selected to test the validity of the purchasing power of money assumed under Say's law — a catastrophic situation in which a nation's industrial plant is blown to pieces by aerial attack. The quantity of money in the country may not have been appreciably changed by the attack. The volume of production, however, fell precipitously. Prices under these circumstances usually become volatile since the ratio of money to goods had been drastically changed, especially

[16] Marx, Karl, "Das Kapital", Vol. I., p. 87.

if the buyers became apprehensive about the availability of supplies and the trend of future prices.[17]

Another variation of this example prevailed in the postwar period when a country was occupied by the conquerors. The output from the remnants of the industrial plants became relatively static. Strong measures were taken to control currency issues in order to hold the quantity of money constant. Agricultural production was not as seriously curtailed as industrial production, and food imports were restricted to the minimum. No effective measures were invoked to bridle the demand for food and clothing. A much larger proportion of the money flowed into the hands of the farmers than in prewar times. This was the position of the Italian farmers in 1945. Their prosperity in the postwar years exceeded even their wildest dreams of other years. They were rich in the paper currency of the realm to the extent that they were self-sufficient, but they lacked confidence in their government; consequently, they began to doubt the soundness of their money. It became more and more difficult to drain off excess purchasing power into the form of investments and in taxes.[18] Much of the pent up purchasing power in the form of paper currency was freely thrown against the limited supplies of industrial goods which were offered sparingly by the manufacturers and owners. Ration allotments at fixed prices were quickly absorbed by the long queues of customers.

[17] For a lucid explanation of the Quantity Theories of Money see Lewinski, Jan st. "Money, Credit, and Prices", Chapter III, pp. 75-79, P. S. King & Son Ltd. London 1929.

[18] There are at least two leaks in the monetary circulatory system that were ignored by Say. For centuries hard cash in some countries of Europe and Asia has vanished into hoards. Much more important, however, is the disappearance of purchasing power in a modern credit economy as repayments of bank loans. If any considerable percentages of current earnings are thus diverted into hoards or for cancellation of bank loans, the above explanation loses its validity.

The Influence of Black Markets

When the retailers' shelves became empty, the people rushed out into the black market to supplement their legal rations. Prices rose phenomenally for certain items, until the disparity between legal and illegal prices became so great that producers refused to deliver their current crops to the *consorzio agraria* at the prevailing official prices. Failure to deliver such supplies made it impossible for legitimate merchants in the towns and cities to meet ration card requirements. More and more of the supplies leaked into the black markets and less and less into the legitimate channels of trade as the prices on the restricted black markets spiraled out of control. If Say were to consider the trends in this case, he would have prognosticated that the disproportionate production in agriculture, contrasted with the curtailed output of industry, would result in increased prices and profits to industry and to the black marketeers, at the expense of agriculture in the long run. The price boom would then be underway caused primarily by too much money in circulation in relation to the volume of commodities offered for sale.[19]

Likewise, Mr. Say would conclude that the converse of a boom would occur if production became abundant in some branches of industry or agriculture while others remained normal; and no change was made in the quantity of purchasing power. An easy way to meet this situation would be to increase the quantity of money in circulation, providing that the various civil and technical obstacles of an increased issue could be surmounted.

Failing this, a temporary glut would certainly become

[19] For an extended discussion of Say's "Law of the Markets" as a point of departure in considering business cycle theories see: Neisser, Hans, "General Overproduction", Journal of Political Economy, Vol. 42, #3, pp. 433-465, University of Chicago, 1934.

a reality — not an absurdity. Prices would fall, and those industries with costs above the bulk line would suffer losses until adjustments were made to meet the exigency. General overproduction in this instance would be attributed to a monetary phenomenon. Once adjustments are made, the general level of intrinsic prices is of no significance. It is always the relationship of values one to another that is important.

The premise of underconsumption is one feature of Say's "law of the markets" that required modification in the light of Lowe's erudition. In recent years there has been a decline in the consumption of butter to the extent of about ten pounds per capita. The use of butter substitutes composed of animal fats and vegetable oils has increased. There was a scarcity of butter because milk was diverted to the manufacture of other dairy products in more critical need than butter during the war. The partial underproduction of butter was offset primarily by a greater production of oleomargarine.

Similarly in pharmacology a shift in the use of medicines has taken place during the war. Sulfanilamide has replaced stannous exide, and in place of vaccines the doctors are now prescribing penicillin. The consumption rates of these competitive items oscillate above and below a horizontal level depending mainly upon relative use values caused by an advancement in the sciences rather than by current market prices. A more complex illustration, involving a series of transactions, may be found in the demand for silk instead of nylon. Since the war with Japan, there has been an overproduction of silk in that country, and an underproduction of food crops. It is conceivable that some balance might be attained if the Japanese people would absorb their own total production of silk, but they aspire to lead the world in silk production. To this end, the commercial

organizations interested in maintaining sericulture at a high level in Japan outlined a long term plan of expanding production. The industry leaders were also prepared to bring pressure upon the Japanese government to subsidize segments of the industry which needed assistance, by establishing support prices both to the sericulturists and to certain processors. They firmly believe they have a comparative advantage in producing silk over most other countries in the world, and they consciously direct this industry in a manner to win world renown for their product. Before the Pearl Harbor attack, the United States was their principal export market, and much of the silk imported to this country was used to manufacture ladies' silk stockings.[20] In 1946 the supply exceeded the effective demand for Japanese silk on the world market and stocks flooded the warehouse facilities at Yokohama and other Nipponese ports. Even limited quantities of Japanese silk offered on the New York silk auctions saturated market demand and prices began breaking below the costs of the imports. Nylon had become the accepted substitute for silk in women's hosiery, causing a situation where the overproduction of silk was counterbalanced by an underproduction of nylon. Market distortions are attributed to two causes in this instance; technological developments in the production of substitute fibers, and the influence of a large scale monopolistic control of nylon and other synthetic materials. Both of these factors are exerting an immeasurable influence upon our markets and upon the production and distribution of some commodities in far away lands.

In these related illustrations it appears that Say's

[20] The monthly average production of stockings in the United States in 1940 in millions of pairs was: silk 43.5, nylon 3.0, and rayon and others 11.1. In 1946 it had shifted as follows: silk 2.0, nylon 29.1, and rayon and others 19.1. The preliminary figures for 1952 are: silk 0.1, nylon 56.6, and rayon and others 2.8.

thesis is tenable for competitive market items. What happens, however, if the items of consumption are complementary, such as bread and butter, coffee and cream, or cheese and crackers? A decline in the consumption of one item of the pair results in a decline in the consumption of the other. Is a decline in the consumption of such pairs fully offset by an increase in the consumption of some other foods? It is doubtful whether one could sustain this point when consumption exceeds the minimum dietary requirements of an ample standard of living; first, because substitutes tend to diminish utilization rates either for qualitative or quantitative reasons, and second, because adjustments must be made by the individual between personal valuations and the current price schedules for the substitute items of consumer goods.

Now we proceed to another illustration to make a point that modifies the law, a case which involves a vertical relationship in industry extending from the production of primary goods through capital goods to the finished consumer goods. A general decline in the demand for consumer goods may induce a retrenchment of investments in capital goods, ultimately curtailing production because the profit incentive has vanished. This sequence of effects is what might be called a chain reaction, which often extends down through the business structure to the basic industries — the mines, farms, and forests. The liquidation of the investments may be impounded in hoards or used to reduce bank indebtedness and other obligations. The deflation of the market may be prolonged and severe without the occurrence of a natural equilibrating force. If an industrial concern is vertically integrated, the same operative price structure will apply except a corrective adjustment may be made more promptly to ameliorate the recession.

9

PERFECT MARKET CONCEPTS

ANY discussion on this topic presupposes a general definition of a market in order to evaluate its state of perfection. Since there exists a wide divergence of opinion as to what constitutes a market, there is likewise no unanimity on what comprises a perfect market. This is especially true if the various concepts are considered from a historical point of view. Moreover, it raises the question as to what criteria should be used to determine the degree of perfection attained.

To the primitive people it may have simply represented a place where barter could be arranged to supply the absolute essentials for life without mortal conflict. In ancient times, a perfect market in some quarters might have been considered one in which luxury goods and implements of combat were made readily available. The medieval merchants were prone to evaluate and classify their market fairs from the standpoint of location, period and duration of time in operation, quality of goods offered, volume of trade, and the breadth of influence exerted on prices in a given area. Some of the Champaign Fairs became notable for their ruling position in the trade of particular classes of goods.[1] The

[1] For example, refer below to the time table of Champagne and Brie Fairs, page 317, Chapter 14.

Nizhni Novgorod Fair became famous as an intercontinental institution where trade was annually cleared for many basic commodities covering great expanses of territory both in Asia and in Europe.

Cournot's Definition

Among the social scientists, a French writer was one of the first to define a market, later paraphrased by Marshall in terms of an ideal situation. Cournot, initiator of the mathematical school, stated that "Economists understand by the term 'market' not any particular market place in which things are bought and sold, but the whole of any region in which buyers and sellers are in such free intercourse with one another that the prices of the same goods tend to equality easily and quickly."[2]

Cournot's conception of a market is a spacial one — a space larger than the town square, but, nevertheless an area so limited that traders can move about paying and receiving approximately the same prices at any given time.

A very similar notion is expressed by Jevons, who lived in a period when markets were undergoing great changes: "Originally a market was a public place in a town where provisions and other objects were exposed for sale; but the word has been generalized so as to mean any body of persons who are in intimate business relations and carry on extensive transactions in any commodity. A great city may contain as many markets as there are important branches of trade, and these markets may or may not be localized. The central point of a market is the public exchange mart or auction rooms, where the traders agree to meet and transact business. In London the stock market, the corn market, the coal market, the sugar market, and many others are distinctly

[2] Cournot, Augustin, "Recherches sur les Principes Mathematiques de la Theorie des Richesses," Chapter IV. 1838.

localized; in Manchester the cotton market, the cotton waste market, and others. But this distinction of locality is not necessary. The traders may be spread over a whole town or region of country, and yet make a market, if they are, by means of fairs, meetings, published price lists, the post office or otherwise, in close communication with each other."[3]

It was Cournot's definition and Jevon's description of a market which Marshall drew upon in formulating his statement of a perfect market.

The Marshallian View

"A perfect market is a district, small or large, in which there are many buyers and many sellers all so keenly on the alert and so well acquainted with one another's affairs that the price of a commodity is always practically the same for the whole of the district."[4]

"Thus the more nearly perfect a market is, the stronger is the tendency for the same price to be paid for the same thing at the same time in all parts of the market; but of course if the market is large, allowance must be made for the expense of delivering the goods to different purchasers; each of whom must be supposed to pay in addition to the market price a special charge on account of delivery."[5]

After reading Marshall's description of a perfect market, one must ponder the question — perfect for whom? The simple criteria of identical prices can be most easily conformed to by a monopoly. Does Marshall imply, then, that markets which are subject to monopolistic or oligopsonistic control are more perfect than free mar-

[3] Jevons, William Stanley, "Theory of Political Economy." The Macmillan Co., N. Y., 1888, 3rd ed.
[4] Marshall, Alfred, Principles of Economics, 8th edition, page 112, Macmillan and Co., N. Y., 1946.
[5] Ibid., page 325.

kets which may be characterized by erratic price movements? The votaries of Marshall may reply that he postulated mobility of the factors and free competition, among rational buyers and sellers fully informed and equally skilled in evaluating the supply-demand relationships. He contended further that there is one universal rule to which the demand curve usually adapts itself — "it is negatively inclined throughout the whole of its length."[6] If we explore these assumptions further other disquieting questions arise. For example, the same price for how long and where?

In a partial attempt to answer this question, Taussig conceived the "penumbra" and he takes issue with Marshall by declaring that, "the demand curve over 'short periods' . . . is necessarily inclined throughout in the same direction. It may be inclined positively, and similarly the supply curve indicating what quantities are offered for sale at different prices, does not necessarily have that constant positive inclination which is usually assumed. In the course of the higgling of the market, this in its turn may have a negative inclination."[7] Prices move through their orbits in undefinable clusters rather than along lines of precise points. Sometimes the prices of these simultaneous exchanges are profuse and cover a considerable ambit. At other times they are few in number and move in a narrow range.

As the number of futures markets increases, the greater will be the strain on the precise notions of price relationships postulated by the earlier writers. If identical prices are only momentary for a limited area, of what significance is this fact?

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[6] Ibid., page 99, footnote 2.

[7] Taussig, F. W., "Is Market Price Determinate," page 402, The Quarterly Journal of Economics, Volume XXXV, May 1921, Cambridge, Massachusetts.

Under dynamic conditions, price changes may be quite erratic and variable at the farm or the factory, but they tend to become more stable and rigid as they approach the point of ultimate utilization by virtue of having added to them a series of fixed costs and flexible middlemen's profits. Has Marshall's concept of a perfect market greater validity to the consumer than to the producer? If not, one must conclude that he visualized a stratified market price structure which would disclose the same characteristic at each major transactional point between producers and consumers. Such price phenomena may only exist for elemental products and simple goods in a relatively static economy and in situations where the demand is comparatively inelastic. A realization of this state of perfection in a market limits it to a small group of traders, dealing in one commodity at a particular place where at any given instant of time the prices are identical.

It is to be noted that Cournot and Marshall determine whether or not a market is perfect by its attainments — the negotiation of uniform prices for a given area — rather than to approach the problem by an analysis of the nature and functions of the institution performing market services.

One of our recent writers attempts to infuse new life into this point of view by giving a broader interpretation of uniform price. In addition to spacial variations manifested by differences in transportation costs, Shepherd adds two other criteria. The time factor, i.e., storage and handling costs, from one period to another while basic supply and demand conditions are substantially the same, and finally variations in grades, the form factor, including minor differences in costs of processing, as a consequence of variances in classes and kinds.[8]

[8] Shepherd, Geoffrey S., Marketing Farm Products, Appendix A, pages 399-409, Iowa State College Press, Ames, Iowa, 1947.

These differences are only a matter of degree, and do not affect the major premise.

Other Criteria of Perfection

Turning to other writers on this subject, Ely stressed freedom of individual action as a dominant factor in price making under ideal circumstances. He said, "The perfect market would be free . . . from monopoly or collusive agreements between buyers and sellers. It would be easily accessible to buyers and sellers either in person or through their brokers or authorized agents; and it would be public in the sense that all interested parties would have prompt knowledge of the prices which were being paid by others. But these conditions are ideal and are seldom satisfied."[9] In addition to the assumptions of full knowledge and complete freedom, a number of market theoreticians list two other conditions essential to a perfect market: (1) The amount of goods which each individual may offer or take shall be such a small proportion of the total supply that his dealings on the market can have no appreciable effect on price, and (2) Price shall be a sole determinant. The parties to the transaction are to remain completely indifferent to any other attributes in the transaction. A few authors go so far as to insist that the product shall also be homogeneous or capable of mutual substitution.[10]

Chamberlin added another refinement to the theory of a perfect market by drawing a distinction between pure and perfect competition. Pure competition, on the one hand, is construed as freedom from monopolistic elements. Perfection, on the other hand, is a much more inclusive conception of the attributes of a market em-

[9] Ely, Richard T., and others — "Outlines of Economics," page 174, The Macmillan Co., New York, 1930.

[10] See Boulding, Kenneth E., "Economic Analysis," page 50-51, Harper Bros., N. Y., 1941.

bracing such factors as mobility of resources, perfect knowledge, access to the market, and other pertinent considerations.[11]

Classical Premises

The seven authors quoted above are not a conclusive list of the economists who have expressed ideas about perfect markets, but the number giving attention to the topic is limited. Those who do give a nod of recognition to the idea in passing are apparently content merely to note that the concept of perfection in markets has been given consideration either by some contemporary or by one or more predecessors. The several who are on record on this subject appear to hold some notions in common.

They assume that the things transferred are invariably physical goods or services.

That the market is simply a place, a commodity, a group of persons or a combination of these — "two women and a goose make a market."

The function of marketing is an activity which directs the flow of economic goods and services into channels of use at an agreed price.

The distinctive criterion of perfection is uniformity of price for a given area.

It is implied under these premises that market perfection may be quite easily attained where conditions of exchange are favorable.

So many questions concerning the application and the effects of a perfect market remain unanswered that the limitations of the classical approach are unconcealed.

The principal limitation in the Cournot-Marshallian approach is centered in their *ingenu* idea of what constitutes a market. They were in effect ranging about in

[11] Chamberlin, Edward, "The Theory of Monopolistic Competition," Chapter II, Harvard University Press, Cambridge, Massachusetts, 1933.

an unexplored area. Their assumptions were imperfect since they were not based on, or tested by, experience. The result produced an untenable conclusion.

No Perfect Markets Exist

In Chapters 2 and 3 of this book the market is defined as a complex institution designed to facilitate the transfer of legal rights and titles to ownership in goods, services, and properties of all kinds. This form of organization has been gradually brought into existence through centuries of practical application and experience. At this stage in its evolution it is made up from several basic rights such as freedom in economic activity, property ownership, the privilege of association, etc. If the institutional interpretation of a market given above withstands the assault of the critics, then it should be quite clear what a Herculean assignment it would be to achieve a state of perfection in just one of the factors constituting a market let alone in seven or more major imprescriptible rights. Moreover, no single criterion such as price could be employed as a measure of perfection. The criteria necessary to judge the degree of perfection in a modern market would, indeed, be diverse and multifold. The possibilities inherent in exploring each of these interdependent components of a market in order to evaluate their functions in creating possession utilities opens wide a vast frontier for market research.

From this viewpoint, a certain conclusion is inescapable. No perfect markets exist. The best that can be done is to strive toward greater efficacy in performing the tasks of passing title of possession from one to another.

In the next chapter, Chapter 10, there may be detected a curious relationship existing between the just price of the scholastic and the Marshallian uniform price ostensibly connoting a perfect market.

10

JUST PRICE AND FAIR VALUE

MARKET institutions are by design formed to serve a common purpose. There are those, in every society, however, who maneuver for positions of influence or control of the markets with the hope that they may at opportune times use the centers of exchange to accomplish a selfish objective irrespective of public interests. Because avarice tempts so many persons all acts of free exchange, since time immemorial, have been subject to a general attitude of distrust in one quarter or another. This predilection arises from a universal problem of all mankind. *What is the right price or the true value of any economic good?* Is any individual, group, organization, or authority to be entrusted with economic power of such magnitude? The men who attempted to professionalize this function in ancient and medieval times were held in low esteem, and trade in general was regarded a calling of a low order. This feeling of hostility pervaded many market assemblies and the people subconsciously formed a defensive front through which they often harassed, hindered, and hamstrung all mercantile business in some degree, but more especially the dealings of strangers and foreigners. As societies became more formalized, the administrative task of regulating merchant activities was either assigned to or usurped by the church, the state or the guilds,

whichever was in ascendency at the time. Much of this resistance to an inevitable order can be attributed to the absence of technique, a faulty socio-economic, philosophy, and an incredible underestimation of the potentialities of commerce.

The Philosophical Bases for Value Determination

Every socio-economic problem of major proportions will in time become endowed with a philosophical residua. The universal enigma concerning the right price or the true value of things has incited a rich stream of thought, some of which is undoubtedly lost to us in antiquity. The lore pertaining to this subject marking the progressive stages of thought may be classified roughly into four distinctive categories. Two of these may be considered prescience dispositions, one the classical, and the last is of contemporary origin. Each category will be taken up in order and designated with a Roman numeral below.

Just Price of Pre-Christian Origin

The doctrine of "just price" had its origin in the attitude of the Greeks concerning economic matters. Aristotle's views as expressed in the fifth book of the Nicomachean Ethics were subsequently quoted often as authority by some of the early medieval philosophers. He perceived that justice could not apply to inanimate things, but it was animate which one should be concerned about. This line of reasoning focused directly on the problem of remunerating the worker for labor time expended in producing an object, and consequently the labor costs would serve as a guide in determining the relative price it should command in exchange. This insight into the problem of valuation won Aristotle many adherents in the medieval and classical schools of philosophers.

The Greeks were not without experience in the function of controlling prices and allocating the supply. Three centuries before Christianity the Athenians consumed more grain than they produced. About one-third to one-half of their requirement had to be imported from Geraestos, Pontius and other places. Stringent regulations had to be instituted to prevent speculators from cornering the grain supply. It was decreed that purchases should be limited to fifty phormi in each transaction, and the profit on a basket of grain should not exceed one obol. A commission of state officials was appointed to investigate and regulate the supply of grain. This body was empowered to inspect grain and grain foods and to control weights, measures, and prices. The penalty for violation of the measure was death and even so violations were frequent.

Just Price (Justium Pretium) Under Roman Law

The doctrine of Just Price was carried westward and incorporated in Roman law modifying its strong individualistic character. Kaulla reports that the first piece of Roman legislation setting down an equation of value may be found in (Lex Plaetoria — Circa 186 B.C.).[1] This act was designed to protect minors against fraud and merely represented the first step in a series of prohibitions protecting persons against fraud through misrepresentation and exorbitant prices. The judges were held responsible for determining the "right" value. In making this determination, the judge was expected to place himself in the position of the normal, average person. Usefulness of the object, devoid of any personal preferences, in a normal situation was to be considered for proper assessment of a fair value to all concerned.

[1] Kaulla, Rudolf, "Theory of the Just Price," p. 31, George Allen and Unwin, Ltd., London, 1940.

The opinion of the judges was supplanted later under Diocletian by rigid price regulations. One of the examples often cited in medieval literature is the rescript in the Roman code.[2] This code prohibited marked differences between the contractural price and the value of a particular product by assuring the seller of redress in all sales where the contract price amounted to less than half of the just price. The seller could cancel the sale unless the purchaser agreed to pay the full price. Later edicts were issued in which rigid price schedules were established for nearly every kind of commodity and service. At times there seemed to be little relationship between the official price and the freely negotiated market price. The penalty for violation of the price edicts was death and many of the younger generation preferred flight from industry and agriculture rather than the bureaucratic impositions governing prices and apprenticeship indentures.

I. Value Equivalence

The philosophers ask, Why do people enter into business transactions? One answer was obvious — they do not go to market to give away what they possess without receiving something in exchange. Neither do they act without restraints in the business of exchange, because goods have imposed on them a social condition which does not permit an unrestrained right of disposition. The scholastics' view of private ownership of property was one of mixed feeling. They said that property for private use was incontestably a natural right, but if someone were in dire need, the owner could not withhold it from his fellow men except where the owner was in a similar state of circumstances. In the beginning God created all things in common for all men. To withhold the right of use from one in need would deprive him of

[2] (Corpus Juris Civilis: codex IV: 44, 2.)

an original right and thus cause an injustice. The medieval private property right was in reality a permissive one that could not be interpreted to contravene the natural law. The civil was held subordinate to the natural law. An understanding of this dual function of property is essential to an insight into the scholastics' meaning of just price.

Under the doctrine of commutative justice of the middle ages no one should aspire to profit from exchange, for he would be expected to give under the principle of equivalence an amount equal to that which he received and no more or no less. The principle of value for value is akin to the biblical law, "eye for eye, tooth for tooth, hand for hand, foot for foot."[3] The possibility of gain through any form of exploitation in commercial exchange is completely ruled out. Widespread adherence to this principle of trade may explain in part why medieval industry remained retarded and the economy continued on a primitive plane. The value for value rule is one which might be most closely adhered to in a barter economy of a static state where prices are primarily established by rigid customs.

II. Buccaneer Trade

The renaissance of trade in Europe and the Mediterranean area which occurred during and following the crusades pervaded the whole medieval structure. This movement toward a money economy reemerged in the Italian cities and revived the spirit of adventure and exploitation similar to that which prevailed in an early period of the Roman empire. The pattern of trade by persons was untrammeled legally and the sky was the limit in plying their persuasive abilities in negotiating contracts of exchange. The merchants of this era entered

[3] Deuteronomy 19, 21.

into market transactions for one purpose, to line their own pockets. Their creed was to obtain something which was of greater value to them than that which they gave in exchange. "A vested interest is a marketable right to get something for nothing." — Veblen. They held the view that no individual should enter into exchange unless there were prospects for gain. Prior to the purchase or sale commitment, maximum and minimum values are established in the minds of the buyers and the sellers. If the market price falls at any point as it must, between the minimum price which the seller will accept and the maximum price which the buyer will pay, both parties gain in the transaction. The point at which the price falls between the two extreme limits will determine the extent of each participant's gain. In a few instances under this arrangement the market price may precisely coincide with either the seller's minimum price or the buyer's maximum price. In which case only one of the two parties makes a gain, the other gains nothing but neither does he lose anything since it does not fall below the minimum or rise above the maximum price at which the individual is willing to buy or sell to effect exchange. Any point beyond these extremes becomes either a seller's disutility or a buyer's surplus.

Certain market structures are created to effect the technique of buying and selling under this philosophical basis. Some of the practices common to this pattern are:

Isolated transactions. Quite often the transfers of ownership thus arranged are concluded without benefit of competitive bids and offers.

Unpublished prices. The prices agreed upon in paired transactions are generally not publicized for the benefit of other interested parties.

Collusive actions. The semi-secret manner of negotiating purchases and sales is conducive to surreptitious agreements among a few buyers or a few sellers which-

ever the case may be, resulting in oligopolic or oligoposonic situations. This attitude is reminiscent of Veblen's contrast of the merchant's pragmatic objective with that of science in which he said, "The intellectual output of wordly wisdom is a body of shrewd rules of conduct in greater part designed to take advantage of human infirmity."[4]

Obscurantism. Concealing facts or withholding essential information for the purpose of gaining a superior bargaining position among buyers and sellers is commonplace even in countries where the means for broadcasting market news are excellently developed.

Favoritism. Purchases and sales made on individually negotiated terms open the way to selective or preferential treatment relative to prices, services, and opportunities to transfer titles.

Raiding the market. This practice has acquired several colorful phrases aptly describing the action to-wit: hedge-hopping, forestalling, engrossing, picking the ripe plums, skimming the cream, and cornering the supply. The object is to effectively exclude or discourage competitors from entering the market by making it formidable or uninviting from the standpoint of profit opportunities.

Critical timing. A high degree of finesse is sometimes developed in bidding for seasonal products or specialty goods or offering them for sale to take advantage of buyers' or sellers' diffidence.

Spreading false rumors and misinformation. This conduct sometimes referred to as the "war of nerves" has an enervating effect on the whole trade body. Spurious facts concerning prices, the statistical position of supply and demand, and purported activities of rival

[4] Veblen, Thorstein — "The Place of Science in Modern Civilization," p. 19. The Viking Press, Inc., N. Y., 1919.

buyers and sellers are especially vicious because they entrap the gullible to serve the ends of the unscrupulous.

Invalid contracts. In some areas of commercial activity, formal contracts are in common use. Because of the dominance of either buyers' or sellers' representatives, these contracts undergo changes favoring the enterpriser who formulated them to the extent that the instruments become invalid for want of mutuality.

Crude pricing. Fixing market terms under this procedure is usually not desirable because the prices only represent rough approximations. In many cases prices are rounded or crudely determined in such a manner as to result in an injustice to some parties occasionally and to others repeatedly.

Under laissez-faire policy it was a common belief that all parties to a transaction should depend upon the self-restraint of each enterpriser because most men were thought to be inherently good and trustworthy in directing their own affairs for individual gain. Moreover, it was assumed that all parties to a transaction might actually realize gains therefrom, otherwise there would be no trade. This notion is still current in some quarters. When such a hypothesis is presented, however, two points should be made clear. (1) That each individual engages in trade for something of more specific value (individual evaluation) than that which he offers in exchange. The Dutch colonists are reputed to have purchased Manhattan (Long Island) from the Indians for $24.00 worth of trinkets. The law of diminishing utility produces some bizarre results when two persons or two groups of people of widely divergent cultures meet to transact business. (2) These values are not realized solely from the results of marketing. They may cut across the whole gamut of economic activity from production to consumption. The specific values of an individual are not admissible for a definitive analysis of

market operations. *The values which are significant are those established by common participation in the market* as described under III.

III. Buy Cheap and Sell Dear

Men go to market to exchange that which they possess for something of more general value than that which they give in exchange. For this proposition, there is an open admission that each trader enters the market with the avowed intention of making a gain of general value in possession utility. It was precisely this intent which the canonists condemned as unworthy and indefensible because it violated the golden rule of giving something in exchange of general value equal in amount to that received. If mankind had continued to observe the scholastics' ideal without modification, trade would have been continued on the feudal pattern, in a static state of localized barter and minimum exchange merely to accommodate communal production and use. Profits from commercial transactions were countenanced by Aquinas insofar as they represented compensation for additional labor and costs such as might be incurred in transportation and storage. Specialization in rendering services solely for the purpose of creating possession utility could not have been realized and the organization of commodity exchanges for futures trading might never have come into existence. The persistence of medieval business men prevailed over the doctrinaire principle of the schoolmen and in the face of necessity the learned monks reexamined their theories and discovered a means of reconciling their views with those of the merchants.

The view of a just price as a static norm was modified to embrace dynamic market changes by introducing a range of just prices. They had been perplexed for a long time by the fact that merchants insisted on receiving a higher price when sales were made on credit than when

sales were made for cash because time presumably was not salable since it was not a product of man's effort — only God's. This was a basic tenent of the churchmen which they were determined to defend at all costs. Retreat on this point would open the way to a transgression that was held punishable by excommunication. Antonino suggested three levels of just price ostensibly to permit charges being made consistent with the status of the individual in his society.

Several writers in the late medieval period devoted much thought to the ethical-social standards of value. Among these were Antonino, Molina, Lessius, Soto, Medina, de Lugo, and others. All conceded that the just price was not a fixed unique figure but one which had a range of lenient, moderate and rigorous degrees.

Lessius was the most explicit of these writers in listing the factors which govern subjective valuations in the judgment of prudent men. These factors may be briefly listed in the following order: abundance or scarcity, necessity or utility, labor or expenses, risks or losses, open sale or sale on request, few or many sellers and buyers, purchasing power or availability of money.

Thus, if a median price is asked in a cash sale, the merchant might be justified in demanding the maximum just price in a credit transaction,[5] provided the range was within reasonable limits. What was within reason was rather obscure, but a 10 to 15 per cent variation from the intermediate just price in the range was apparently acceptable.

The effect of recognizing different stages of fair value pulled down the barriers of the rigid socio-economic system of the middle ages and opened the whole continent of Europe to a revival of commerce and industry on an unprecedented scale.

[5] Antonino of Florence — "Summa Theologiae Moralis," Vol. II: 1, 8, 1. Venice, 1479.

From this line of reasoning may we conclude that all, or nearly all, persons who engage in market transactions may expect to realize net gains of a general value from their trading activities? The answer to this question may be most succinctly stated in a precept which for definiteness takes the form of an economic law.

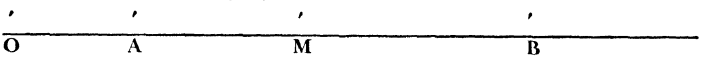
IV. One Man's Gain Is Another Man's Loss

The classical concept of mutual reciprocity in exchange is supplanted by the following rule. *In a true market transaction one man's gain is another man's loss.*[6]

[6] This rule can be mathematically demonstrated in the following way:
Symbols,

a = minimum subjective price of the seller.
b = maximum subjective price of the buyer.
c = the actual price at which the transaction is made.
t = the objective or true value at the time of the transaction, taking all factors into account with the assumption of near perfect knowledge.

If there is to be a transaction at all, b must be greater than a. It also follows that $a < m < b$. Geometrically, the following diagram is used to illustrate this proposition.

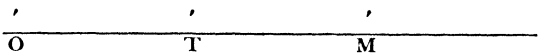


OA = a, OM = m, and OB = b. The segment AB corresponds to the bargaining area and M must lie in that segment.

In the classical argument, both buyer and seller are said to gain whenever a transaction is completed because of the relationship among the quantities a, b, and m. Thus, the buyer is said to gain b − m, the line segment MB in the diagram; and the seller is said to gain m − a, the line segment AM in the diagram.

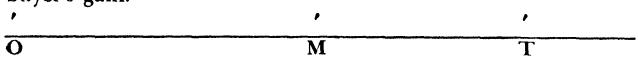
It should be noted that the true price has no influence on the classical argument.

In this line of reasoning, the true price is fundamental. The essence of this approach is that if the true price t is less than the market price m, the seller gains the difference m − t and the buyer loses the same amount.



In the diagram above OT = t, OM = m, and $t < m$. The segment TM represents the amount gained by the seller and lost by the buyer.

If $t > m$, on the other hand, the seller loses t − m, and the buyer gains t − m. In the following diagram MT represents the seller's loss and the buyer's gain.



It is impossible for both to gain or both to lose, but it is within the realm of possibility for each to break even in a static situation. It is assumed that each principal possesses equal abilities to project and administer ownership into the future. If the expectation of gain is realized by one buyer or seller it could legally have been equally realized by the other principal to the transaction.

For proof of this proposition it will be necessary to isolate a transaction performed exclusively to create possession utility. Millions of these transactions take place in the futures markets of the world. Let us assume that Mr. X has surveyed the corn market and becomes convinced that grain will rise in price in the coming months. Accordingly, he places a purchase order with his broker for 25,000 bushels at $2.00 per bushel and deposits the necessary margin. He has no intention of receiving the physical grain. He is merely concerned in securing an equity in rights to ownership in this quantity of corn. On the opposite side of the transaction Mr. Z has arrayed a series of facts which indicate in his judgment that the price of corn is going to fall. He offered through his broker to sell 25,000 bushels of corn at $2.00. Now Mr. Z is not a corn grower. He has no intention of delivering the physical product under this contract. He is also merely interested in settling the deal for a cash difference at any time in his discretion and he feels certain the difference will be in his favor. It is possible but hardly probable that he will close out the contract at a break-even point. Now both of these traders can not be right. Let us further assume that both parties maintained their position for 60 days, although this is not necessary, until it became apparent that the price of corn would rise to $2.10 per bushel in the delivery month. Mr. X stands to gain $2500.00 less commissions paid to his broker and Mr. Z will assume a loss in the same amount plus

his broker's charges. Mr. X's judgment in this instance was superior to Mr. Z's and X's gain will be Z's loss.

Such transactions have never been confined to futures markets exclusively. They have always existed and they are becoming more and more numerous in the spot markets of the world especially during periods of short supply. The "on order contracts" represent a claim to title which may be negotiable in many instances similar to future contracts. The gain realized from price differences in these market negotiations creating possession utility are just as real as any gains obtained in creating the other utilities common to the production function.

The necessity of delineating and classifying these sources of income in production and market processes should be quite evident to those engaged in market research. It is a common occurrence in business circles to meet men who have gained a reputation for their acumen as "traders" just as other men have earned the title of "production experts." Often these virtues are not joined in the same personality. In some business enterprises, the gains from efficiency in production are lost as a result of bungling market commitments. In like manner, the profits from wise negotiations in the market are dissipated by inept management of production. In business where the size and the volume of trade are great enough to justify departmentalization, the task of directing market negotiations may be divorced from the job of managing production operations. Proper accounting procedures will reveal the effectiveness of each division. If difficulties occur in either division, it will expedite the analysis and permit either the production or marketing specialist to prescribe ways and means to overcome deficiencies. In small enterprises where the functions of management are combined, it may not be a simple task to pin-point the trouble zone and it may be even more difficult to prescribe ways and means of surmounting their limitations.

Fair Value

An analysis of the components of price and the theory of value is beyond the scope of this book, but it is considered essential to make clear the role of marketing in price and and value formulation. Inherent in the philosophical basis under roman numeral IV discussed above are some elements that need further elaboration as an introduction to a relatively new concept of valuation. This discovery is of particular significance to those who are specialized in marketing. And it has not received the recognition it merits from social scientists in general.

In the late years of the 19th century, the courts of the land were confronted with a new problem of valuation as an outgrowth of the struggle between industrial giants maneuvering for positions of competitive advantage in steel, transportation, public utilities and other divisions of economic activity. In the next decade the United States Industrial Commission was holding hearings probing the activities of the financiers and the business captains of that period. These proceedings attracted the attention of one of America's foremost economists, Thorstein Veblen, who published his observations in 1904 based on the testimony gleaned by the Industrial Commission.

The startling point in this evidence was a new form of property hitherto glossed over by other economists. Andrew Carnegie occupied a position of advantage in the steel industry. He attained this strategic position by vertically integrating his firm and by achieving low cost production. He soon gained the reputation of being a relentless competitor. When he threatened to invade the tin plate segment of the industry, his rivals consolidated their holdings by forming the United States Steel Company with the backing of powerful financial interests from Wall Street. This combination resolved to

buy out Carnegie paying him the grand sum of 300 million dollars for plants and other interests reputed to be worth only 75 million dollars. The value of 75 million dollars for plant and equipment as corporeal property was comprehensive to those familiar with classical economic theory, but seemingly no scientific apparatus was at hand to explain the arresting figure of 225 million dollars. What should this sum be labelled as an economic phenomenon? Was Carnegie a ruthless Buccaneer getting something for nothing? Veblen concluded that the 225 million dollars should be called intangible property. To him it represented a form of exploitation. The new corporate colossus called the United State Steel Company was capitalized at two billion dollars. Their total resources pooled in this venture was possibly less than one billion dollars. The outstanding debt was the 300 million dollars paid Carnegie and owed to their financial backers. The balance of 700 million also represented a form of intangible property. Thus for each dollar of corporeal property in this new capital formation there was a dollar of intangible and incorporeal property created eventually to be ripened into corporeal property of one form or another.[7] Intangible property is defined as anticipated future earnings based on the vested right of exacting what the market will yield through any means within the law.

Alert citizens became concerned about these capitalistic machinations because rates, profits, and other forms of income on intangible investments were out of proportion to the service rendered or the risk involved. In a

[7] The 300 million dollar Carnegie purchase on transfer to the United States Steel Company is made up of 75 million dollars in corporeal property and 225 million dollars of incorporeal property since it became an acknowledged debt of the new firm. The 700 million dollar excess capitalization over corporeal property holdings and incorporeal debt represents intangible property to be sold to the investing public in the form of common stocks.

taxation case the assessed value of the properties owned by the Adams Express Company in the state of Ohio was raised from $23,000 to $449,337. The reason for this increase was based on the market value of its stocks and bonds, since the business was a very profitable one operating effectively without much corporeal property.

The Munn vs. Illinois case has been cited above (see Chapter 5) relative to the rights of the state to fix prices, which was construed as confiscation without due process because the state deprived the warehousemen of the right to fix their own schedule of service charges. The issue involved here again was one of the use of intangible properties.

The recognition of the existence of intangible property by the courts and the social scientists produced a rash of problems indicating the necessity for an extension in value theory. In many cases it had a direct bearing on industrial disputes, real estate settlements, assessments for tax purposes, dissolution of partnerships, and valuation for the purpose of fixing transportation and public utility rates. The courts were petitioned to settle a number of such cases and out of this experience they evolved the doctrine of reasonable or fair value.[8]

Summary

In some respects, it appears that mankind is no closer to a solution of the problem of determining values today than were the Roman jurists or the ecclesiastical fathers. Perhaps it is a case of technological advancements overstriding the means of economic analysis. The remarkable industrial development and the large scale conflicts

[8] For example refer to:
Los Angeles Gas and Electric vs Railroad Commission of California. 289 U.S. 287 (1933).
Dayton Power and Light Company vs Public Utilities Commission of Ohio. 292 U.S. 290 (1934).
Consolidated Gas vs. N. Y. 157 Fed. 849 (1907) and
Willcox vs Consolidated Gas Company. 212 U.S. 19.

within and between nations have proliferated a whole series of new problems in pricing and valuation. There has been considerable progress in the direction of a better understanding of these economic puzzles in the institutional sense, but if the strict theoretical standards of classical marginal utility analysis must be adhered to, then the range of applicability is definitely too limited for comprehensive market value analysis.

Another phase of value determination outlined above is indicative of the growing complexity of economic processes. The expanding concept of proprietary rights manifested in corporeal, incorporeal, and intangible properties increases the number of variables, and for many of these no means of measurement have yet been devised.

The business of marketing is primarily that of seeking out opportunities and projecting prices into the future. It is in essence a series of anticipated transactions that may occur any time in the future. This idea does not suggest periodicity; neither does it assure a definite quantitive or a qualitative magnitude. Consequently it simulates a flow of changes in property rights and each change is induced by prospects for gains in a successive transaction. The prices of the present are not, as some believe, an anticipated future price discounted to the present because the rate of discount is not explicit and a contract is not necessarily entered into assuring a definite price in the future. This is a risk that must be assumed by the buyers and sellers. The discounted price is actually an interest concept of price differences and as such it involves a rate of discount, a period of time, and the sum of the investment involved. The number of transactions meeting the requirements of the latter are few and far between because they represent almost certain gains, and those taking the other side of the transaction may be reluctant to absorb the losses.

Another facet of this problem in pricing and one of the most important court decisions of the century relative to market policy is the subject matter of the next chapter.

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INDUSTRY PRICING

ANOTHER round in the battle between heavy industries and the government relative to pricing policies was terminated by a six to one Supreme Court decision April 26, 1948. The final verdict was in the government's favor. For twelve years the Federal Trade Commission had pressed its suit against seventy-four cement manufacturers and the Cement Institute challenging their delivered-price formulas. The incidence of this act against the industry was precipitated by the sealed bids submitted for public works. The Navy Department received forty identical bids in the amount of $17,148.60 each. "A sample of 25,610 openings (of sealed bids) typical of those in which such bids were encountered revealed the existence of uniformity among the bids submitted on several hundred different commodities in more than 250 groups of products in seventeen major industrial classifications."[1] Again when the Secretary of the Interior called for bids on cement for the construction of Boulder Dam, "He needed 400,000 barrels of cement; but when he advertised for bids, ten leading companies all offered an identical bid of $1.29 a barrel — a price which, Secretary Ickes says, is twenty cents a barrel higher than was asked

[1] Temporary National Economic Committee Monograph #21, pp. 301-302.

sixty days ago."[2] In the call for sealed bids to furnish 6,000 barrels of cement to the United States Engineer Office in Tucumcari, New Mexico, ten cement manufacturers submitted figures which removed any vestige of doubt about the identity of their price quotations. All bids were for the same price refined to the sixth digit beyond the decimal point at $3.286854 per bbl.[3] A veritable mountain of evidence was thrown up during the three years the trial examiner sat listening to arguments pro and con. He assembled 99,000 pages of testimony and exhibits, and the attorneys filed 4,000 pages of briefs. Justice Black concluded the case with a 22,000 word statement for the majority of the High Court.

Since 1880, beginning with the steel manufacturers some major industries in the United States have been evolving price techniques which have had far-reaching effects upon their location, forms of organization, business administration, and upon trade in general. To implement their programs, they have shown remarkable ingenuity in striking implicit or explicit agreements for their edification; choosing price leading firms; pooling ideas and resources; forming industry-wide associations; and welding together formidable combines with ample resources to command respect from all quarters. These industrial firms dealing in whiskey, oil, coal, salt, tobacco, and transportation facilities aroused the public by their preemptory tactics. Senators Sherman and Edmunds were inspired to draft a restraining act that was to become a bulwark of defense against predatory business concerns. This measure became the white hope for

[2] New Republic, Vol. LXXV, #963, page 2, May 17, New York, 1933.
[3] Commission's Exhibit, 175A Sec. 157 F 2d. p. 576; F.T.C. V Cement Institute 68 Sect. 793 (p. 890).

safeguarding consumers' pocketbooks and shielding the public interest.[4]

The Sherman Anti-Trust Act

The gist of this act is expressed in its initial paragraphs:

1) Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is hereby declared to be illegal . . . .

2) Every person who shall monopolize, or attempt to monopolize or combine or conspire with any other person or persons, to monopolize any part of the trade of commerce among the several states, or with foreign nations, shall be deemed guilty of a misdemeanor . . . .[5]

This manifesto of 1890 emanated from the conviction that economic power vested in few hands must be subdued to attain an ideal state of morality in relation to material things. Years of application have not changed this fundamental conviction and the main tenets of the

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[4] Congress was given the power under Section 8 of Article I of the Constitution to regulate commerce with foreign nations, among the states and between our citizens and the indigenous tribes of Indians. This power had been invoked a number of times by a wide range of legislation affecting commerce in many ways. Some of these acts are here listed:

Interstate Commerce Act	1887
Sherman Anti-Trust Act	1890
Employers' Liability Act	1896
Hepburn Act	1906
Hours-of-Service Act	1907
Federal Trade Commission Act	1914
Clayton Anti-Trust Act	1914
Adamson Act	1916
Transportation Act	1920
Packers and Stockyards Act	1922
Grain Futures Act	1922
National Industrial Recovery Act	1933
Securities and Exchange Commission Act	1933
Robinson-Patman Act	1936

[5] 324 U.S. 836.

act have provided a model for democratizing commerce in other parts of the world.[6]

The year 1914 was marked by two historic pieces of legislation to stem monopolistic expansion. The Federal Trade Commission Act simply stated that unfair methods of competition in commerce and unfair or deceptive acts or practices in commerce are . . . . unfair.[7] The Federal Trade Commission is empowered to enforce this act and interpret its provisions with the aid of the courts. In the same year the famous Clayton Act became law which was subsequently extended by the Robinson-Patman Amendment in 1936.[8] The act now forbids sellers from discriminating between different customers by varying the price if such difference: (1) substantially diminishes competition in any commercial activity, (2) tends to create a monopoly of any interstate trade, or (3) may in any way unfavorably affect the forces of competition prevailing among sellers, buyers, or between buyers and sellers. However, if differences in costs of production, marketing and distribution are appreciable, then the seller may be justified in charging differential prices.[9] The provision of the amendment which several litigants tried vainly to invoke ostensibly recognizes price discrimination if the seller can prove that the price differences were made in good faith to match the offers of other competitors.[10]

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[6] It served, for example, as a working model for the legal staff in G.H.Q. — S.C.A.P. Tokyo, assigned the task of recasting Japanese legislation and promulgating laws to cope with the 15 entrenched feudal family firms which controlled roughly three-fourths of the financial, industrial, and commercial interests of the country.

[7] Section 5, Federal Trade Commission Act 38 Stat. 719.

[8] Section 2, Clayton Act 28 Stat. 730 as amended by the Robinson-Patman Act 49 Stat. 1526.

[9] Ibid., Section 2 (a) and also see Patman, Wright, "The Robinson-Patman Act," p. 391, Ronald Press Co., New York, 1938.

[10] Ibid., Section 2 (b).

Corporate Colossuses

One of the first issues to come before the courts was the relevancy of size of going concerns to the degree of control they exercise over business in their fields of specialization. The year that Congress passed the Sherman Anti-Trust Act, J. B. Duke brought about the merger of five leading tobacco companies by forming the American Tobacco Company. This new concern inherited 90 per cent of the cigarette business and a decade later it increased its control to embrace 95 per cent of the total output. In a like manner, it gained control of plug and smoking tobaccos, except cigars, to control at least three-fourths of the supply. The cigar industry was not mechanized, and the small handicraft concerns resisted amalgamation to the point where the American Tobacco Company never corralled more than 17 per cent of the business. The American colossus, having conquered its home market, made its bid for international control in 1901 by acquiring Ogden's Ltd., a large English concern, thus directly joining battle with the Imperial Tobacco Company. An agreement was struck between these two giants in 1902 in which each reserved for itself the home market and formed a joint corporation, the British-American Tobacco Company, to exploit the world market. Concentration and control continued to run its course within the American trust, resulting in the reformation of a new American Tobacco Company in 1904 in which 60 per cent of the stock was acquired by ten principals.[11]

Under the provisions of the Sherman Act, the Supreme Court ordered the dissolution of the trust on the

[11] United States v. American Tobacco Co., 221 U.S. 106-193. Also 191 F 371-431.

grounds that it constituted a combination in restraint of trade. The business was atomized into 14 corporations and the 29 defendants were instructed not to acquire a collective major interest in any of the new companies. The Court's strictures were at best ephemeral, for newly created oligopolies projected the spirit and techniques of the parent corporation, only on a smaller scale and with a higher degree of specialization. Profits on the capital investment were not adversely affected and criticisms of their collusive tactics both in buying raw leaf and selling finished products have continued to pour into the Department of Justice and the Federal Trade Commission.

The Court was similarly considerate in 1920 in judging the United States Steel Company's operations. It sustained the principle that "the law does not make mere size (a provocation) or the existence of unexerted power an offence."[12]

There was no inclination in this judgment to engage the giants as an evil in themselves. The court assumed the role of a referee of actions and not a judge of the inherent nature of business institutions. A quarter century of observations has apparently changed this point of view. Section 2 of the Sherman Anti-Trust Act has received a more potent interpretation as a weapon against price determination and restraint of trade. In the case of United States v. Aluminum Company of America, the Court declared that monopolies were monopolies and no qualitative distinction could be made between good and bad ones — none of them could be condoned under the law. The aluminum produced in this country prior to the war, and that large degree of control was interpreted as a monopoly because "it must sell at some price and the only price at which it could

[12] United States v. United States Steel Co., 251 U.S. 417 (1920).

sell is a price which it itself fixed. Thereafter, the power and its exercise must . . . . coalesce."[13]

Large industrial units under this ruling should be broken down into that number of concerns which at least assure some measure of competition one with the other. This line of reasoning was applied by the Supreme Court in the prosecution of the three leading manufacturers of cigarettes, June 10, 1946.

The Big Three in Cigarettes — The American, Reynolds, and Liggett and Meyers Tobacco Companies were charged with having pursued parallel lines of action in buying leaf from the growers and in selling their finished tobacco products.[14]

Their collective influence over the cigarette industry was so great it was found prejudicial to other struggling firms selling ten cent brands. This power to annihilate competitors even by an oligopoly is illegal. The mere fact that such a combination of firms exist and possess such powers is construed to be illegal even though no evidence is presented to prove conspiracy. The Yellow Cab Case (1947) and the litigation involving the motion picture industry (1948) affirm this new view of the High court.[15]

Identical Pricing on the Basing Point System

Now we come to a consideration of certain techniques of market price determination significant for their implications to market theoreticians. In 1923 the Federal Trade Commission was petitioned to bring action against the United States Steel Company by the Western Associa-

[13] United States v. Aluminum Company of America, 148 F 2nd 416, 429. pp. 811-814.
[14] American Tobacco Co. et al. v. United States, 328 U. S., 781-816.
[15] United States v. Yellow Cab Co., 332 U. S. 218-234.
Paramount Pictures, Inc. et al. v. United States 16 LW 4389.

tion of Rolled Steel Consumers. Their grievance was directed against the "Pittsburgh Plus" price quotations which they contended were discriminatory. This formula later became known as the *Single Basing Point System.* Under this method of quotation, all steel products were sold on a delivered basis. The price was fixed at one point — Pittsburgh, and freight from this point to the point of destination was added irrespective of where the steel may have been produced. The buyers were given no alternative in determining where they would take delivery of their purchases. Title passed at the point where the steel was used. Three eminent economists, Commons, Fetter, and Ripley, were chosen to advise the Federal Trade Commission in the case. Time and events have proven that their advice to the Commission was fundamentally sound. They did not counsel dissolution on the grounds of monopolistic practices as the attorneys for the prosecution urged. Instead they labeled the procedure discriminatory and suggested that the Commission require the steel companies to quote mill-net prices enabling the buyers to take delivery at point of origin, thus confining the transaction exclusively to steel products. Either buyer or seller then might remain free to negotiate a contract with transportation companies for deliveries to points of utilization.

Under the single basing point system chimerical freight charges were paid by the buyers: e.g., a manufacturer in South Chicago who purchased steel from a Gary, Indiana plant would pay freight from Pittsburgh even though the steel was actually shipped only a few miles from a Chicago mill. Furthermore, the Chicago steel may have been produced at a lower cost than the steel processed at Pittsburgh.

The Commission ordered the steel company to substitute actual sites of manufacture as basing points per-

mitting the suppliers to continue sales exclusively on a delivered basis. The action of sustaining the delivered price procedure rather than insisting on mill-net quotations implied the acceptability of a multiple basing point system.

The Glucose Cases — The Corn Products Refining Company operated two plants, one at Chicago and the other in Kansas City. Chicago was made the single basing point and all prices quoted to the buyers included freight from Chicago whether the products were shipped from Kansas City or from Chicago. If its products were sold to the neighboring cities up the rivers 75 miles at either St. Joseph or Topeka, the freight charges were those prevailing for the long Chicago haul of 500 miles not the short Kansas City haul of 65-75 miles from the point of origin. If, for some reason, shipments originated at Kansas City destined for Peoria, Illinois, the seller would absorb the difference in freight costs quoted from those actually paid since the products would be transported approximately twice the distance they would be if delivered from Chicago.

The Federal Trade Commission contended that many buyers were forced to pay "phantom freight" and thus discrimination prevailed to such a degree that it affected their ability to compete with others buying glucose products at lower prices. The United States Supreme Court decisively supported the Commission in its charges that Section 2 of the Clayton Act had been violated.[16]

The Staley Company of Decatur, Illinois, became involved in this litigation for following the price leadership of the Corn Products Refining Company. Its customers obviously paid imaginary freight bills on purchases near the company's plant. The Staley case is

[16] Corn Products Refining Company et al. v. Federal Trade Commission 324 U. S. 726; 65 Sect. 961-1970.

an interesting one for the points of defense offered supporting its actions. The defendant contended that he engaged in business at a later date than his competitor and that his prices were proper because under Section 2 (b) of the Clayton Act he had in good faith met the price of his competitor.

The Supreme Court again sustained the contentions of the Federal Trade Commission by pointing out that the price charged by Corn Products was illegal; therefore, Staley's prices were likewise illegal. The Court went on to point out that the defendant misconstrued the intent of Section 2 (b) of the Clayton Act because it only applied specifically to particular points of competition and not to an over-all situation such as that which prevails in a basing point system. The Court further observed that in most instances the defendant charged higher rather than lower prices by virtue of its competition with Corn Products. In what way may his actions in this instance be interpreted to effect good faith since his customers near the point of production were never given the advantage of their favorable location in buying the products of the industry? These decisions of April 23, 1945 swept away the underpinnings of business conducted on a single basing point plan.[17]

The Cement Case — The High Court's forbearance in going along with the idea of delivered price techniques in the Pittsburgh Plus case instead of insisting on mill-net quotations opened the door to multiple base pricing and myriad abuses.

"The Commission's findings of fact set out at great length and with painstaking detail numerous concerted activities carried on in order to make the multiple basing point system work in such way that competition

[17] Federal Trade Commission v. A. E. Staley Mfg. Co. 324 U.S. 746; 65 Sect. 971-977.

in quality, price and terms of sale of cement would be non-existent, and that uniform prices, job contracts, discounts, and terms of sale would be continuously maintained. The Commission found that many of these activities were carried on by the Cement Institute, the industry's unincorporated trade association, and that in other instances the activities were under the immediate control of groups of respondents. Among the collective methods used to accomplish these purposes, according to the findings, were: boycotts; discharge of uncooperative employees; organized opposition to the erection of new cement plants; selling cement in a recalcitrant price cutter's sales territory at a price so low that the recalcitrant was forced to adhere to the established basing-point prices; discouraging the shipment of cement by truck or barge; and preparing and distributing freight rate books which provided respondents with similar figures to use as actual or phantom freight factors, thus guaranteeing that their delivered prices (base prices plus freight factors) would be identical on all sales whether made to individual purchasers under open bids or to governmental agencies under sealed bids. These are but a few of the many activities of respondents which the Commission found to have been done in combination to reduce or destroy price competition in cement."[18]

One authority, Prof. Fetter, succinctly appraised the importance of this procedure in pricing to monopolists in the following words: "The basing-point practice is by far and away the most successful single device that large American business (producing) . . . homogeneous products has hit upon in the last 75 years."[19]

The suit against the cement companies, then, became

[18] Federal Trade Commission v. Cement Institute 68 Sect. 793 (Sec. pp. 807-808).

[19] Temporary National Economic Committee Monograph #21, page 151.

a delicate test case to determine whether any collective arrangement in pricing might infer conspiracy and collusion.

The respondents maintained that uniform prices at the mill would result in localizing purchases around each mill, thus creating a whole series of local monopolies. Transportation is such an important part of cost, it is essential to permit freight absorption in some instances and phantom freights in others in order to diffuse competition between the various producers.

Mill-net prices if imposed would lead to a relocation of many industries influenced by the quantity and the cost of moving raw materials. The ratio of raw materials used to finished goods produced in some instances approaches the spectacular.

Transportation costs are so significant, many concerns are limited in the extent of territory they can serve. It is not economical to transport cement beyond 300 miles from the mill. If a favorable location can be found within a radius of 150 to 200 miles to potential markets, it is considered advisable to build new mills. Consumers in distant areas may be starved for supplies or they may pay excessive prices for supplies in order to construct their facilities. Apropos to this point, they also anticipate the possibility of attrited price wars in areas like the Lehigh Valley for cement or Pittsburgh for steel where the industry has concentrated production facilities.

An appreciable portion of the total costs of operation are constant, thus the point at which marginal costs equal average costs is never attained because they remain unaffected by the volume of output. Local demand is less constant than that which will prevail over a wider area. To sustain operations of plant and facilities for a reasonable portion of total capacity, on one hand, is assurance against a shut down, and the management of these firms

are often willing to project sales into territories of competitors up to the point where returns barely cover either prime or marginal costs. High freight cost, on the other hand, tends to inhibit competition imprisoning the respective producers within markets narrowly confined to a central location where costs of different factors are equilibrated to the lowest aggregate total.

Objections to the Multiple Base Point System

The Court asserted that there is no essential difference between the multiple and single basing point systems because they "function in the same general manner and produce the same consequences — identity of prices and diversity of net premiums."[20] The delivered price is always identical at any particular point irrespective of any difference in freight costs to the sellers. This element of rigidity is normally possible only by charging more than actual freight to some customers in order to absorb freight costs in serving other customers.

As It Pertains to Transportation — The presumption is strong, however, that more gains were realized by the industry from phantom freight charges than were the losses assumed from freight absorption. The Federal Trade Commission in one instance estimated that unnecessary transportation costs exceeded 24 cents a barrel on cement or one-fifth of the cost of production and sales.

The system is uneconomical because it involves a considerable amount of cross-handling arising from sales promotion and from a capricious demand for the products of one mill in preference to others. When prices are tied to rail rates, it results in variable returns to the different producers which favor those who de-

[20] Federal Trade Commission v. Cement Institute 68 Supreme Court pp. 795-822 (See page 802).

termine the structural organization of the market system.

Influence Upon the Location of Industries. — Under a multiple base point system, consumption within the bounds of a base point area is hindered while incentive to expand production on the periphery is stimulated.

Non-base mills are limited in opportunities to sell supplies. They are restricted for the most part to the immediate home areas while base point mills command an unrestricted advantage over the entire base area in a sort of a "heads I win, tails you lose" proposition.

It Restricts Access to Markets — In the heavy industries, freight costs comprise a large part of the total delivered price. When delivered prices are arbitrarily quoted to customers, it deprives them of opportunities to bargain with other sellers of transportation and thus occludes them from particular markets to which they should have access. Every railway station on the map is considered as a separate and distinct market by the sellers under the base-point system. This peremptory design to create fictitious markets dilutes competition and shatters the collective forces of demand.

Equal access to natural markets is impeded in innumerable ways by an oligopoly to retain control over distribution and minimize buyers price determination.

Its Effects on the Economy — The pattern of distribution prevailing under the base-point system tends to retard the relocation of plants to areas of greatest comparative advantage.

The system induces rigidity in the price structure and retards value changes to conform to current economic conditions.

Industry leadership is vitiated by the drive for profits, and the debasement results in supplanting objectives of economic efficiency and motives of human service.

The base system increases the costs of marketing by

substituting promotional advertising and other costly sales efforts for competitive pricing.

The problem of administrative regulation is made complex, and in some instances the costs of social control become burdensome.

Court Decisions Reveal Flaws in the System

The Court sustained the Federal Trade Commission finding the defendants guilty of violating Section 5 of the Federal Trade Commission Act by engaging in a conspiracy to restrict competition among themselves. The Court further held that the *"existence of a combination (is not) an indispensable ingredient of an unfair method of competition under the Federal Trade Commission Act."*[21] The High Court also found that the cement manufacturers had violated section 2 (b) of the Clayton Act because sales under the multiple basing point delivered-price plan resulted in unfair competition among buyers of cement. The defendants denied this charge claiming their prices were *just* and were quoted in good faith. The Court, however, turned to the procedure established in the Glucose cases declaring their basing point prices illegal and unauthorized under the good faith clause.[22]

Another fault was found in the multiple basing point price system 16 days later by the Seventh Circuit Court of Appeals in an action against 14 manufacturers of rigid steel conduits. Here the Court went so far as to inhibit individual action stemming from an implicit collective understanding. "Each conduit seller knows that each of the other sellers is using the basing point formula; each knows that by using it he will be able to quote identical delivered prices and thus present a condition of matched prices under which purchasers are

[21] Ibid., page 820.

[22] Ibid., pp. 814-815.

isolated and deprived of choice among sellers so far as price advantage is concerned. Each seller must systematically increase or decrease his mill-net price for customers at numerous destinations in order to match the delivered prices of his competitors. Each seller consciously intends not to attempt the exclusion of any competition from his natural freight advantage territory by reducing the price, and in effect invites the others to share the available business at matched prices in his natural market in return for a reciprocal invitation."[23]

The Postage Stamp Price System

Under this system all concerns may quote identical delivered prices to any and all points in the country. In effect, this system can in no way be distinguished from zone pricing and it appears vulnerable to attack on the same grounds as those discovered by the Seventh Circuit Court of Appeals in the crepe paper case.[24]

Up to this time the Court has never ruled in a case concerning the postage stamp practice of pricing. It is the view of some critics that the Court will discover no grounds for convicting a single monopoly using this plan of pricing since the whole United States market will constitute one large zone. There will be no boundaries between customers where price differentials will prevail within the country: therefore, no evidence of discrimination can be established.

For the following reasons it seems to this writer that the postage stamp system of pricing by a monopoly is as vulnerable as other delivered prices charged by duopolies, oligopolies and associated sellers.

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[23] *C.C.A.* 7 (Kerner, C. J.) Triangle Conduit and Cable Co., Inc. v. Federal Trade Commission, May 12, 1948 16 LW pp. 2566-2567.

[24] Fort Howard Paper Co. et al. v. Federal Trade Commission, 156 F (2d) 899, 1946.

The single monopoly which quotes a postage stamp price may in effect be a multi-unit organization closely resembling an industry adhering to the single basing-point system. Its branch plants and offices might be scattered over a wide geographical area and the unitary price quoted might be established at the point yielding the highest average price for all sales made throughout the country. In this connection, there may be no freight absorption because the minimum quotation could conceivably be identical with the marginal cost item. The margin of profit in such an instance would tend to increase directly as the distance decreases from point of delivery, other things being equal. In this situation the single monopoly could use its profits from fictitious freights to dissuade, bribe, and intimidate potential competitors from entering the area of commerce against the entrenched and vested interest. Agreement among individuals within a corporate structure for gleaning unearned increments would seem to be as much a conspiracy against the public interest as if they were participants in separate corporations. Their acts can be just as arbitrary and inconsiderate of the customers' welfare in either situation.

A single monopoly quoting uniform delivered prices for the entire country assumes not only the power to sell a non-competitive product which it produces or possesses, but it arbitrarily usurps the right to sell a transportation service rendered by other agencies. This tie-in sale deprives the buyers of the option of entering the transportation market to negotiate the terms of the contract for services where alternative facilities and variable rates may prevail.

In a conventional competitive market situation the comparative advantage of location diminishes in progressive gradations as the distance increases from the point of distribution. The total effect of a flat rate pre-

vailing under the postage stamp system of pricing would be to completely eliminate any benefits arising from spatial consideration excepting the time factor. It would constitute schematic discrimination administered in homeopathic doses as the distances increased from centers of distribution. Theoretically, these differences could not be appreciable between customers serving a common community; but the principle of discrimination is invoked and liability should not be tempered by the magnitude of the offense in any given place of business.

Finally, it is probable that the seller will find no appropriate shelter under the good faith clause in Section 2 (b) of the Clayton Act, inasmuch as good and bad monopolies are not distinguishable in the eyes of the law, and the flat price may constitute prima facie evidence proving that no attempt was made to pass on to the buyer the natural advantage he possesses by virtue of his proximity to supply.

Mill-Net Prices

Under the circumstances mill-net prices still appear to possess the largest measure of justness in a highly competitive capitalistic society. Producers may independently make deliveries on other terms than on a f.o.b. basis. They may, for pricing purposes, zone the sales areas, stipulate rates for their goods on a C.I.F. basis, or name flat prices common to all points in the country. The established commercial institutions which have temporarily escaped the vicissitudes of a dynamic order by formulating various ingenious devices to shelter and nurture their fragile enterprises are being forced into the open fray by a series of epochal decisions. Respite from these court opinions may come from new policy-determining legislation or from more reassuring progress in litigation.

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PART II

HISTORICAL ORIGINS

12

PRIMITIVE AND TRIBAL TRADE

THE practice of gift giving — The intimate and magnanimous impulses which prompted gift giving among the primitive people everywhere demonstrated the advantages to be gained from the multiple uses of possessions. It was the first form of transfer of property rights to emerge, however ephemeral it may have been. The chief incentive for passing economic goods from hand to hand was to placate some spirit or to gloss the ego of some earthly superior. The need for a formal institution to effect exchanges did not become apparent, though, within the confines of tribal communal life because intimate association with one another was required for survival, as well as for social amenities. Simple properties, with few exceptions, were universally regarded as being held in common. Gradually, the savages extended the practice of gift giving to a wider circle of friendly persons, even exceeding the metes and bounds of their own tribal territories. When this occurred, the attitude of the recipient was generally characterized by an air of utter indifference; for it was considered indecorous to manifest any interest in the gift or to covet possession. In a like manner, the giver may haughtily present the gift with a mien of detachment by casting it at the receiver's feet or

brusquely forcing it into the hands of some lowly person acting as a servant of the beneficiary.*

Silent Trade

It is theorized that some bold members of the tribe proceeded under cover of darkness to a selected place on a recognized boundary of a neighboring tribe's territory. Here, they laid down some gifts, conscious that their offerings soon would be detected by vigilant members of the rival tribe. The givers retired to the background and waited. The neighboring tribesmen, not inured to acting rashly, guardedly took precautions against trickery by approaching the boundary at nightfall to investigate and carry away the goods offered by their untrustworthy neighbors.

Now, it must have been obvious to the beneficiaries of such a kind act that their neighboring tribesmen were not altogether altruistic in their motives, especially, if there had been belligerent acts in the past. From their experience in exchanging gifts intratribally it was relatively easy to conclude that such generosity could not go unrewarded. Consequently, on some future date, the favor was reciprocated by placing an assortment of things on the border which they believed would be treasured by their neighbors. A judicious selection of the return gift presumably would encourage further exchanges in a similar manner.

Gifts ceremonialized — Superstitious inhibitions to such exchanges of gifts were not uncommon because most goods were thought to retain some trace of the personality of the giver. Thus, it became imperative to exchange gifts only with persons whose intentions were not evil. Otherwise, the benefactor might accept some-

*Malinowski, Bronislaw, "Argonauts of the Western Pacific" Chapter VI, George Routledge & sons, Ltd., London and E. P. Dutton Co., New York, 1932.

thing which had been hexed. Such an article would form the connecting link between the donor and recipient, resulting in death to the latter through sorcery. The savages invented a means of overcoming their qualms by resorting to elaborate ritualistic ceremonies to immunize the recipients against the transmission of inherent evils. This innovation permitted exchanges to go on with the aid of "medicine men". The inconvenience of ceremonializing each gift exchange with enemies and capricious strangers emphasized its inefficiency as a means of trading. In the Northeastern Transvaal, a malarial sub-mountainous area only recently penetrated by sociological explorers, the Lovedu tribe complete four out of every five exchanges of goods by ritualistic celebrations.[1] In some instances the aborigines circumvented this hazard by shifting the function of bartering to an intermediary class of persons, an individual, or a tribe.[2] A legend was current that these specialists in bartering were sacrosanct beings through whom no sorcery could be transmitted. The intermediaries for the Lhota Naga of Assam might expose themselves to danger, but the ultimate consumers could acquire their incidental needs without peril. The trade between people of Tibet and Nepal thus conducted formed a hereditary caste of middlemen.

The Origin of Barter

In the long run, while experimental gift exchanges had their distinct advantages, there arose a desire to improve on this technique. By one means or another, information would be conveyed to the neighboring tribe admonishing them not to carry away goods immediately

[1] Krige, Eileen Jensen, "Economics of Exchange in a Primitive Society". African Journal of Economics, Vol. 9 No. 1, Pp. 1-21, March, 1941.

[2] The Kulan, as a host tribe, acted as intermediaries in negotiating trade between the Sinaketans, the Boyawas, and the Dabus.

which might be placed at the boundary. Instead, they should, in a reasonable time, match the offerings with an equivalent amount of goods placed in a pile opposite the one presented. When the goods from both tribes were properly paired, the primitives making the initial proffer would advance to the grounds and critically examine the goods available for exchange. If they were satisfied with the kind, amount, and quality, they would take what was offered consummating the transaction. If the amount laid down on the line by the neighboring tribe was not sufficient in kind and quality, the tribesmen would simply remove their own offerings initially placed at the boundary. An extension or refinement upon the system of pairing transactions was evolved later as a step toward a barter transaction. No goods would be taken up by either side until the quantity and variety set in apposition was considered sufficient to consummate the exchange.

The Formalization of a Market Institution

When the primitives became conscious of the advantages to be gained in exchanging goods from their experiences in gift giving, they contrived ways and means to enter into direct barter. Mutual trust and friendliness developed. At this stage in the social and economic development of the tribes, they also perceived the enormous advantage of personal contact and the art of persuasion in consummating their barter transactions. It is at this point, then, that we have the first formalization of a market and the market place began to be institutionalized. The mark or boundary became a neutral area even though the act of bartering was done by men armed to the teeth prepared for any contingency.

A seacoast people, the Jukum tribe barter with the Munchis. They offer fish and grain in exchange for skins and meats. This whole business affair is conducted in an atmosphere surcharged with fear. The Jukums

are armed with spears and they sit in their canoes ready to paddle away, while the Munchis armed with clubs stand alerted for a quick withdrawal into the bush at the first sign of trouble.

For a long time, the act of bartering was incidental to the meeting of primitives wherever their paths crossed. The acquisition of goods through barter resulted in an increasing demand on the part of the primitive for more goods, not only from fellow tribesmen but from neighboring peoples, both friendly and hostile. Their contacts were not left to chance. They were prearranged as to time and place. Eventually, the gods of the primitive peoples were given a definite function in making hallow the grounds on which exchanges took place. It was their duty to protect and to sanctify the grounds, transforming it into a neutral territory free from conflict. Not infrequently, open conflict broke out among these benighted souls seriously disrupting their spasmodic interchanges of goods, but necessity generally served to heal these breaches so trade went on. It is a curious fact that these natives, however antisocial they may have been at the outset, soon recognized the principles of law and order as basic to exchange.

The primitive trade areas of today are centered in some of the South Pacific Islands, Indonesia, West Africa, and Central America. Recent ethnological studies reveal distinct stages of economic development among different racial groups in these zones. These variations in advancement are attributed primarily to their aptitude in perfecting market techniques. This point is clearly illustrated by contrasting the Polynesian and Melanesian economic systems. "Both peoples live in an island world, with fishing and crabbing as occupations on the beach, and in both areas the same agricultural products are grown on the land. Both depend

primarily upon agriculture and fishing for a livelihood.'"[3] The Polynesian people, on the one hand, tend to stress self-sufficiency in preference to dependence upon trade. They minimize the functions of exchange, and they transfer goods from one to another in a most informal manner. "For the most part every household is self-supporting, and for special skills such as house building or canoe making, certain highly honored men within each community take the major responsibility. Each province or small island is almost entirely self-supporting, and maintains its own art style. . . . Yet the Polynesian culture was in many respects more elaborate and integrated than the Melanesian. Political units were larger; the same language was spoken over wide areas; caste existed. But the style of economic life was different. In Polynesia, a chief wishing to give a feast levied certain contributions upon all his subjects."[4] On the other hand, the passion for trade in Melanesia transcends all ordinary measures. ". . . One Melanesian community after another depends upon exchange, daily markets in which fish are exchanged for taro, lime for betel nuts, sea shells for manufactured products, pots for sago, coconuts for fish, stone celts for netted bags, wooden plates for pots, and even sea water (salt) for fresh water. . . . A community wishing to give a feast made trade arrangements with neighboring communities."[5]

No self respecting native woman in Bali would forego the pleasure of attending the market, sometimes several miles distant, to purchase the selfsame item she might have readily obtained from her next-door neighbor, by informal barter.

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[3] Findlay Mackenzie, ed., "Planned Society Yesterday, Today, Tomorrow," (Copyright, 1937, by Prentice-Hall, Inc., New York), "Primitive Society," Margaret Mead, p. 14. Reprinted by permission of the publisher.
[4] Ibid, pp. 14-15.
[5] Ibid, pp. 14-15.

"One (Polynesia) was a stratified society which regarded the problem of economic sufficiency as solved by the presence of — skilled persons within the community; the other (Melanesia) was a localized, unstratified society which depended upon a vast trade network to supply even the essential tools and utensils of life."[6]

Coercive Barter

In the hot and humid climate of the equatorial belt, the natives live precariously close to the margin. Most of them have evolved some system of trade which partially utilizes a medium of exchange, but they prefer to barter for their daily necessities. Mead reports that some tribes in the New Guinea area only use native currency for about one-fourth of their transactions. There is some limited use of credit extension which usually nets the creditor a lucrative return in kind. The urgency of their needs, however, demands an exchange of products for products. Moreover, this exchange is restricted to an exchange of a specific product for another specific product. "The Usiai wants fish, he can never get enough fish, his children at home are hungry. If he sells his day's load of taro for dogs' teeth, he must go home empty handed, unless he can buy fish with the dogs' teeth. But all the fishermen have come for taro or sago, or betel nuts, or bark fiber."[7] Even though barter may be considered primitive and crude as a method of exchange, it can actually be the most effective means of securing vital necessities where there is an acute scarcity of goods. "The need for proteins by the land people, of carbohydrates by the sea people, is far more pressing than either's need for money, which

[6] Ibid, p. 15.
[7] Mead, Margaret, "Melanesian Middlemen", Natural History, Volume XXX, No. 2, pp. 123-127, March-April 1930.

will command some vague, less defined good in the future. Everyone is close to the subsistence level for food and so food is bartered against food".[8]

The coercive barter transaction is clearly illustrated in another type of primitive exchange. "While the land people grow the betel nut and the pepper leaf, the sea people burn and refine the coral lime with which the betel and pepper leaf are chewed. In the market the same sized fish will command ten taro or forty betel nut. But a cup of lime commands eighty betel nut, but only four taro. Betel chewing need is matched against betel chewing need to coerce the sea people into providing enough lime for the land people."[9]

In another citation, Mead both appraises and reveals the resultant effects upon the welfare of the two modes of life. "The Melanesians had a far greater variety of material things than the Polynesians. They had pottery, whereas the Polynesians cooked in earth ovens; they had bows and arrows as well as spears and clubs. They depended upon the inventiveness and industry of many small communities instead of upon the development of an adequate but locally restricted self-subsistent style of life. And these two ways of life, in which people make what they need for themselves, or reluctantly make more than they need of one object in order to obtain what they need of some other object, are not confined to the primitive level, nor are they, in as many instances as we usually think, dependent upon natural resources and the development of machine civilization. They are primarily a contrast in values, in attitudes toward life, in which one system snatches greedily at the diversity and at the products of its neighbor, while the other aims at a dignified self-sufficiency. Whenever, in the course of laying down an economic program, a theorist insists

[8] Ibid, p. 127.
[9] Ibid, p. 127.

that one approach, rather than the other, is inevitable in certain conditions of economic life, it is pertinent to recall this contrast."[10]

In passing, it must be noted, also, that barter is not restricted alone to the primitive people. It is resorted to in the most advanced nations of the world in calamitous times, such as during periods of war, and depressions, or following in the wake of some natural catastrophe as an earthquake. In postwar periods when governments totter, currencies become debased, and industries deteriorate, people fall back upon the elemental basis of trade by bartering things for things. If the disaster is great, men and nations will limit their trading to coercive barter; Polish coal for Lofoten fish, and Burmese rice for Japanese cloth. Internal postwar trade commanded Kaffir for kimonos, cigarettes for cameras, chocolates for cameos, and sugar for Samurai swords.

African Tribal Markets

The pattern of market organization in North Africa vividly illustrates its inextensile status. Socio-economic growth crystallized in this corner of the continent before the Christian era — long before medieval fairs flourished in Europe, and it has remained down through the years a relatively impenetrable region to alien ideas of progress. The market sites along the Barbary coast and extending inland across Algeria and Morocco number in the thousands. Fogg reported in 1938 as many as 109 tribal markets in the Spanish zone of Morocco alone.[11] From a plane one may see an intricate network of roads and trails extending out of Arab villages or enclosures and converging on some centrally located olive grove, palmetto patch, or oasis situated in the open country. These are the Islamic market sites. For-

[10] Op. cit. p. 16, Mead (Planned Society)

[11] Fogg, Walter, "A Tribal Market in the Spanish Zone of Morocco", Africa Vol. XI, No. 4 pp. 428-445, 1938.

merly they were merely well trampled fallow acres occupied only on market days. Now, in the post-protectorate era, the market sites may be surrounded by a fence or wall and provided with a few administration buildings and shelters.

These market sites are usually situated in the open country within a few hours travel time from their settlements. Their proximity permits the local residents a few hours midday trading and time to travel to and from these centers of activity between dawn and darkness. Like the religious bazaars of early medieval Europe, the Moslem's market is an inclusive institution of many functions.

The Market as a Neutral Zone

In common with its European counterpart, it was first of all a sanctuary in pre-protectorate days where an individual could seek refuge and remain inviolate against the vindictive retaliations of his enemies and the judicial verdicts of the elders under the law of the land as long as he remained within its confines. In these consecrated compounds where violence in any form was sacrilegious, contentious antagonists might meet to negotiate the terms for extirpating their crimes. The tribal markets were never without their complement of judges, counsels, and scribes to facilitate legal and administrative functions. Since these market places are considered sacrosanct, they are usually identified with some patron saint or diety and thus constitute a shrine for worship and a place to offer sacrifices. In this conjunction the holy men congregate at the markets to practice their magic and placate numerous evil spirits which are thought to be inordinately fond of frequenting the same environs.

The Area as a Social and Service Center

Life quickens perceptibly in the community when market days roll around, because they are generally

crowded with social events. Families are reunited periodically at the market. Loves, hatreds, and intrigues are revived, marriage agreements entered into, and devotion to some cause or principle rekindled in the presence of the tribal saint. The visiting tradesmen import news from other nearby communities and from the far corners of the world. News items are disseminated about the market by criers. Important public announcements are made by officials and gossip flies about freely among these voluble folk. Perhaps, the climax in the day's social activities is reached when these dwellers of the arid plains and hills are being amused in sundry ways by snake charmers, magicians, acrobats, and dancers.

This communal enterprise is cherished also for the varied services it offers to make life more abundant and living more congenial. The Arab may get his shoes and sandals repaired, his head shaved, whiskers trimmed, machines repaired, and his horses shod. If the patron feels the need for rejuvenation, his barber specializes in blood-letting and leech tending. His barren wife may consult the witch doctor to become fecund. The charm writers and the magic doctors ply their humbug with a range of accessories from live hoopoes to hedgehog gut.

Market Circuits

One market day per week is usually sufficient to clear the trade for most communities or districts. Through custom, each local tribal market is assigned a particular day of the week to avoid conflict in timing with neighboring markets.[12] In the French Sudan, inhabited by the Lobi tribes, markets are numerous. There is one market for every 3700 persons, but attendance on any given day seldom exceeds 500 and gatherings of 1000

[12] Ibid, p. 439. Refer to illustration. (See p. 310).

are rare.[13]. The configuration of each weekly circuit of markets is likely to assume an irregular pattern in conforming to custom or historical precedence, conditioned to some extent by topography, roads, and distances from the home base of itinerant merchants. These market constellations contain certain bright points of trade which may form a major grouping of markets superimposed upon a series of the weekly or lesser market systems. The greater distances between these points require more time for the traveling merchants to make the rounds, thus they form the basis for a group of monthly or other periodic markets. In a like manner, a third system of seasonal markets might conceivably be formed. As a matter of fact, all tribal markets reflect a tendency toward seasonality in volume of trade, attendance, and the commodities offered for sale.[14] Thriving daily markets called medinahs are found in all metropolitan areas within this region of Africa, and in some respects they resemble the tribal markets in mode of trading, internal organization, and heterogeneity of functions.

The selling of local produce, poultry, and dairy products, and handicraft items is commonly assigned to the women folk while the men conduct most of the commerce in machines, horses, fibers, fabrics, and nearly all imports such as spices, condiments and exotics. There is no sex differentiation in the labor of selling certain items where men and women produce commodities by joint effort, such as charcoal, grain, fruits, rope, honey, and wax. Some degree of specialization among the tradesmen is also discernible on the basis of births, crafts, and place of residence. The most notable example in this instance is the Jews. They characteristically engage in money changing, converting French francs,

[13] Herskovits, Melville J., "The Economic Life of Primitive Peoples" p. 190, Alfred A. Knopf, New York — London 1940.
[14] Op. cit., p. 440, Fogg. Refer to chart.

Spanish pesetas, and native currencies from one media to the other, a function which is forbidden to the Mussulmen on religious grounds. The Jews may also deal in imported cloths, hardware, footwear, and hides. Where they render services, they are often paid their wages in kind, and in some regions they are not free to move about without great personal risk, except under the protection of some influential native.

Extrinsic Values of Tribal Trade

Tribal markets are characterized by their close knit socio-politico-economic relationships. They are as much a social event, gravid with political significance, as they are affairs of commerce. Prices are influenced by socially accepted standards modified by labor effort in production, e.g., a basket, pot, or pan may be customarily exchanged for the amount of grain it will hold. The generosity of the one offering grain in exchange for the container is put to the test by the extent to which the vessel is heaped. Doling out this quantity generally draws out much good natured banter. The Moslems are inclined to display a marked attitude of indifference toward the things they offer for sale which tends to give social significance to the bargain. Prices are often higher when it rains than when the sun shines to reflect the added discomfort of attending markets on such days. The profit motive in domestic transactions is obscured by the interplay of non-economic factors, but trade with strangers may be suffused with deception and avarice giving full rein to their passion for profits.

Where differences arise in determining a just price, an official arbiter may be called on to settle the issue. In some instances the chiefs of the markets such as in the Ngoni tribe may even impose administrative pricing to stimulate trade and maximize distribution. Market authority of this magnitude is justified on the grounds

that it will equalize consumption between areas of production as well as to lavish the indigent tribesmen with a variety of foodstuffs to enrich their native diets and make them more palatable.

Markets of Central America

We have in recent year learned much about the early civilizations that flourished in the neighboring states to the south. The sciences which revel in the past — archaeology, anthropology, and anthroponomy, have announced many new discoveries from their diggings in the ruins south of the border. Distinctive objects of art and utility have been found in a range of territory extending from the Pueblo villages of Arizona to deposits in Yucatan. Some examples may be cited, such as pieces of pottery of cholula design, vessels made from El Salvador clay, and copper bells shaped in Mexico Valley. This wide distribution of handicraft items attests the extent of economic intercourse that must have prevailed between the Maya and Aztec people and their predecessors.

To these indigenous Americans every market day was a social event of great import. Like the Arabs, they made the occasion one of worship, trade, and disputation. A round of markets held on successive days of the week was a familiar pattern. At least once or twice a year, a feast was given in honor of a patron diety and a great market fair was held attracting many merchants and a multitude of people. There was a distinguished merchant class which possessed its own emblem, staff, and diety. "Yacatecuhtli was depicted as a merchant traveling with staff in hand. He was clothed in a blue shoulder cape and wore gold ear plugs. His face was painted red and black, and in his free hand he carried a yellow and blue shield."[15] Certain market areas were

[15] Thompson, J. Eric, "Mexico Before Cortez", p. 126, Charles Scribner's Sons, New York — London, 1933.

identified by their specialties. There were slave markets at Azcapotzalco and Izocan, gold at Oaxaca, jade in Guerrero, textiles at Texcoco, and at Acolman the natives concentrated their sole efforts on dogs. The people in the handicraft centers were generally poor, but the traders waxed rich. Chichicastenango was a center of wealth, for most of its citizens were middlemen, and its weekly market attracted visitors from far and wide. In fact, every adult who desired to buy or sell anything was expected to attend the nearest market because otherwise the wrath of the market god might be aroused. The Aztecs effectively suppressed the practice of forestalling by universally subscribing to the superstition that it was unlucky to sell things enroute to market. This belief was so strong that it still persists throughout Central America.

The Great Market of Tlaltelolco

One of Cortez's soldiers vividly describes this trade center which they saw in their march on Mexico City.

"When we arrived at the great market place, called Tlaltelolco, we were astounded at the number of people and the quantity of merchandise that it contained, and at the good order and control that was maintained, for we had never seen such a thing before. The chieftains, who accompanied us, acted as guides. Each kind of merchandise was kept by itself and had its fixed place marked out. Let us begin with the dealers in gold, silver, and precious stones, feathers, mantles, and embroidered goods. Then there were other wares consisting of Indian slaves both men and women; and I say that they bring as many of them to that great market for sale as the Portuguese bring Negroes from Guinea; and they brought them along tied to long poles, with collars around their necks so that they could not escape, and others they left free. Next there were other traders who sold great pieces of cloth and cotton, and articles of

twisted thread, and there were cacahuateros who sold caco. In this way one could see every kind of merchandise that is to be found in the whole of New Spain (Mexico), placed in arrangement in the same manner as they do in my own country, which is Medina del Campo, where they hold the fairs, where each line of booths has its particular kind of merchandise, and so it is in this great market. There were those who sold cloths of henequen and ropes and the sandals with which they are shod, which are made from the same plant, and sweet cooked roots, and other tubers which they get from this plant, all were kept in one part of the market in the place assigned to them. In another part there were skins of jaguars, otters, deer and other animals, badgers and mountain cats, some tanned and others untanned, as well as other classes of merchandise.

"Let us go and speak of those who sold beans and sage and other vegetables and herbs in another part, and to those who sold fowls, cocks with wattles (turkeys), rabbits, hares, deer, mallards, young dogs and other things of that sort in their part of the market, and let us also mention the fruiterers, and the women who sold cooked food, dough and tripe in their own part of the market; then every sort of pottery made in a thousand different forms from great water jars to little jugs, and these also had a place to themselves; then those who sold lumber, boards, cradles, beams, blocks, and benches, each article by itself, and the vendors of pitch-pine firewood (for torches), and other things of a similar nature. I must furthermore mention, asking your pardon, that they also sold many canoes full of human excrement, and these were kept in the creeks near the market, and this they use for making salt or tanning skins, for without it they say that they cannot be well prepared . . . .

"Paper, which in this country is called Amal, and reeds scented with liquidambar, and full of tobacco, and yellow ointments and things of that sort are sold by

themselves, and much cochineal is sold under the arcades which are in that great market place, and there are many vendors of herbs and other sorts of trades. There are also buildings where three magistrates sit in judgment, and there are executive officers like Alguacils who inspect the merchandise. I am forgetting those who sell salt, and those who make the stone knives, and how they split them off the stone itself; and the fisherwomen and others who sell some small cakes made from a sort of ooze which they get out of the great lake, which curdles, and from this they make a bread having a flavor something like cheese. There are for sale axes of brass (bronze) and copper and tin, and gourds and gaily painted jars made of wood. I could wish that I had finished telling of all the things which are sold there, but they are so numerous and of such different quality and the great market place with its surrounding arcades was so crowded with people, that one would not have been able to see and enquire about it all in two days."[18]

Obstacles to Primitive Trade

Presently, much interest is manifested in the multiple cross currents of human activity which limit or interfere with our institutional developments. From different quarters, attention is riveted on various barriers to trade, their origins, causes, and effects. Some light may be thrown on the nature of these impediments for the purpose of contrast by parading them past this point for brief review.

The most obvious limitation, of course, is the scarcity of economic goods attributed in some degree to a self-sufficient mode of life and in part to an undeveloped technology. Warfare invariably affected trade, sometimes favorably, but more often unfavorably, by cutting supply lines, damaging capital equipment, retarding production, and eliminating customers. A natural se-

[18] Ibid, pp. 75-77.

quence of war is the substitution of fear and suspicion for mutual trust and confidence which forms the basis for trade. Fear and mistrust tend to break society into fragments and drive it into the seclusion of provincialism. Provincialism is the primary cause of linguistic differences and the disruption of lines of communication.

The degree of maturity attained in civil administration and in formulating economic organizations is related to the stages of development passed through in perfecting the technology of trade. The individual should be able to distinguish moral precepts from economic expediency and apply them to his needs independently. He must break the spell of fetishes, of taboos, or of imaginary animisms associated with economic goods, in order to gain the high ground of objectivity in his attitude toward them for purpose of exchange. Without arriving at this rational attitude, there can be no efficient medium of exchange. If there is no intermediary commodity to facilitate trade, then barter or gift exchange is the only resort, and frequently this mode of intercourse is stringently restricted by the arbitrary action of either party to the transaction. Finally, trade in a primitive society is usually hampered by inadequate transportation facilities and curtailed by seasonality in production.

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13

THE ERA OF PAGAN TRADE IN NORTHERN EUROPE

THE millennium extending from 400 to 1400 A.D. is sometimes alluded to as the *Dark Ages.* Through the sedulous search of many scholars much fiction about economic activity in this period is being transmuted into fact. The evidence reveals an era of exploration and trade little suspected by the earlier historians.

The prelude to this development in Northern Europe was enacted by a community of people inhabiting an area of the low countries roughly corresponding to what is now Southern Holland.

The Seamen Merchants of Frisia

The pagan Frisians were a sea faring people who ventured far from their native towns and ports. Archeological findings indicate that they penetrated the Baltic as far North and East as Birka, Sweden; Slesvik Hedeby in Denmark, and there is some evidence of Frisian trade in Finland, at Novgorod, Russia, the North Sea to Trondhjem Fjord, along the shores of Scotland and England and on as far West as Ireland. Their boats appeared often on the Irish Sea in the Sixth Century. The Anglo-Saxon invasion of Britain, in which the Frisians are reputed to have taken part, served to extend

the sphere of Frisian commercial influence. The evidence is conclusive that the Frisians played an important role in cross-channel commerce, and as intermediaries in the trade between countries of North and South Europe and as far away as the Orient. The area of intense international trade was centered on the lower Rhine, the Meuse, and the Scheldt. The slave trade was affected to some extent by the introduction of Christianity, but it lasted until at least as late as 1066 when abolished by the royal decrees of the Norman Kings. The second article of commercial importance in Frisian trade was raw material produced in great quantities on the salt marshes north of the Rhine effluence. In these fertile grasslands herders tended thousands of sheep and the production of large quantities of wool providing the basis for the cloth weaving trade. The Frisians were engaged as the middlemen for the distribution of Flanders' fabrics which became by 800 widely known throughout all the trade centers of Europe for their excellence of quality. Some grades of cloth were standardized and were in such universal demand they were eventually used as a medium of exchange.

Southern Frisians were conquered by the Franks in the first half of the eighth century. It may have been primarily a Missionary project to extend the influence of Christianity, but it is likely that it was also inspired by commercial motives. In this conquest, the fundamental bases of trade were at first unfavorably disturbed. The Franks were a lands' people who did not maintain the marine commerce in as full volume as that established by the Frisians. Ironically the fruits of this conquest opened the way for the invasion of the Norsemen and during the ninth century the lowlands were overrun by the aggressive sea rovers from Norway and Denmark.

The Frisian cloth trade had been so firmly established as an important item of commerce in the preceeding centuries that its increasing volume gradually filled the void caused by the declining slave trade. So strong was this current of trade that the inroads of the vikings from the North only disrupted the business of exchange temporarily. In the long run, medieval commerce was conceivably augmented by their visitations. The trade center of Duurstede was attacked five times and burned twice by the Northmen in the ninth century, and yet trade persisted at this strategic port and other juncture points in the Rhineland where trade routes from the East and the South converged with those from the North and West. Frisian trade centered in the Rhine area was eventually supplanted by rising German commercialism. The Frisians displayed throughout this long period such a remarkable inclination for commercial enterprise that even after their conquest, their skilled seamanship served to project trade and exploration over a considerable area of Northwestern Europe until the viking interlopers superceded them on the seas.

Viking Trade

The term "viking" is used in the popular sense to connote audacious seamanship. The etymology of this word taken from the Scandinavian language remains clouded, but artists, authors, and poets have put its legendary symbols to good use. Like the three prongs of Neptune's Trident, the vikings represent three branches of the same racial species and they spearheaded its exploits at sea in diverse directions, sometimes collectively and at other times as sole representatives of their own racial branch. The Norwegians vikings sailed northward around the Cape to the White Sea region; south along the Atlantic coast into the Mediterranean; but most notable of all, they turned the high dragon

prows of their trim craft westward to discover Iceland, Greenland, and the American continent. The Danish seafarers plied their boats across the English Channel and southward into the inlets and bays of the Atlantic coast, also traversing the Mediterranean. The Swedes were mainly preoccupied in exploring and projecting trade in the Baltic Sea region pushing inland along the coast, and eastward into Russia, thence southward into the Byzantine Empire to the gates of Constantinople.

The Threefold Objective of Viking Expeditions

Tempermentally, the vikings of old excelled most men of their time in the spirit in which they entered into their hazardous voyages and in their attitude toward business enterprise. Bugge asserts that they "had little in common with the long bearded, grimy Chapman who in Germany and in England was saving up penny upon penny in the sweat of his brow."[1]

Trade Promotion — The initial phase of the viking era probably developed out of a desire to obtain some essential commodities not easily produced in the northern latitudes. After the spring crops had been sown, or following the autumn harvest, some of the leading farmers along the seacoast broke the monotony of agrarian routine by engaging in domestic coastal barter or by organizing a seagoing expedition, either for raiding some remote settlement or to secure supplies of grain, honey, metals, malt, leather, and weapons in exchange for dried fish, furs, skins, walrus tusks, and ropes. A few townsmen joined in these enterprises often as suppliers of goods or credit, or as marketeers. Goods from the seaports were carried inland to the towns and farms by peddlers. The early expeditions were exploratory and generally less violent than the subsequent

[1] Ravndal, G. Bie, "Stories of the East Vikings," P. 30 (A. Bugge), Augsburg Publishing House, Minneapolis, Minn., 1938.

viking incursions. Often these freebooters from the sea would approach a settlement showing the white sides of their shields to indicate peaceful intentions, but after completing business transactions, there was always the possibility of them suddenly turning belligerent and with drawn swords entering the fray in furious battle against anyone who might resist their perfidious designs against the community. The success which attended these first pursuits afield was so inviting it stimulated the formation of bigger and better units of enterprise by an agreement among neighboring farmers and merchants. In this agreement some members furnished the ships while others pooled goods and credit to form the cargo. Returns were customarily divided equally between the ship owners and the suppliers. The profits of the venture were further subdivided equitably among the individuals in proportion to their contribution, making some allowances for experience and skill in bargaining. Another variation of the agreement applied to the joint ownership of a ship in equal shares by the business partners. The cargo, however, remained individual property and could be loaded in varying amounts according to the resources of each enterpriser in the firm. In this case, the returns for cargo were divided in proportion to the amount provided by each shipper. Veblen surmises that in the middle of the ninth century these small associations comprised from two to a dozen boats of thirty tons burden each, manned by about eighty men.[2] Gradually these small, informal, transient associations crystallized into more formal organizations. Their operations became routinized and continuous. The procedures for sharing profits or losses, contributing supplies, selecting leadership and settling disputes formed the basis for an unwritten merchant

[2] Veblen, Thorstein, "An Early Experiment in Trusts", Journal of Political Economy, P. 272, Vol. XII, March, 1904.

marine law, which was later absorbed by the international merchants code. During the latter part of the ninth century the ground work was laid for more elaborate undertakings. It is probable that tonnage increased year after year since there is evidence that both the size of the crews and the number of boats were also increased. The facilities and equipment for expeditionary forays were perfected, new techniques of trade and market outlets developed, and leadership trained for extensive operations. By the middle of the tenth century the number of viking ships ranged somewhere between 600 and 1000 with average crews of from 150 to 200 men.[3] The volume of trade, likewise, increased phenomenally and became more varied in character.

"It was the prospects of good trade that enticed the merchants, and induced them to venture their lives. If the voyage was successful, they monopolized the market and asked their own prices. They had the right to expect good payment for the things they had with them; there was much that the Greenlanders needed and they were ready to pay extortionate charges for them, grain and malt, hardware and timber, apart from luxuries and all kinds of wares which were novelties to them and made their women stare. As this trade of necessity could only be barter, it was up to the colonists to offer valuables in exchange, things which it would pay the merchants to carry back and sell on the markets of Europe."[4]

Some of the commodities imported by Scandinavia in this period were: textiles, iron, leather, weapons, fruits, wines, silk-stuffs, spices, salt, dyes, precious metals, and jewelry. The exports were: dried and salt fish, furs, whale oil, walrus tusks, ropes, skins, wax, tar, and timber

[3] Ibid. P. 273.

[4] Norlund, Poul, "Viking Settlers in Greenland, and Their Decendants During Five Hundred Years", P. 94 (Translation), Cambridge University Press, London, 1936.

products. The most lucrative part of the business, however, was trafficking in slaves and providing passenger and freight services. These enterprises finally graduated into big business for their time, and the "squeeze was on" to force individual entrepreneurs out of business.

Territorial Expansion and Conquest. — When Europe lost its sheet anchor in the Roman Empire, most of the West reverted to an agrarian status. The thriving chain of cities which constituted the Empire's focal points of influence along the route, extending from Italy to the British Isles, had fallen in decay. No longer centers of industry and trade, they relinquished their cultural and political character, many of them to become mere rustic villages dotting great expanses of wastelands reclaimed again by forests and inhabited by wolves. The happy combination of elements which once filled this region with promise began to recede and at the end of the eighth century it reached its lowest ebb.

Throughout the eighth century the Franks pushed irresistibly northward crushing the vaunted sea power of the Frisians by subjugating the people. Next, they defeated the Saxons and swept them into banishment to come face to face with the Danes across the Eider River border. Considering the fate of their neighboring nations, the viking Danes, to avert attack, decided to strike first. They eventually defeated the Franks to conquer Frisia. Later the Norwegian vikings conquered and occupied Normandy. It was in this period that the rapacious Northmen swept in wave upon wave without warning to enslave, torture, rape and murder the residents of peaceful coastal settlements. The fury of the attacks by these infamous pagans upon the Christian Celts and Franks accentuated the struggle as a clash of two faiths. At first, their onslaughts were test attacks to probe the enemy's strength.

The initial victories of all the viking raids spurred

them on to sustained assaults which ultimately resulted in the conquest of the Scottish Islands, Frisia, Normandy, Ireland, and East Baltic States, England, and Western Russia. In addition to these territorial conquests, the Norsemen colonized the Faroes, Iceland, and Greenland, and the Swedes extended their sphere of influence across Russia as far south as Constantinople, to contact the trade caravans from the East. The chief centers of this expansive territory became bases of operations for the Northmen. Their seagoing craft traveled from point to point more or less on schedule, forming a network of markets through which slaves, plunder and products of the different kingdoms flowed out to all insular and continental points. At that time, there were no moral compunctions in the North against making slaves of the captive Christians, or in the southern countries against making slaves of the pagans. It was the most profitable item in commerce, and both males and females were freely bought and sold, and carried away many leagues from their native lands. One of the sagas relates an incident of significance in slave trade. "On a certain occasion a wealthy merchant named Gille, ... surnamed the Russian because of his many journeys to that country, set up his booth in the market *at Gotaelv* (Gottenborg) and received a visit from the Icelander Hoskuldr who was anxious to buy a female slave. Gille drew back a curtain dividing off the inner part of the tent and showed Hoskuldr twelve female slaves. Hoskuldr bought one and she proved to be an Irish King's daughter who had been made captive by viking raiders."[5]

Piracy — The Business of freebooting attracted new recruits and increasing amounts of capital investment at an impressive rate as news reached home of fresh conquests abroad. Rival enterprises began preying on one

[5] Mawer, Allen, "The Vikings", pp. 96-97, Cambridge University Press, London, 1913.

another at sea and in the market towns. The famous Danish market center at Odense on the isle of Funen was sacked repeatedly by the pirates from the isle of Wollin. Competition between these rival units became excessive. Finally, it was evident the industry needed some stabilizing influence and a leader came to the fore from the Jomsvikings to form a coalition of the larger associations which operated in the South Baltic region. The superiority of this organization soon became apparent, and many concerns hastened to affiliate with the new trust which was rapidly gaining a monopoly position in the trade. Its renown and authority spread to the far reaches of the North, touching political as well as economic interests everywhere. After Veblen reviewed the saga literature, he describes this situation in the following words: ". . . . toward the close of the tenth century the trust stood in a high state of prosperity and was in a position virtually to dictate the course of the traffic for all that portion of the viking trade that centered in the Baltic. Its prestige and influence were strong wherever the traffic extended, even in the region of the western isles and in the fjord country of Norway. It had even come to be a factor of first-rate consequence in international politics, and its power was feared and courted by those two sovereigns who established the Danish rule in England, as well as by their Swedish, Norwegian, and Russian contemporaries."[6]

Market Sites — The most famous market sites in old Scandinavia were known to predate the viking era. Many of them had already acquired the aurora of divinity as pagan shrines, and they were invariably made a sanctuary free of violence against persons and property. At first, throngs were attracted to these places for the purpose of worship and sacrifice. The priests thus

[6] Op. Cit. P. 277 (Veblen)

received much goods as gifts to the gods, some of which they authoritatively appropriated for their own use. At times, when surpluses of certain goods accumulated, the pagan priests would barter them for other items of necessity. They encouraged traders to visit their shrines by providing safety in transit within the jurisdiction of the temple as well as a secure repository for gold, silver, and other valuable items of commerce. With some exceptions, the factors determining the location of the market sites in Scandinavia were quite similar to those in the Mediterranean area. They were, first of all, important junctures in either the sea lanes or the overland routes. Second, they were commonly situated at territorial borders or in strategic, deep, sheltered harbors. Some of the principal markets of the 9th-11th centuries were: Visby on the isle of Gotland; Odense on Funen; Skirningsaal, Sarpsborg, and Tunsberg on the shores of the Oslofjord, Nidaros (Trondhjem) and Bergen of Norway; Bajarkoe towns of Sweden and Finland; Heidaby near Slesvig; Limerick, Dublin, and Wexford of Ireland; London, Bristol, Grimsby, Newcastle, and Lynn of England; and Eyrar of Iceland. No attempt is made here to enumerate the many settlements of the East Vikings in Russia.

As commercial activities increased, the priests were supplanted by market officials called *Gjaldkeri* who invoked strict rules and regulations governing all transactions. Inevitably, there occurred some jurisdictional disputes in the vicinity of these commercial centers and it became necessary to establish boundaries between town and country. Market codes were formulated by the merchants to facilitate trade, and to reassure everyone of fair dealings. Two of these codes, the *Grogaas* of Iceland and the *Bjarkoierretter* of the Baltic, are worthy of mention because they were quite similar on many points to the merchant law evolved in the piepoudre courts of France.

Coins, Weights and Measures — In the beginning, most of the Northmen's transactions were consummated by direct barter. Early in the ninth century, however, two or three commodity mediums of exchange became accepted standards of comparative value, reminiscent of the system of pairing used by the native South Sea Islanders. One cat skin was equal to two fox skins, and one ell of linen would exchange for six lambskins. One of the most common items of commerce in Scandinavia was a woolen textile called wadmal. It was used for clothing, for temporary shelters, and as sail cloth. No expedition overseas was complete without an extra supply of wadmal to replace the ship's sails in case of emergency. Wadmal was made a medium of exchange by royal decree, and it proved to be a boon to all viking commerce because every hand loom in the land became a potential mint. This textile was woven in two or three qualities, and its value became variable as the supply increased or diminished. Ordinarily, five to seven ells were considered equal in value to one ounce of silver. In Norway and Iceland fox skins and cows were also accepted standards of value. Before and after the nineteenth century a number of large caches of coins, presumably buried by viking raiders and traders, were unearthed in Denmark, Norway and Sweden. These collections reveal the extensive nature of international trade in the ninth-twelfth centuries, and throw some light on the degree to which trade was facilitated by many divisible units of gold and silver currency.

Some common linear units of measurement were based on the average length of the foot, thumb to the first joint as an inch, and finger tip (middle finger) to elbow as an ell. Later a double *ell* (1 yard) called a *stika* was introduced in Iceland. Some weight measures similar to our ounce and pound and multiples thereof were in general use. Liquids and grains were measured out in various kinds of containers and bags in common

use throughout the north. Records were kept among traders by means of the time-honored notched stick. After the notches were made, the stick was split end to end through the center and one side was given to each party to the transaction. To verify the record later, the two parts were matched and the notches had to coincide with one another. It was not uncommon for vikings to extend credit in business deals, and the going interest rate was generally fixed at ten per cent or less. The introduction of Christianity interferred with the practice of usury for a long period before the reformation. Bargains and agreements were simply made in the presence of two or more witnesses and sealed with a handshake. Their verbal contracts with few exceptions were faithfully fulfilled to the last detail.

The Decline — The star of the viking international coalition slowly went down and disappeared in the mists of oblivion. Its setting followed a rash and ill-advised military campaign against Norway. The Jomsvikings were defeated by Jarl Haakon and his son Eric in the great naval engagement at Hjorungavaag in the year 985. After successive reverses, the trade combine never regained its former prestige and its organization steadily lost substance under the mismanagement of Sigvaldi. It has been aptly put that "too little thought was given to 'economics of production' and the charges were pushed beyond 'what the traffic would bear'."

The introduction of Christianity in the north knocked the bottom out of slave trade, since the bondage of Christians was prohibited. The long arm of law and order instigated by the strong centralized governments then forming barred other illicit activities and subjected them to some stringent regulations. Freight and passenger traffic, and limited trading privileges were not sufficient to cover the costs of operation and create reserves against depreciation and obsolescence. The

free trading vikings could not thrive in the atmosphere of premercantilism which came into vogue in the 12th century. Their enterprises fell into the laps of the monarchs by default, when these royal persons monopolized particular segments of lucrative international commerce for the edification of their own exchequers.

The Viking Contribution — The innate capacity of the vikings for designing patterns of organization has influenced economic activities in all capitalistic societies down to the present day. They cast the die for big business units essential for large scale operations on an international basis. This specific form of organization was effectively applied for three centuries by their successors, the Hanseatic League and the Merchant Adventurers. As a corollary to the trust or combine, they evolved a workable system for partners to pool economic factors and share profits and losses in their business ventures.

The attitude of the vikings imparted a new meaning to trade. It was accorded a high place of esteem in the pagan societies and many young men were attracted to the merchant profession as a lifework. In this social mileau, new commercial centers were founded and connected by a comprehensive network of trade routes. The flow of goods and ideas through these channels served to spread new cultures and stimulate interest in the arts and sciences. This development is epitomized in the spread of Christianity and its subsequent influence upon slave trade. The most brilliant achievement of the vikings, however, is reserved for final commendation — their pioneer work in navigation, exploration, and colonization. Self confidence in their mastery over the seas gave them courage to venture out and beyond the known limits of their narrow world. They opened new vistas and discovered new continents in their irresistable drive to find new wealth, fresh adventures,

and a niche in the hall of fame that they might be eulogized forever in the recitation of the sagas.

The Hanseatic League

For 300 years the German merchants along the South Baltic coast understudied the viking traders in commercial enterprise before they got an opportunity to venture out on their own account. Around the middle of the twelfth century while the Jomsvikings were suffering reverses, the German merchants on the periphery of the Dano-Swedish Empire quickly usurped trade opportunities momentarily neglected by these Scandinavians. The first Hanses were made up of entrepreneurs who agreed to travel and trade en masse for mutual protection. They soon established connections in ports and towns which assured them a place to barter and a status of relative security. The Hanse which survived the vissitudes of time longest in any foreign land was formed by a few merchants from Cologne who were granted special privileges in England as early as 1194 by Richard the Lionhearted. Their first London domicile was known as Guild Hall; later they moved to new quarters — the Steelyard, and they carried on trade in this location until 1598 when Queen Elizabeth ordered them out of the country. These early associations sometimes called *Universitas* were primarily concerned with trade, but as their influence spread and permeated deeper into the body politic they came into conflict with the ruling nobility. From this point forward, the Hanses assumed a dual role as a politico-economic organization to smooth the path of their trading fraternities. It became their chief function to secure exclusive privileges wherever guile, intrigue, diplomacy, threats, or force might be used to good advantage. They demanded freedom of latitude in their operations, security of their persons and property both on and off location, and con-

cessions pertaining to tolls, fees, fines, and custom duties. The first Hanses established their headquarters at Visby on the island of Gottland. This location was a convenient stop-over center for merchants traveling between Novgorod in the East and the cities on the west coast of Europe. Trade connections were established with other cities along the Baltic coast extending east and northward from Lubeck to Reval. The benefits of membership in the Hanse soon became apparent, and many new autonomous Hanses joined the loose confederation. The initial period of association was one of camaraderie and mutual effort to create bases of trade and to perfect a system designed to give them exclusive control over commerce devoid of any reciprocal rights. The Danes retaliated by capturing the cities of Hamburg and Lubeck and subjugated the interlopers to administrative control for twelve years. Later the Danes attempted to overrun Holstein, but a coalition of the Hanse towns met the Danish imperialists on the battlefield at Bornhoved 1227 to stem the Nordic tide from sweeping further south. The Danes continued to harry Hanse shipping in the Baltic until they precipitated a naval skirmish in 1249, in which they were outmaneuvered.

This centennial victory for the Hanses brought to a close the first phase of organized German trade in northern Europe. After 1250 the character of the association changed. An increasing proportion of commercial transactions was directed by written documents emanating from central offices, and revenues from shipping supplemented the profits of trade. The Hanses gained in numbers, extended their lines of trade to remote points, and they increased their control over many of the staple items in northern commerce. The Lubeck statesmen outwitted the merchants of Visby to assume the nominal leadership of a new coalition known as the Hanseatic

League, which had as many as 77 cities on its membership roll at one time.

As long at the Danes controlled the Cattegat, the Germans were forced to channel their east-west flow of goods through Lubeck across the narrow isthmus of Holstein to Hamburg and on to the West by way of the Elbe River route. The strategic importance of Lubeck as the axis of Hanse Baltic trade is easily discerned when it is pointed out that the Danes could have completely dominated all Baltic commerce if they had chosen to conquer Holstein.

As Valdemar III, king of the Danes, grew in maturity on the Danish throne, he decided on another course — to drive the ever menacing League out of the Baltic by destroying their ships and by raiding their chief centers of trade. True to his plan, he succeeded in sacking Visby in 1361, but he lost the rich prize reputed to be worth more than 100 million dollars at today's values in a storm while returning homeward. The Hanse leaders were infuriated by the King's audacity, and they called a conference at Cologne of the principal League cities which entered a compact to fight the Danes unto death. They laid their plans for attack and they levied a tax on all Hanse merchandise to finance the campaign. The first attack by the bunsas of Lubeck and the Wendish cities was attempted in 1362 and was defeated when Valdemar intercepted their fleet cutting off supplies to the land forces left at Helsingborg. About seven years later the Hanses struck again with a formidable force invading the Danish Islands and taking Copenhagen. As a consequence of this exploit Valdemar Atterdag contracted unjustifiable misgivings about the invinciability of the League, and the astute leaders of Lubeck were quick to drive a hard bargain in the treaty of Stralsund in 1369. This treaty granted concessions which permitted the League's ships to move freely through the

Sound out into the North Sea, extending their monopolistic control over trade in fish, cloth, grains, and furs to the western islands and the fjord country. The management of business enterprises became increasingly more complex as the bases of operation were further removed from headquarters. Absentee control through a system of partnerships, assistants, commission agencies or personal representatives under contract required prudence in the selection of personnel, meticulous record of transactions, and a judicious choice of risks in order to realize the greatest net profits from the undertaking.

The League attained the zenith of its influence and earning power about the middle of the 14th century. To gain this position it had used fair means and foul to invade new territory and fasten itself like leeches upon the indigenous population. Once these arrogant German burghers gained a foothold, they assiduously fortified themselves behind strong walls in exclusive compounds called factories. Within these barricades they evolved the original patterns of fanatic totalitarian regimentation governing their own lives and those of others. Their treatment of apprentices was degrading in the extreme; their initiations were barbarous and they were sworn to Monkish celibacy for the entire period of their foreign tenure. Here they were a law unto themselves both temporal and spiritual, for they maintained their own church. They administered justice, and meted out punishments. They practiced deceit and fraud with impunity. They brooked no interference with their business, and they discriminated against traders from other countries by imposing trade barriers and exacting exorbitant tolls. There was no element of social consciousness in their close textured cartel.

No trade organization committed to these policies

could hope to last indefinitely. The processes of degeneration began shortly after the League's greatest victory in the Treaty of Stralsund, 1370. The first fractures in the organizational structure were caused by internal dissensions. Some free cities broke with the League to reinstate their allegiance to territorial sovereigns; others were weaned away by a desire to pursue their own selfish ends. Shipping was constantly harassed by a gang of freebooters under the notorious leadership of the Victual Brothers — outlaws which the League earlier subsidized to raid Scandinavian cities. The Treaty of Thorn and the Union of Kalmar indicated a trend toward territorial alliances which cast a shadow over the despotic League. Another blow to the League occurred in a curious natural phenomenon. The Herring began to desert the Baltic about 1425 to infest the North Sea coastlines as though they, too, desired to have no part in the monopolistic trade of the League. The English and the Dutch reaped their conjunctural gains from this capricious piscatorial shift, and used them to attain maritime supremacy, and to challenge the appropriated trade rights of the Germans.

The Hanseatic League is not credited with any significant contributions that had not already been features of other merchant communities. The vikings had blazed the trails, many of which were not maintained by the Germans. They had established the market centers and developed methods of exchange. In like manner, the Lombards preceded them as financiers and as users of credit instruments and written records. All this the German burghers inherited and possibly refined to some degree. They failed to grasp the idea of reciprocity as an essential ingredient in exchange. They instituted xenophobic policies to exalt their endogamic ideals. The German townsmen, with all their genius for organization, never succeeded in welding the diverse

units of the League into an integrated business enterprise. Moreover, these avaricious traders were steeped in the tradition of following a policy of exploitation of the masses at home and abroad. To the very end they remained adamant to changes in keeping with the times, and incapable of visualizing trade as a democratic process in which all participants could take part on an equal plane.

The Merchants of the Staple

One of the oldest and most informal organizations for trade in England was the merchant staple system. The organization in scope and functions is difficult to describe vividly because its existence was so tenuous for long periods of time that it resembled a shadow more than a reality. It emerged from an era of craft or trade guilds to assume the imaginal form of a franchise quite similar in some respects to the monopolistic privileges granted market fairs. The brotherhood adopted a patron saint in Thomas Becket to dignify their calling, and by implication, to fix the date and place of their origin — 1248. Prior to the 14th century, a large proportion of England's export trade, consisting mostly of wool and cloth, was performed by alien merchants. The word "staple" was probably derived from the French term *estape* signifying a mart or a market place and it connotes stability. The principal items handled by the merchants of the staple were wool, woolfells, leather, lead and tin, and sometimes butter, cheese, and honey were admitted to this list of commodities. It is also surmised by the historians that these merchants occasionally dealt in English woolen fabrics, a fact which later became a bone of contention between the merchants of the staple and the merchant adventurers, in settling their respective fields of mercantile specialization.

It was during the age of the national chartered

monopolies that mercantilism fructified to yield both political and economic objectives for the crown. The obsequious staplers were swayed by every whim of the king because their status as traders depended upon his central authority. The 13th to the 17th centuries are rich with illustrations of royal management of commercial affairs particularly affecting the locations of markets and the persons accorded the right to trade. As the fortunes or alliances of the kings varied, they freely cited statutes, ordinances, or decrees shifting the location of staple markets from city to city and from principality to principality beyond the seas, as well as to shuttle the enterprises back and forth across the English Channel in retreat or in aggression.

In 1313, no distinction was made between alien and native merchants in granting rights to export wool from England. Forty years later it was decreed a felony for any Englishman to export wool.[7] Edward II issued an ordinance in 1326 designating 17 towns in England, Ireland and Wales as staple centers. No commoner was permitted to use imported cloth, and in 1337 the exportation of English wool was expressly prohibited.[8] The death penalty for exporting English wool was lifted in 1363,[9] but in 1369 it was made a three-year prison offense including forfeiture of all goods if apprehended in the act of exporting.[10] Throughout these early years, Calais and Bruges vied with one another to secure the English trade whenever the English chose to export wool and other staples. Not infrequently the English kings would favor one city or sovereign power over other rivals with schimatic effects to achieve a political coup. Adherence to sound commercial policy was too often

[7] 27 Edward III, Statute II
[8] 11 Edward III Caps. 1-5
[9] 38 Edward III, Statute i, Caps. 2 and 6.
[10] 43 Edward III, Cap. 1.

neglected for power politics by the kings who considered themselves men of destiny.

The Merchant Adventurers

In tracing the origin of the merchant adventurers it appears that this fellowship of itinerant traders is an offshoot of a common rootstock with the merchants of the staple. Both associations emerged from the guild of mercers, both claim the same patron saint, and originally their functions were quite similar. As it has been pointed out, the staplers specialized primarily in assembling and exporting such English raw materials as metals, fibers, skins, and some agricultural products. By contrast, the merchant adventurers eventually stress the functions of exporting and selling finished goods of English manufacture, particularly wool cloth. To the adventurers goes the credit, too, for displacing alien traders in England — especially the Germans. The fluorescence of the merchant adventurers' system like the staplers' was one of slow evolution. The staplers were probably the dominant fellowship in the period 1250 to 1450 because the domestic manufacture of cloth had not reached a high state of development. After 1450, however, the adventurers superseded their rivals to hold the center of the stage for the second 200 year span of time.

English metals, lead and tin, had figured prominently as exports as far back in time as 300 B.C., and English cloth was known to the northern peoples long before the great medieval trading companies were formed. Henry I looked favorably upon control of domestic trade by Englishmen, and he encouraged the craft guilds to form associations for trade. In 1296, John II, the Duke of Brabant, extended an invitation to merchants of all countries to trade in his Lowland provinces. He granted them special privileges of residence, freedom of enterprise, and the right of self-government. The

Low Countries had already earned an enviable reputation for their fine woolen fabrics and the fame of the Bruges cloth fair had spread to the four corners of Europe. The adventurers of England were especially favored for their imports of wool and unfinished cloth since it augmented the supply of raw fiber in competition to that sent up from Spain, and it provided additional employment to the Flemish mercers. Wherever the merchant adventurers chose to locate, much trade activity and prosperity followed to the edification of the residents of the Lowland cities.

History in retrospect reveals the motives underlying the various monarchs' actions in granting monopolistic franchises to the groups of businessmen who formed the great medieval trading companies. They sought to cultivate sources of credit, and to extend their political influence. The adventurers were forced to assume debts incurred by Edward VI and also by Queen Elizabeth during the first years of her reign.[11] In order to achieve these ends, they assured themselves of maximum administrative control over the market institutions by limiting the places and the periods of marketing; the persons who might exercise the right to buy and sell, and the commodities to be handled. Imitating the German Hanses, membership was granted according to patrimony and apprenticeship training, and it was forfeited if marriage was contracted with an alien woman. The merchant adventurers were limited to wholesale transactions, and admission to the fellowship was further regulated by the amount of the membership fee. In the successive charters granted the merchant adventurers there appears to be a trend toward more democratic control within the framework of the fellowship, but

[11] Burgon, John William, "The Life and Times of Sir Thomas Gresham", Vol. 1, Chap. II, pp. 54-112, Robert Jennings 62 Cheapside, London 1839.

whatever measures of independence were gained in the ascendency might be considered indicative of the crown's dependence upon their services in promoting trade and the King's other interests abroad.[12] The fellowship beyond the seas was accorded the right to elect a governor and 24 sober and honest deputies as assistants. These men formed the legislative body empowered to establish rules and make laws governing their conduct. None of their laws, however, were to detract from the prerogative of the king or to oppose in any way the major interests of the commonwealth.

In organizational structure the merchant adventurers were always regarded by the crown as one corporate enterprise made up of several units. The headquarters of the concern was always situated beyond the seas in some foreign country, but the London brotherhood was accorded leadership in domestic affairs of the brotherhood. At times the provincial units revolted against the London representatives for their arbitrary and self-centered decisions in administrative matters effecting the interests of members in the outlying areas.

Prior to the 17th century, English cloth was exported to the low countries undyed and undressed; and profits from commerce in the English woolens were shared

[12] Chronological List of Charters granted the Merchant Adventurers

Grant or Charter of	1296	by John II, Duke of Brabant
Grant or Charter of	1359	at Bruges, Edward III
Grant or Charter of	1407	by Henry IV
Grant or Charter of	1413	Henry V
Grant or Charter of	1420	Henry V
Grant or Charter of	1428	Henry VI
Grant or Charter of	1462	Edward IV
Commercial Treaty	1496	Intercursus Magnus
The Charter of	1505	Henry VII
The Charter of	1564	Queen Elizabeth
The Charter of	1586	Queen Elizabeth
The Charter of	1604	James I
The Charter of	1618	James I
The Charter of	1661	Charles II
Existence terminated	1808	by Napoleonic War

with the craftsmen and tradesmen of the continent. About this time, however, a hue and cry went up in England demanding that these extra values be added by processing the cloth at home. Some experiments had been run to prove that dying and dressing could be satisfactorily performed by domestic craftsmen. King James I was persuaded in 1614 to prohibit the export of unfinished woolen goods by proclamation. Subsequently, the charter of the merchant adventurers was revoked and a new company was formed to sell English cloth on the continent. The venture proved to be a dismal failure because demand failed to develop and the Dutch clothmakers set up competitive looms in diverse places along the west coast of the continent.

The situation in the English industry became so critical that the King appealed, in his desperation, to the merchant adventurers for assistance to recapture the English cloth trade on the continent. In their hour of triumph — 1618, the adventurers secured a charter in which they exacted unparalleled privileges giving them exclusive control over shipping, administration, judication, fiscal policies, negotiations, and sales in the Low Countries and Germany. Around 1625, there were possibly 5000 member adventurers directed in their trade activities by two score leaders. The merchant adventurers might have been more fortunate had their quest for commercial power been tempered; for their incomparable franchise created jealousy among their own countrymen, it aroused the competitive nations, and it incurred the hostility of Parliament which was subsequently assuaged by a loan of 30,000 pounds to buoy up the navy.

The favorable charter granted to the merchant adventurers came too late in the life cycle of the concern to avert its inevitable decline. The Dutch were indefatigable trade rivals and implacable foes in war. At home the western units of the brotherhood continued

their relentless resistence to the monopolistic privileges of the adventurers. The drive was on to liberalize trade in both domestic and foreign markets. It was an era of expansion for chartered trade corporations organized on a joint stock basis. Intensification of production and distribution took some of the edge off foreign markets as well as to restrict the arbitrary imposts of the franchised enterprises. The death knell was sounded, for the merchant adventurers by the incessant wars between England and the nations of the mainland. The final curtain was rung down on their circumscribed activities in Hamburg by Napoleon 1808.

Other Chartered Companies

The Germans, English, and Dutch successively committed the same error as their viking predecessors in permitting the channels of commerce to become fouled and clogged by monopolistic privileges and restrictions. It appears that the sovereign rulers failed to appreciate the potentialities of a free trade or they chose a course of expediency in settling the issues of state and waging wars in the age of mercantilism. In retrospect, it is clear that the inception of trade in each era and for each nation furcated from the activities of private enterprisers who assumed the risks of projecting commerce beyond the seas.

Those who were vested with power, and should have known the course of wisdom, found it difficult to desist from meddling in the business either to satiate some vain impulse or to satisfy a more substantive urge. Moreover, the body of knowledge bearing on the instrumentalities of trade was limited and not decisive. The deductions drawn from previous experiences were apparently not conclusive and were submitted for further tests to prove their worth. A case in point was the attitude toward the precious metals — the nations which

acquired the most gold and silver invariably contrived to hoard the treasure, failing to comprehend its true function as a basis of credit in international exchange. "*They* grasped at the shadow — bullion, and dropped the substance — credit."[18]

Queen Mary dispatched a few ships eastward to arrange trade with Russia and to establish a land and sea trade route to Cathay in the Orient. This venture became known as the Moscovy Company, first formed in 1555, and later chartered by Queen Elizabeth in 1566. The success of various provincial units of the merchant adventurers beginning about the middle of the 16th century resulted in the sporadic growth of new business ventures for overseas trade. They burst into full bloom in Queen Elizabeth's reign, yielding grand dividends both to her and her privateers. The Spanish Company was chartered in 1577, the Eastland Merchants in 1578, and the Levant Company in 1581. There were other less notorious enterprises formed in this same period, all implemented in a large degree by the merchant adventurers and dominated by the crown. A few monopolies usurped the total foreign trade with England. The seas were made unsafe; transportation costs rose; banking and credit were constricted; both supply and demand were reduced to yield the maximum profit on the minimum number of transactions. In this period of Queen Elizabeth's reign, the monopolists levied their tribute on every common item whether luxury or necessity. The whole English economy was blighted by the commercial policies imposed by the chartered companies and condoned by the Queen. Public opinion finally became so voluble it spurred Parliament and the Queen to action. During the last years of her reign, Elizabeth redeemed herself by repudiating the rigid

[18] Unwin, George, "Studies in Economic History" p. 179, Royal Economic Society and MacMillan Co. Ltd., London 1947.

organizations controlling trade, canceled their charters, lifted restrictions, and opened great areas to free enterprise. She abolished certain fees, discriminatory taxes and custom duties. The navy was utilized to protect her merchantmen and to instill confidence in overseas commerce. These policies did much to build the British Empire and extend its influence around the world.

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Prototype of Tribal Market Grids in North Africa

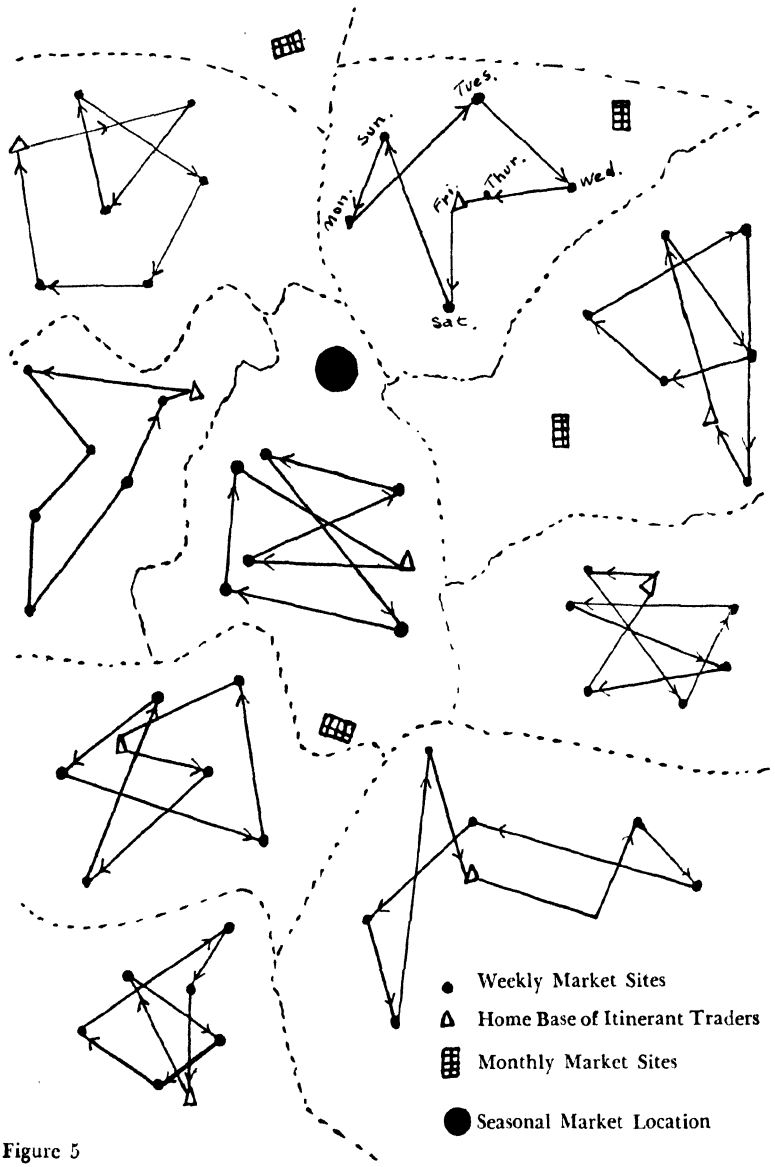

Figure 5

14

MEDIEVAL MARKET FAIRS

THROUGHOUT the first centuries of Christendom trade was generally intermittent and unpredictable. At the fall of the Roman Empire, a process of disintegration set in because the remnants of government left as a bequest from the Romans were too weak internally to sustain a united centralized system. At most of the outposts, the petty officials seized control and claimed it as their prerogative to rule. The territory which is now France, England, and Germany was shattered into hundreds of fragmentary units and each unit became a small armed camp which began waging war on neighboring localities. Warfare induced vandalism, incited robbery and rendered private property precarious, and endangered personal freedom. It was an age of violence. Communities sank back into a state of self-sufficiency, and feudalism took root everywhere. Commercial intercourse sank to a low ebb, but it did not disappear. Exchange was limited to a few refined articles of jewelry, precious stones, fine cloths, spices, slaves, and weapons which only the lords of the manors could afford to acquire. The main items in trade between the feudal estates were salt for curing meats, tar as a preventive for diseases in sheep, and metals in limited quantities for shaping tools.

Agriculture was in a low state of development. The

livestock generally was of poor type and unproductive. " . . . The fleece of a sheep weighed often less than two ounces. Many of the stock had to be killed before winter, as there was no proper fodder to keep them, and those that survived were often so weak in the spring that they had to be dragged to pasture on a sledge. Insufficient stock meant insufficient manure, and though the fields were allowed to lie fallow every third year, they were exhausted by constant crops of cereals, and gave a yield of only about six bushels of wheat an acre, of which two had to be retained for seed."[1]

Hunger and famine was the common lot of man throughout all ages before the close of the seventeenth century. Wolford reported as many as twenty-two famines in a single century, the thirteenth. From the year 1000 to 1600 there were more than fifty famines in Europe or an average of one extremely lean year in every twelve. Plagues followed famines taking a heavy toll of human lives. The survivors were so weakened by hunger and disease, and they succeeded in eking out an existence from the soil only with super-human effort. The causes of mankind's plight in former years were attributable more to his ignorance than to the forces of nature. He had to learn by painful experiences the value of organization and efficient administration of human affairs. Peace had to supersede violence. Mutual exchange of ideas and wares should be made to displace isolation and self-sufficiency. Individual rights and freedom transcend the divine authority of the clergy and the nobility. Gradually it dawned upon man that he could realize infinitely greater wealth and happiness in exchanging the ordinary articles of food, clothing, and shelter than he could in buying and selling either slaves or weapons.

[1] Day, Clive, "A History of Commerce," p. 35, Longmans Green & Company, New York, 1922.

The rebirth of commerce was predicated upon production which in turn was achieved by organization and specialization. As soon as some individuals in society began specializing in the production of particular goods in excess of their personal needs, the incentive to barter manifested itself. If the items produced were in strong demand, it tended to increase the volume of production. When the volume of production rose, it stimulated an interest in systematizing distribution and in formulating plans of procedure. The flow of goods was soon channelized through certain centers where traders could meet periodically for the purpose of mutual exchange.

The Local Market. — In ancient and medieval times when barter was the common form of exchange, centers of trade were roughly classified into three broad categories. The first of these was the *local market.* People contrived to meet occasionally either formally or informally for negotiating exchanges of supplies and services even in areas of undiversified production and in an economy of self-sufficiency. Local markets, none the less, were relegated by our economic historians to the lowest rank in the hierarchy of exchange institutions because the volume of trade through them in sparsely settled areas was relatively insignificant and uneventful. For the first sixteen centuries of the Christian era, the flow of goods in many places in Europe was still so tenuous it would neither support resident merchants nor local markets. Periodic market fairs sufficed to clear the trade for large geographical areas.

Before the invention of steam locomotion, it might be said that trade was geared to the cadence of the camel and the speed of the sail. The difficulties encountered in getting from place to place were one of the most obvious limitations to commercial activity. In some instances, goods from the orient destined for Europe were in transit either overland or overseas for a period

of two to three years. These treks and voyages involved indescribable hardships and great personal risks to the merchant traders.

The Fair. — The second form of organization, *the fair,* was evolved through time as a means to bring large assemblies of persons together periodically at specified places for the purpose of worship, trade, and amusement. The word "fair" has its origin in the Latin term *feria,* meaning a festival. The institution, however, antedates the western civilizations, but its origin has not been revealed. The trail of historical evidence leads us across the Levant and fades out in the east beyond the valleys of the Tigris and the Euphrates. The fair had its genesis in the migratory movement of people who cut across national boundaries in their pilgrimage to distant meccas. Their encampments at favorite watering places and crossroads along the way brought them into contact with the natives of the region. The lure of gifts and the opportunity to barter domestic products for exotic things from other lands provided the essential social solvent for mutual intercourse. A system of seasonal fairs held on staggered dates at strategic locations gave the itinerant merchants time to travel from one fair to another in a never-ending circuit throughout the year. This arrangement was admirably adapted to the tempo of economic life in ancient and feudal times. As an adjunct to the fair, a class of itinerant peddlers gradually formed to extend the business of trading into the hinterland. They acquired a stock of goods either at the seaport towns or at the interior fairs. Their itinerary was also imitatively planned in such a way as to arrive at other seasonal fairs along the way. The products of the interior which they acquired by trading could be exchanged again for imports.

In some of the worse periods of feudal isolation every stranger was looked upon with suspicion. The doughty

middlemen of that age were often assailed, robbed, and made slaves because they had the temerity to intrude in a place where they had not been born, where they were unknown and without friends to vouch for them. The trails to the interior were intolerably bad and so narrow that carts or wagons could not pass. Much of the travel was done on foot or on horseback. In many places bridges had not been constructed so it was often necessary to travel long miles to get from one place to another not far removed as the crow flies. The petty rulers remote from the high roads of commerce were either unwilling or unable to provide protection against violence to life and property for those who desired to travel across their manorial lands to villages and hamlets where they stopped briefly to trade. Eventually, some enlightened sovereigns decreed laws to protect the rights of these traders in their travels, legalized their transactions before witnesses, and granted them valuable franchises for a consideration. There were still other obstacles to trade in those times which taxed the ingenuity of the principals in a barter transaction to the limit. There was great scarcity of money, and usury was considered iniquitous. Nearly everything was brought physically to the fairs and exhibited for direct exchange. Since no effective credit system had been evolved, exchange had to be contrived either for gold or in crude indivisible units of goods for goods, e.g. livestock for jewels. This lack of refinement proved to be a barrier to many exchanges that might have been otherwise consummated, and as a consequence, commerce was retarded for centuries in certain areas of the world even where natural resources were abundant.

Market Grid. — Lastly, the term *Market grid* is proposed to designate a trade area or a system of fairs serving a region such as the network of fairs centered about Champagne during the eleventh to the thirteenth cen-

turies. A similar system of markets even less remote from the primitive barter stage exists today in some parts of the world, such as, the tribal markets in Spanish Morocco and among insular people in the South Pacific areas. This concept is appropriate in the description of modern integrated market systems which are nation or world-wide in their inter-relationship and their interdependence.

The Fairs of Champagne

Out of the lethargy of the Dark Ages emerged a general economic revival in Western Europe laying the foundations for cultural growth two centuries later, 1100 to 1300. The great movements of overland trade between Northern Europe and the Mediterranean Area traversed France. Some of the counts and bishops whose fortified towns nestled in these channels of trade perceived the value of commerce to the community with an eye to the personal revenues it would yield them from tolls, fines, and fees. The most famous fairs of medieval Europe were founded in the rich county of Champagne. These fairs were eventually integrated into a grid of fairs under control authority serving an extensive geographical area. This market system was comprised of several towns at which a number of seasonal fairs were inaugurated each year. The tradition of holding annual festivals in some of these towns possibly extended back in time even to the fifth century. Sidonius Appollinaris (427 A.D.) alluded to fairs in a district of France known later as Champagne. An ancient fair at Lyons set up a special privilege granted by the Roman conquerors. The transition into an intensive commercial system dates from the twelfth century, and the following listed places were the principal towns embraced in the system of fairs held at Champagne and Brie:

Commercial Centers	Date of Franchise	Major Commodity Specialties
Troyes, — warm fair	1114	Linen, Wool
St. Remi — cold fair	—	Leather, Skins
Provins, — autumn fair	1137	Silk, Furs
St. Ayoul — May fair	1138	Wine, Livestock, Salt, Tar
Bur-sur-aube, — Easter fair	1114	Grain, Honey, Cheese
Lagny, su-marne — January fair	1154	Wax, Dyes, Rope

"There is no way of telling how far back this commercial activity had started. The surviving records of Genoa are among the oldest of their kind left, (1191 and 1197) but even they were not by some generations the earliest of their sort produced in Genoa itself. The channel of trade, in which the merchants of Asti and those who did business with them operated, was too wide and deep to have been constructed overnight. The strongly founded credits of the individual merchants — even more, the strongly founded credits general among all merchants — could not have been built up in a short time. The fortunes of the larger dealers must have been impressive for the time, and the total capital turned over in each year's business might have inspired respect in any generation until comparatively recent times. The accumulation of such capital is slow. Transportation problems had been ironed out and risks greatly reduced. To create such a state of affairs, required a long time and steadily exerted organizing and business genius. This world of business could not have been new in the later twelfth century."[1]

Business activities at the fairs were arranged in a manner affording the maximum degree of specialization. Trading was confined to cloth and related items for a period of several days after the official opening of the fair. When trading in cloth subsided, the town criers would terminate further transactions in fabrics

[1] Reynolds, Robert L., "Genoese Trade in the Late Twelfth Century, Particularly in Cloth From the Fairs of Champagne", Journal of Economic and Business History, Vol. III, No. 1., p. 381. Harvard University Press, Cambridge, Massachusetts, 1930.

and announce the fair open to trade in leather, furs, and hides during the next few days. Finally, the commerce of the fair would be devoted to miscellaneous items, settlement of accounts, exchange of currencies, extension of credit and payment of debts.

"There were four sets of merchants to be kept in mind. First, there were the northern merchants who bought up the cloth for sale at the fairs of Champagne. Secondly, there were the caravan merchants, who purchased the cloth at the fairs and took or sent it over land routes to Genoa . . . Thirdly, in Genoa there were cloth merchants *(draperii)* who bought this cloth from the caravan merchants. Although individually not of great wealth, these cloth merchants occupied a key position in both the trade in cloth and the finishing part of the industry . . . They were constantly in debt to the caravan merchants from whom they purchased much of their cloth. They financed the export of this cloth by means of temporary partnerships entered into with the capitalists of Genoa . . . The fourth set of merchants were the importers of Genoa who because of their wealth could easily give credit to the caravan merchants whom they supplied with foreign wares to be carried north . . ."[8]

It was not uncommon to require all resident shopkeepers within a range of several miles to close their business establishments during the period when similar kinds of merchandise were on sale at the fairs. As a concession to these merchants, they were exempted from paying toll for some period on their transactions at the fair. Occasionally the people of the community would register bitter complaints against the exactions of the church or the nobility and they boycotted the fairs and the markets. Arbitrators were sometimes chosen to settle controversies over tolls and fees.

[8] Ibid., p. 362.

The success of the Champagne fairs can be attributed to the initiative and ingenuity of the presiding bishops and small nobility in fostering trade with a relatively free hand. The church was instrumental in maintaining the peace of the fair, and the armed guards of the barons and counts assured the traders security and order in the conduct of their business. In time this protection was extended to cover transit of goods and money to and from the markets.

"The actual means and methods used in transporting men, merchandise, credit instruments and cash between Genoa and Champagne are only partially revealed by the Genoese records, and tell little not already known. Mules and horses were the carriers of cargo and merchants. The pack-animal's bale or *torsellus* was even a unit in trade, cloths being sometimes sold in *torsellus* lots.[4] It was the frequent occurrence for merchants to rent mules and horses in Genoa for given round-trips to Champagne.[5] There were *vecturarii* or professional pack-train freighters from both Italy and the North prepared to conduct shipments, with or without supervision, along the way. These might accept consignments either prepaid or collect. There are not abundant traces of the activities of these men in the remaining Genoese records, however, and they may not have been so important as they were a little later in trade between Mediterranean ports and Champagne.[6]

"The documents tell nothing directly about the organization of the six big caravans which left Genoa every year for the Champagne fairs. But they tell some

[4] Reynolds, Robert L., "The Market for Northern Textiles in Genoa, 1179-1200", *Revue Belge de Philologie et d' Histoire,* Reprint, Vol. VIII, No. 3, p. 838, 1929.
[5] Reynolds, "Genoese Trade in the Late Twelfth Century", p. 375, n. 1.
[6] Reynolds, Robert L., "Merchants of Arras and the Overland Trade with Genoa, Twelfth Century," *Revue Belge de Philologie et d' Histoire,* Reprint, Vol. IX, No. 2, pp. 512-514, 1930.

surprising things indirectly. For one thing, they cast real doubt upon preconceptions as to the difficulties and dangers of overland commerce in the period. The seasons, which would seem to have governed a traffic which crossed the Alpine passes, made absolutely no difference. A great shipment, always one of the most important of the year, left Genoa in the last ten days of December, directed towards the fair of Lagny which opened January 2. A shipment from the north arrived in Genoa early in January, while one of the largest shipments, coming from the fair of Lagny, arrived during the first week of March. The wealthiest of the men of Asti went repeatedly with their northbound shipments in late December and returned from Lagny at once in early March. If the journey took nearly a month each way, as is likely, they spent some two months in January and February on the way over Alpine passes for the sake of a few days' business in the North.[7]

"As is evident from the foregoing, the trade was organized on a basis of almost clocklike regularity. The shipments were made up and started north year after year with perfect precision. The arrivals of the return caravans were as much a part of business calculation as the Church holidays. The risks could not have been great, for risk clauses were not inserted in agreements to deliver merchandise nor in notes covering loans which were to be repaid in Champagne. It was habitual for the merchants to enter into contract obligations which could only have been liquidated if all went well with complicated selling and buying, lending and borrowing hundreds of miles from Genoa. Year after year the same men entered into the same sorts of agreements, often with

[7] This information is derived from a tabular tracing of the business and movements in 1191 and 1197 of every individual among the caravan merchants, aided by notes from the more fragmentary records of other years. *Ibid.*, p. 375, n. 1.

the same creditors, sufficient proof that all customarily went well with such affairs."[8]

The fair cities provided an armed escort for the traveling merchants who promised to trade exclusively at the fairs where tolls were collected. Transactions in the trade centers were further safeguarded by providing scales, the official seal and a corps of notaries to legalize the transfers.

The Merchant Code. — By and by the merchants formed guilds in the region north of the Alps similar to organization of the consuls and provosts set up by tradesmen in Italy to promote the interest of their profession and improve their status. From this increasing influence they distilled the right to settle transactional disputes in their own courts. In exercising this right, a body of merchant law was formulated which was distinguished from other codes for its practical application to commerce in all of its ramifications.[9] The number of traders that converged on Champagne each year from all parts of Europe soon gave the trading cities the atmosphere of an international settlement. The international character of this trade is reflected in the following account:

"However, in spite of all shortcomings in the cartularies of the Twelfth Century the wares of exchange in the Genoese-African traffic throw considerable light upon the importance of Africa in the commercial activity of Genoa in the Mediterranean Sea. The sixty wares mentioned in rather scattered fashion throughout the thousands of contracts of Genoese merchants suggest a commercial activity that was carried on over three continents; they portray a unity that included such distant lands as Turkestan, India, and the East Indies in the

[8] Ibid., pp. 379-381.

[9] *Jus Nundinarm* was a blend of Roman Law, Frankish trade customs, and general tradition of commercial practices elsewhere.

East; Champagne, Flanders, and Germany in the North; and the Sahara and Central Africa in the South. The African trade served as a complement to the other two great mercantile endeavors of the Genoese merchants. The Genoese often used this African trade as an outlet for the many cloths which the northern merchants carried southward from the fairs of Champagne and Flanders and from the cloth centers of Lombardy; from their own city the Genoese sent or carried northward into Lombardy and beyond many of the softer pelts and much of the leather and alum which came to them from Moslem cities across the Mediterranean. Many of the dye pigments, spices, precious stones, and pearls, which came from the far and near east to the Levantine ports and which the Genoese traders carried from Syria and Alexandria,[10] eventually found a final market, not in Genoa, but in the colorful perfumed bazaars of the Moslems of North Africa."[11]

Any affair relating to the welfare of commerce could be referred to the fair courts. The decisions handed down by these expeditious tribunals were ultimately effective to the end of the long trade routes extending across national boundaries and into the city-states. No city or state which aspired to traffic in commerce could defy the power of the Champagne merchant courts or spurn their verdicts because the rights to trade at the fairs would be revoked. Their power even superseded the dominion of the church and the nobility in some matters causing reforms or a modification of sovereign laws and customs outside the pale of commercial activities.

[10] For a list of wares carried from the Levant to Genoa, see Byrne, E. H., "The Genoese Trade with Syria in the Twelfth Century," *American* Historical Review, Vol. XXV, p. 218, 1920.

[11] Krueger, Hilmar C., "The Wares of Exchange in the Genoese-African Traffic of the Twelfth Century," *Speculum*, Vol. XII No. 1, p. 7, January 1937. Published by the Medieval Academy of America, Cambridge, Massachusetts.

A New Class Emerges

The feverish affairs of business and its corollary host of distractions typical of the market fairs created a milieu essentially different from the feudal society which engulfed them because it afforded individuals a greater personal fredom of action in economic pursuits. Many of the tradesmen won free urban tenure, and seignioral tolls were scaled down. Trade was released from the chains of provincialism and administered under a new code improvised to fit the needs of the times. These exceptions to the normal procedures in the province of the nobility and the clergy were conducive to forming a permanent commercial center. The vagrant merchants were enfranchised by the count, domesticated by the townswomen, and anchored by the acquisition of property to form a resident commercial class sometimes known as the bourgeoise.

Those who managed to escape the bonds of serfdom and rise to the status of a merchant also attained the right to travel about from place to place in order to facilitate trade. This precious privilege was accentuated by obsequious churchmen and nobles who became dependent upon the tolls and loans of the merchants to the point where they not only provided armed escorts, but they also made restitution for losses from brigandage. As a special concession, the traveling merchants either assumed or were granted the right to bear arms for their own protection.

The functions of trading implied the power to own, control, and convey private property. The right to transfer ownership, however, was abridged by stringent rules and edicts governing the proper time and place of occurrence in order to make the transactions legal. Originally these limitations were invoked as a measure of public welfare to curb thefts of movable properties such as livestock, and commodities difficult to identify.

In the appointed market places, freemen enjoyed unalloyed liberties of action in an environment of peace and protection. The merchants occasionally extracted an exemption from payment of tolls and fees to the church or the ruling court. They often secured franchises for exclusive rights to trade in particular goods. These monopoly grants, in effect, guaranteed the merchant profits and provided the basis for the extension of private property ownership. Attracted by the lure of profits, trade was stimulated to the point where it induced an increase in handicraft or industrial activities. Increases in productivity, the widening influence of private property ownership, and the realization of larger profits broadened the base for royal levies. As the elements of material and spiritual attainment became manifest, the custodians of society were prone to consolidate their gains and institutionalize the procedures. An example of this progress is the rapid transition that followed from subjective to objective exchange.

Out of the cumbersomeness of barter and the variability of currency exchange was born a new and wonderful idea: the use of paper as a medium of exchange in the form of a "fair letter". Such a document projected payments of obligations to a future date which in effect involved an extension of credit. Settlement of accounts then could be cleared at other fairs largely through cancellation of debits and credits leaving only the balances to be settled by payment in the coin of the realm.

Even in this early period, creditors and debtors were vaguely conscious of the importance of a lapse of time between the dates when debts were contracted to the hour of their payment. Usury was not condoned by the church, so the money lenders resorted to a subterfuge. They extended credit of one sum and received a larger principal, *pour amour*. The difference ostensibly represented a gift from the debtors out of the goodness of their

hearts. In the due course of time, both churchmen and nobles fell on evil days. They became patrons of the money lenders; in fact, their needs were so great they absorbed the major portion of the business. Reynolds reports that the credit merchants were circumspect in their dealings with members of the clergy and the royalty. "These merchants in the overland trade were able and willing to advance funds to men from other classes. Churchmen of Northern Europe who needed money for expenses for themselves and their trains were able to borrow large lump sums from the merchants of Arras or Asti."[12] The merchants were content with short simple notes when lending large amounts to other merchants but were exceedingly careful to hedge in bishops and other churchmen with a whole array of oaths and pledges and guarantor's oaths.[13]

Eventually the church tolerantly ignored the practice of usury. Fixed rates of 10% or more for the use of money became established and accepted by the more sophisticated members of society. Thus, another barrier was cleared favorable to the diffusion of private property.

At the time the Lombards and the Genoese were plodding across the Alps to peddle their wares, other peninsular countrymen wandered off to the far end of the earth to discover new realms of trade in the far-flung empire of Kublai Khan. The chronicles of these travelers describing Mongol markets provide an interesting contrast with the concurrent Champagne fairs.

The Great Kinsay Market[14]

As a trade war raged between Genoa and Venice,

[12] Loans to Bishop Raoul or Rodulf of Liege and Walter, "electus" of Combrai were made by caravan merchants and financiers of Arras and Rome, respectively, in 1191 (ASG Not, Gugl. Cass., fols. 38, 68).

[13] Reynolds, "Genoese Trade in the Late Twelfth Century", pp. 378-379.

[14] Kinsay was formerly known as Lin-ngan now Hang-chan fu. It is also referred to as Kinsai, King-sze, Khansa, Khinsa, Kingsai, Khanzai, Cansay, and Campsay (City of Heaven).

1298, the Genoese captured a Venetian named Marco Polo who spent his time in jail writing a fabulous tale of his travels to the far east, the Orient. So fantastic was his account that it was widely read for amusement rather than studied as a valuable source of information. Other writings of contemporary travelers have been brought to light which substantially support the author's story of Kublai Khan's court and the customs in Cathay. That part of Marco Polo's book describing markets and commerce in the far east is significant both for the intensive and extensive development of market institutions in the Orient which surpassed anything existing in Europe in the medieval period.

"The position of the city is such that it has on one side a lake of fresh and exquisitely clear water, and on the other, a very large river. The waters of the latter fill a number of canals of all sizes which run through the different quarters of the city, carry away all impurities, and then enter the lake; whence they issue again and flow to the ocean, thus producing a most excellent atmosphere. By means of these channels, as well as by the streets, you can go all about the city. Both streets and canals are so wide and spacious that carts on the one and boats on the other can readily pass to and fro, conveying necessary supplies to the inhabitants.

"At the opposite side the city is shut in by a channel perhaps 40 miles in length, very wide, and full of water derived from the river aforesaid, which was made by the ancient kings of the country in order to relieve the river when flooding its banks. This serves also as a defense to the city, and the earth dug from it has been thrown inwards forming a kind of mound enclosing the city.

"In this part are the ten principal markets, though besides these there are a vast number of others in the different parts of town. The former are all squares of

half a mile to the side and along their front passes the main street, which is 40 paces in width, and runs straight from end to end of the city crossing many bridges of easy and commodious approach.[15] At every four miles of its length comes one of those great squares of two miles in compass. So also parallel to this great street, but at the back of the market places, there runs a very large canal, on the bank of which toward the squares are built great houses of stone in which the merchants from India and other foreign parts store their wares to be handy for the markets. In each of the squares is held a market three days in a week, frequented by 40,000 to 50,000 persons who bring thither for sale every kind of meat and gems, as a roebuck, red deer, fallow deer, hares, rabbits, partridges, pheasants, francolins, quails, fowls, capons, and of ducks and geese an infinite quantity; for so many are bred on the lake that for a Venice groat of silver you can have a couple of geese and two couple of ducks . . . . .

"Those markets make a daily display of every kind of vegetables and fruits . . . . .

"From the ocean sea also come daily supplies of fish in great quantity, brought 25 miles up the river, and there is also great store of fish from the lake . . . . Anyone who should see the supply of fish in the market would suppose it impossible that such a quantity could ever be sold; and yet in a few hours the whole shall be cleared away; so great is the number of inhabitants who are accustomed to delicate living. Indeed they eat fish and flesh at the same meal.

"All the ten market places are encompassed by lofty houses, and below these are shops where all sorts of crafts are carried on, and all sorts of wares are on sale, including spices and jewels and pearls. Some of these shops are entirely devoted to the sale of wine made from

[15] Variously estimated from 360 to 12,000 by different writers.

rice and spices, which is constantly made fresh, and is sold very cheap.

"In each of the squares are two great palaces facing one another, in which are established the officers appointed by the King to decide differences arising between merchants, or other inhabitants of the quarter. It is the daily duty of these officers to see that the guards are at their posts on the neighboring bridges, and to punish them at their discretion if they are absent.

"All along the main street that we have spoken of, as running from end to end of the city, both sides are lined with houses and great palaces and the gardens pertaining to them, whilst in the intervals are the houses of tradesmen engaged in their different crafts. The crowd of people that you meet here at all hours, passing this way and that on their different errands is so vast that no one would believe it possible that victuals enough could be provided for their consumption, unless they should see how, on every market day all those squares are thronged and crammed with purchasers, and with the traders who have brought in stores of provisions by land or water; and everything they bring in is disposed of.

"To give you an example of the vast consumption in this city, let us take the article *pepper;* and that will enable you in some measure to estimate what must be the quantity of victual, such as meat, wine, groceries, which have to be provided for the general consumption. How Messer Marco heard it stated by one of the Great Khan's officers of customs that the quantity of pepper introduced daily for consumption into the city of Kinsay amounted to 43 loads, each load being equal to 223 lbs., or ten and one-half short tons every market day."[16]

Excerpts from the reports and manuscripts of other

[16] Polo, Marco, "The Book of Ser Marco Polo, The Venetian, Concerning the Kingdoms and Marvels of the East," translated by Sir Henry Yule, Vol. II, pp. 200-204, Charles Scribner's Sons, New York, 1903.

travelers about the famed Kinsay market are herewith cited to add credence to Polo's observations. Even if the descriptions of Kinsay by the various writers possessed with an imagination of Oriental proportions are discounted liberally, it was still undoubtedly one of the principal cities of the Middle Ages.

Friar Odoric, a Venetian traveling through China about 1324-27, reported:

". . . It is the greatest city in the whole world, so great indeed that I should scarcely venture to tell of it . . . . It is a good hundred miles in compass, and there is not in it a span of ground which is not well peopled. And many a tenement is there which shall have 10 or 12 households comprised in it. And there be also great suburbs which contain a greater population than even the city itself . . . But if anyone should desire to tell all the vastness and great marvels of this city, a good quire of stationery would not hold the matter, I trow. For tis the greatest and noblest city and the finest for merchandise that the whole world containeth."[17]

Wassaf sings his praises of the city in the following words:

"Khanzai is the greatest of the cities of Chin, 'Stretching like Paradise through the breath of Heaven.' Its shape is oblong, and the measurement of its perimeter is about 24 parasangs. Its streets are paved with burnt brick and stone. The public edifices and the houses are built of wood and adorned with a profusion of paintings of exquisite elegance . . . . The length of the chief streets is three parasangs, and the city contains 64 quadrangles corresponding to one another in structure, and with parallel ranges of columns. The salt excise brings in daily 700 *balish* in paper-money. The number of craftsmen is so great that 32,000 are employed at the dyer's art alone; from that fact you may estimate the rest . . . .

[17] Ibid., pp. 212-213.

Amid the city there are 360 bridges erected over canals ample as the Tigris, which are ramifications of the great river of Chin; and different kinds of vessels and ferry-boats, adapted to every class, ply upon the waters in such numbers as to pass all powers of enumeration . . . The concourse of all kinds of foreigners from the four quarters of the world, such as the calls of trade and travel bring together in a kingdom like this may easily be conceived."[18]

Another citation is taken from Ibn Batuta:

"This city is the greatest I have ever seen on the surface of the earth. It is three days' journey in length, so that a traveler passing through the city has to make his marches and halts! . . . It is subdivided into six towns, each of which has a separate enclosure while one great wall surrounds the whole . . ."

The Great Russian Fair of Nizhni Novgorod

About the time King Philip began meddling with the administrative machinery of the Champagne fairs, causing their decline, the last great medieval fair of Europe was being formed at the shrine of St. Macarius, a place of pilgrimages. Eventually, the fair became so important, the Czar sequestrated the right of collecting tolls from the monks by relocating it in a small city now named Makarevski a few miles away from the original monastic site.

For almost 200 years (1624-1816) the Makarevski fair prospered, much like other fair towns throughout Russia, but in 1816 it was swept with a disasterous fire wiping out the town and all the fair facilities.

Czar Alexander I (Pavlovich) decided to relocate the fair 50 miles to the east at the confluence of the Volga and Oka Rivers where the city of Gorki (Nizhni Novgorod) is now situated. This location is only 250 miles

[18] Ibid., pp. 213-214.

east of where these rivers empty into the greatest navigable river in Russia, the Volga. The Kama River and its tributaries comprise a navigable system totaling 7500 miles extending north and east draining the western slopes of the Ural Mountains. The Oka River flows east and north for 275 miles from the environs of Moscow to join the Volga at Nizhni Novgorod. The headwaters of the "river of song" — the Volga — lie far to the northwest of Moscow toward the Baltic region. It flows east to Kazan and thence south into the Caspian Sea — a distance of 2300 miles.

When the fair was in season, some 14,000 boats plied the waters of the Volga above Novgorod, and as many as 8,000 ships manned by nearly a quarter million hands navigated the Kama and the Volga Rivers to the south and east of Nizhni Novgorod. Warehouses and places of storage lined the river banks for miles above and below the fairgrounds, and the river teemed with craft moving cargoes in and out of the market area.

The Nizhni Novgorod fair was the last survivor of the European medieval market fairs to withstand the march of progress, and it was also the greatest river-border fair of all time, both in scope of operation and in degree of influence upon Eurasian trade. It attracted for purposes of trade and entertainment Slavs and Tartars and Moslems and Christians. It formed the common ground where the traders of the east could meet the merchants from the west to establish prices and clear huge stocks of surplus productions from two continents primarily by direct barter. Credit was used only to a limited extent and contracts for future delivery were practically non-existent. The fair was also geographically centered in a vast area of Russian home industries connected by navigable waterways for cheap transportation of basic raw materials.

Decennial Volume of trade at the Nizhni Novgorod Fair

Year	Approx. Value of Merchandise (Millions of Rubles)[19]
1820	32
1830	35
1840	48
1850	60
1860	105
1870	143
1880	200
1890	181
1900	146
1910	199
1920	Closed by war (Revolution) and reopened in 1923
1928	271
1930	Closed by decree

During the 100 year period from 1820 to 1920, trade in Russia was cleared through about 18,000 fairs. Some of the pivotal regional fairs constituting the Russian market grids in that period are listed with pre-war estimates of their sales volume in millions of rubles: Peron 25; Irbit 20; Minsk 20; Grenburg 14; and Pokrov 11. Some other fairs of regional importance were: Omsk, Ishim, Riga, Kiev, and Baku.

A further analysis of trade at the Nizhni Novgorod fair is presented in the table below giving an itemized account of sales in millions of ruble over a 40 year period.

Items	Average Volume of Sales (Millions of Rubles)			
	1870	1890	1895	1909
Cotton and cotton goods	25.0	25.0	56.0	00.0
Wool and woolen goods	17.0	17.0	13.0	19.2
Linens (flax and hemp)	3.5	4.2	3.3	5.2
Silks	7.0	5.5	1.2	2.3
Furs	7.0	8.5	13.6	25.0
Hides and leather goods	5.5	7.5	10.0	20.5
Metal wares	10.0	22.0	24.0	4.0
Fish	4.0	5.3	3.2	5.5
Sugar	3.7	2.8	1.3	0.4
Tea	8.4	14.6	15.0	6.0

[19] The prewar value of the ruble was about $.515. No adjustment was made in these figures for the changing value of the ruble throughout the century covered.

The fair was officially opened on July 15 by a bishop of the Russian Orthodox Church celebrating Mass and it was closed August 25 with appropriate religious services. The business of buying and selling, however, really began in June among some merchants and shopkeepers and it continued until about September 15. It appears that most of the transactions were struck in a leisurely and amiable manner while the merchants discussed terms over a cup of tea. Such verbal contracts were sealed with a handshake. The members of this trading community retained control over their affairs by meeting in general assembly a few times during the fair season.

A number of factors account for the decline of Russian fairs toward the end of the 19th century. The completion of the transcontinental railroad through Siberia and the establishment of differential tariffs caused sugar to be moved directly from Moscow to Siberia. Iron was shipped to various parts of the country by rail from the Urals. Persian goods began moving overland on the new railroad connecting Tashkent, Chkaloff (Grenburg) and Samara to points nearer the ultimate consumers. The development of a railway system in the south of Russia intercepted such of the goods that formerly flowed indirectly through the fairs. Distribution by rail to local markets and shopkeepers was more direct, quicker and cheaper than via river boats to central fairs thence to the local communities by devious routes through several tiers of middlemen. Local manufacturers began selling more wares directly by description or by sample as the means of communication improved. Finally, the program of socialization sounded the death knell to the reign of free trading in the festival atmosphere of the market fairs.

Parallelism of Market Organization and Significance of the Market Fairs

One of the characteristics of medieval trade is the

rather sharp demarcation between domestic bartering in the local markets and inter-regional exchange at the fairs. In some periods there seem to be only a tenuous relationship or coordination between the two avenues of trade. The commodities offered in the two market systems were different. The personnel of the one held nothing in common with the other and the methods of management were distinct. It is from the institution of medieval fairs and the procedures evolved in their administration that we have inherited so many embryonic ideas which formed the basis for our modern market institutions.

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Appendix A

THE COMMODITY EXCHANGE ACT[1]

This is the Federal law which regulates futures trading in agricultural commodities on 18 commodity futures markets.

The act is based upon the power of Congress to regulate interstate commerce. Its constitutionality was upheld by the United States Supreme Court in 1923.

In effect, the law provides that all futures transactions in commodities covered by the act must be made on an exchange designated as a contract market.

The act prohibits undesirable practices and transactions, such as:

Price manipulation and cornering of a commodity.
Cheating or defrauding of customers.
Making false reports to customers.
Disseminating false crop or market information.
"Bucketing" of orders, and bucket shops.
"Wash" sales and other fictitious transactions.
"Puts," "calls," or "privileges."[2]

Any exchange or board of trade desiring to conduct a futures market in any commodity named in the act must first be designated by the Secretary of Agriculture as a "contract market," and must conform with requirements specified in the act.

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[1] Following is an abridged version of the act. The full text as amended and rules and regulations pertaining thereto can be obtained from the Secretary of Agriculture U. S. D. A., Washington 25, D. C.

[2] Exerpts from Leaflet No. 330 issued by the U. S. D. A.

To be Designated as a Contract Market, an Exchange must meet Certain Conditions, Including:

Location at a terminal market, with sufficient cash sales to reflect values, and an official inspection service approved by the Secretary of Agriculture.[3]

Provision for keeping records and filing reports prescribed by the Secretary.

Provision for prevention of price manipulation and cornering and the sending out of false or misleading crop or market information by the exchange or its members.

Admission of cooperatives to membership on equal terms with others.

Futures Commission Merchants and Floor Brokers Must be Registered.

All persons who handle or execute orders for others must register each year with the Secretary of Agriculture. This includes such traders as:

Futures Commission Merchants (commonly referred to as brokerage firms), including individuals, associations, partnerships, corporations, and trusts engaged in soliciting or in accepting orders to buy or sell commodity futures, and

Floor Brokers, who execute orders for others in the trading "pit" or "ring" on an exchange floor.

Customer's Funds are Protected.

A futures commission merchant must keep customers' funds separate from his own capital.

He may not use customers' funds in his own business.

He may not use funds belonging to one customer to finance the trades of another customer.

He may deposit customers' funds in a bank or invest them in certain kinds of securities.

[3] An exchange located elsewhere is eligible if it provides for deliveries of commodities at a delivery point or points and on conditions approved by the Secretary of Agriculture.

The Commodities Covered are Specified.

The act defines "commodity" to mean wheat, cotton, rice, corn, oats, barley, rye, flaxseed, grain sorghums, mill feeds, butter, eggs, Solanum tuberosum (Irish potatoes), wool tops, fats and oils (including lard, tallow, cottonseed oil, peanut oil, soybean oil, and all other fats and oils), cottonseed meal, cottonseed, peanuts, soybeans and soybean meal.[4]

Limits are Placed on Large-Scale Speculation.

The act authorizes the fixing of limits on the amount of speculative purchases or sales by a person on one day and the amount of his speculative holdings of futures.

Two Means of Dealing with Violations are Stipulated.

Criminal proceedings: Violations of certain sections of the Commodity Exchange Act are criminal offenses, and proceedings may be instituted in a United States District Court. Upon conviction, a person may be fined not more than $10,000 and imprisoned for not more than 1 year, or both.

Administrative proceedings before the Secretary of Agriculture: Any person who is found, after hearings, to have violated any provision of the act may be denied trading privileges on all contract markets by the Secretary of Agriculture. The Secretary may also suspend or revoke the registration of futures commission merchants or floor brokers found guilty of violating the act. Orders of the Secretary may be appealed to a United States Court of Appeals.

[4] No new commodities have been added to this list by the Commodity Exchange Authority since October 9, 1940. (3/3/53).

Appendix B

THE COMMODITY EXCHANGE AUTHORITY

It is an agency of the U. S. Department of Agriculture acting for the Secretary of Agriculture in the administration and enforcement of the Commodity Exchange Act. The act confers upon the Secretary of Agriculture the principal powers for enforcement of the law, including authority to issue rules and regulations to carry out its provisions.

It also acts for the Commodity Exchange Commission, consisting of the Secretary of Agriculture, the Secretary of Commerce, and the Attorney General, which has certain responsibilities under the act, principally with respect to fixing of limits on speculative trading by any person and to violations of the law by contract markets.

Its headquarters is in Washington, D. C., and its field offices are in Chicago, New York, New Orleans, Kansas City, and Minneapolis.

Enforcement of the Commodity Exchange Act involves five principal kinds of work.

1. Contract Markets are Designated and all Brokers are Registered.

An exchange wishing to conduct futures trading in a commodity must make an application. This is reviewed to insure conformity with the act before the exchange is designated as a contract market for the commodity.

All new or proposed rules, regulations, and bylaws of contract markets are examined to see that they are not contrary to the act.

Each year applications of futures commission merchants and floor brokers are received and registrations issued.

2. Brokerage Firms Records are Audited.

To prevent misuse of customers' funds and see that separate accounting records are kept and the funds segregated, accountants of the Commodity Exchange Authority make audits of the books of futures commission merchants.

3. Questionable practices and Violations of the Act are Under its Scrutiny.

Instances may occur in which customers are cheated or defrauded, and sometimes there are cases of bucketing of customers orders, "wash" or fictitious trades, or other illegal practices.

Some traders may attempt to manipulate or move futures prices up or down artificially to their own advantage, or to corner the market.

Transactions or practices which appear to be in violation of the act are brought to light in various ways — through complaints, audits of books and records, examination of reports, special trade practice surveys of exchange trading, and other means.

4. Supervision Over Daily Trading.

Constant watch is kept over operations and conditions in the futures markets to preserve their open competitive status. This constant watch is a way of learning quickly about unusual market conditions. It reveals from the early stages, for example, the build-up of large traders' positions, which unchecked may result in price manipulation, corners or "squeezes."

Daily reports by futures commission merchants give the total amount or volume of trading and the open contracts in each future and commodity. Reports by large traders give detailed facts on their operations. Figures on prices, deliveries on futures contracts, stocks of cash commodities, and other basic facts affecting the futures market are brought together.

This system of reports provides the basis for the release of factual data on futures trading. Such data were not available to the public until Federal regulation began. Releases are issued daily giving the figures on volume of trading and open contracts. These are carried regularly by wire services and newspapers.

5. Limits on Speculation by Large Traders.

As one means of preventing large-scale operations by market "plungers," the Commodity Exchange Act amendments of 1936 authorize the Commodity Exchange Commission to fix limits on the amount of any person's speculative trading and open contracts. In the following years evidence prepared by economists and trading analysts of the Commodity Exchange Authority on the effects of large-scale trading in various commodities upon prices was given at public hearings of the Commodity Exchange Commission. The limits, specify fixed amounts in bushels, bales, or carlots, in general prevent an individual trader from having trades or positions amounts to more than 2 or 3 percent of all open contracts.[5]

[5] For a more detailed description of the functions and services of the Commodity Exchange Authority read "Commodity Exchange Act as Amended" and the rules and regulations of the Secretary of Agriculture promulgated thereunder. Revised August 13, 1952, U. S. D. A.

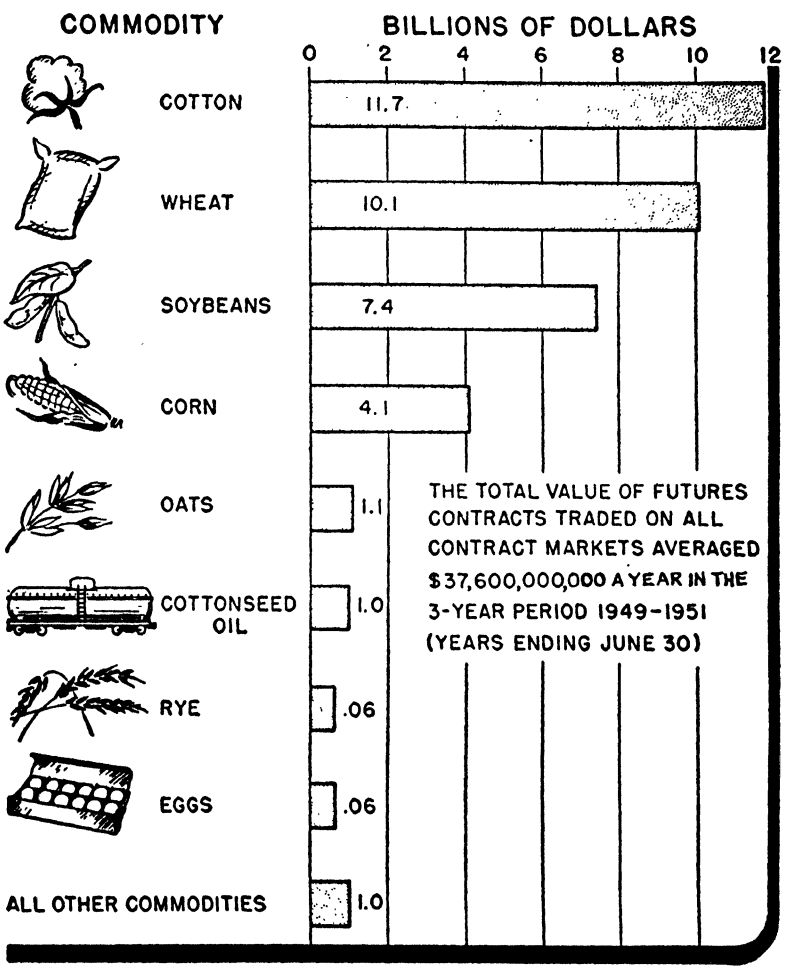
VALUE OF FUTURES TRADING SUPERVISED
BY THE COMMODITY EXCHANGE AUTHORITY
OVER $37 BILLION ANNUALLY
COMMODITY
BILLIONS OF DOLLARS
0
2
4
6
8
10
12
COTTON
11.7
WHEAT
10.1
SOYBEANS
7.4
CORN
4.1
OATS
1.1
COTTONSEED OIL
1.0
RYE
.06
EGGS
.06
ALL OTHER COMMODITIES
1.0
THE TOTAL VALUE OF FUTURES CONTRACTS TRADED ON ALL CONTRACT MARKETS AVERAGED $37,600,000,000 A YEAR IN THE 3-YEAR PERIOD 1949-1951 (YEARS ENDING JUNE 30)

Figure 6

Appendix C

COMMODITY MARKETS

Commodity	*Date Futures Trading Began*	*Name of Exchange*
Provisions	1850-59	Chicago Board of Trade
Wheat	1850-59	Chicago Board of Trade
Corn	1850-59	Chicago Board of Trade
Oats	1850-59	Chicago Board of Trade
Rye	1850-59	Chicago Board of Trade
Field seeds	1862	Toledo Board of Trade[1]
Wheat	1864	Milwaukee Chamber of Commerce[2]
Corn	1864	Milwaukee Chamber of Commerce
Oats	1864	Milwaukee Chamber of Commerce
Rye	1864	Milwaukee Chamber of Commerce
Wheat	1870	New York Produce Exchange
Cotton	1870	New York Cotton Exchange
Wheat	1872	St. Louis Merchants Exchange
Corn	1872	St. Louis Merchants Exchange
Wheat	1880	Chicago Open Board of Trade
Corn	1880	Chicago Open Board of Trade
Oats	1880	Chicago Open Board of Trade
Rye	1880	Chicago Open Board of Trade
Cotton	1880	New Orleans Cotton Exchange
Coffee*	1882	New York Coffee and Sugar Exchange
Wheat	1885	Duluth Board of Trade
Rye	1885	Duluth Board of Trade
Barley	1885	Duluth Board of Trade
Wheat	1890	Minneapolis Chamber of Commerce[3]
Oats	1890	Minneapolis Chamber of Commerce
Rye	1890	Minneapolis Chamber of Commerce
Flaxseed	1892	Duluth Board of Trade

Commodity	*Date Futures Trading Began*	*Name of Exchange*
Wheat	1899	Kansas City Board of Trade
Corn	1899	Kansas City Board of Trade
Oats	1899	Kansas City Board of Trade
Wheat	1904	Omaha Grain Exchange[4]
Cottonseed oil	1904	New York Produce Exchange
Barley	1912	San Francisco Chamber of Commerce[5]
Sugar*	1914	New York Coffee and Sugar Exchange
Barley	1917	Los Angeles Grain Exchange[6]
Butter	1919	Chicago Mercantile Exchange
Eggs	1919	Chicago Mercantile Exchange
Flaxseed	1920	Minneapolis Chamber of Commerce
Cotton	1924	Chicago Board of Trade
Butter	1925	New York Mercantile Exchange
Eggs	1925	New York Mercantile Exchange
Cottonseed oil	1925	New Orleans Cotton Exchange
Cocoa*	1925	New York Cocoa Exchange
Wheat	1926	Seattle Grain Exchange
Rubber*	1926	Rubber Exchange of New York[7]
Silk*[8]	1928	National Raw Silk Exchange (New York)[7]
Tin*[8]	1928	National Metal Exchange (New York)[7]
Wheat	1929	Portland Grain Exchange
Cottonseed	1929	Memphis Merchants Exchange Clearing Association
Cottonseed meal	1929	Memphis Merchants Exchange Clearing Association
Copper*	1929	National Metal Exchange (New York)[7]
Hides*	1929	New York Hide Exchange
Mill feeds	1929	St. Louis Merchants Exchange
Wool Tops	1930	(Wool Associates) New York Cotton Exchange
Live hogs*[8]	1930	Chicago Livestock Exchange
Potatoes	1931	Chicago Mercantile Exchange
Silver*[9]	1931	National Metal Exchange (New York)

Commodity	*Date Futures Trading Began*	*Name of Exchange*
Molasses*	1931	New York Coffee and Sugar Exchange
Bran	1932	Kansas City Board of Trade
Shorts	1932	Kansas City Board of Trade
Zinc*	1934	Commodity Exchange Inc.
Lead*[7]	1934	Commodity Exchange Inc.
Soy beans	1936	Chicago Board of Trade
Frozen eggs	1937	Chicago Mercantile Exchange
Black pepper*	1937	New York Produce Exchange
Potatoes	1941	New York Produce Exchange
Wool, grease	1941	(Wool Associates) New York Cotton Exchange
Onions*	1942	Chicago Mercantile Exchange
Grains sorghums	1944	Kansas City Board of Trade
Dressed turkey*	1945	Chicago Mercantile Exchange
Apples*	1948	Chicago Mercantile Exchange
Dressed poultry*	1949	Chicago Mercantile Exchange
Rice	1949	New York Mercantile Exchange
Soy bean oil	1950	Chicago Board of Trade
Soy bean meal	1951	Chicago Board of Trade

*Not designated as a contract market under Commodity Exchange Authority since these commodities are not included in the listing under the Commodity Exchange Act.

[1] Ceased operations.

[2] Known as the Milwaukee Grain Exchange since 1946.

[3] Changed to Minneapolis Grain Exchange in 1947.

[4] Suspended December 7, 1932 as a Grain Futures Market, but cash trading in grain continues.

[5] Name changed to San Francisco Grain Exchange.

[6] This contract market was vacated by order of the Secretary of Agriculture on February 9, 1953 effective May 1, 1953.

[7] Four exchanges dealing in rubber, silk, metals, and hides were merged into one organization now known as the Commodity Exchange, Inc., New York.

[8] Trading suspended before World War II and not resumed to date (1953).

[9] Trading suspended in 1934 when silver was nationalized and a prohibitive transaction tax was imposed.

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