Opinion

Evil Empire?

BY CHARLES GERENA

We are a nation built on capitalism. Americans value progress and venerate the entrepreneurs who blaze new trails in the pursuit of profits.

As a nation born of revolution, however, we also distrust any institution that gets too big for its britches. Entrepreneurs from Andrew Carnegie to Bill Gates became magnets of criticism as their once-fledgling companies grew into corporate behemoths.

The truth is big business is neither a bully nor a benefactor. Its goal is to make money. In the process, it tends to serve its own interests as well as those of consumers. However, not all firms conduct themselves in ways that the public deems socially acceptable.

America's love-hate relationship with big business predates the appearance of the first Wal-Mart discount store. The late 1800s saw the rise of industrial powerhouses like Standard Oil and U.S. Steel. Magnates such as John D. Rockefeller and J.P. Morgan profited as wealth became more concentrated and fears of diminishing market competition grew.

However, they weren't supposed to be the only ones made better off by industrial concentration. This was supposed to be good for society in general. Morgan Witzel, in his introduction to an edited volume titled *Big Business and the Muck-Rakers, 1900-1910*, explains the mindset at the time: "Without the need to compete and spend money fighting off business rivals, corporations could concentrate on becoming more efficient, reducing costs, and providing cheaper goods to the public."

Things didn't turn out that way, though. Many prices didn't fall and inefficiencies remained. On top of that, labor unrest increased and scandals over worker safety and product quality made the headlines of muckraking magazines like *McClure's*. Also, some companies, particularly railroads, used their economic power to garner favorable treatment by lawmakers.

Fast-forwarding to the 1980s, corporate raiders like Carl Icahn and Boone Pickens led hostile takeovers of companies and carved their acquisitions into pieces to sell off at a quick profit. While businesses across America consumed a lot of time and money to keep these wolves at bay, some argue that many weak operations were eliminated, which executives may never have shuttered.

Then there was the spate of corporate scandals of the late 1990s and early 2000s. Companies like Enron, WorldCom, and Adelphia Communications based their growth on questionable accounting practices and financial arrangements obscured from public scrutiny. Eventually, their actions were uncovered, undermining trust in their companies and leading to criminal investigations of CEOs and CFOs.

At this point, you may be wondering: "I thought he said big business wasn't inherently evil? It sure sounds like that's the case."

Well, it isn't. Once a company reaches a certain size, it can reduce its average total costs over the long run by employing machinery that is more efficient, dividing processes and assigning them to specialized workers, and earning discounts on bulk purchases. Such economies of scale enable companies to lower their prices for goods and services, which benefits the consumer.

This alludes to another aspect of becoming big — it is often the result of consumers rewarding a company for giving them what they want. If some firms can satisfy their customers more effectively than their rivals, they will sell more, resulting in increased concentration in an industry.

Microsoft, for instance, now controls an overwhelming share of its market. While the company's current size may dampen its incentive to be innovative, who could really think that we would be better off without its products?

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Rather than focus on "bigness," perhaps we should think about why businesses, large or small, go astray. For example, one could argue that excessive regulation provides an incentive for companies to seek out shortcuts that skirt the edge of ethical behavior. Such regulation also may create barriers to entry for new companies.

The more important issue may be the complexity of a company rather than its size. "... Innovative financing techniques have made it more difficult for outside investors to understand a particular firm's risk profile and the performance of its various lines of business," noted Fed Governor Susan Schmidt Bies in a February 2004 speech. "Traditional accounting standards have not kept pace with the risk-management tools employed by sophisticated corporations." Bies suggested that improved corporate transparency would help market participants gauge a company's strategies and actions.

Ultimately, markets exist to optimize the use of scarce resources and produce what people value most. They are concerned with efficiency, not morality. Therefore, consumers must serve as the moral compass of Corporate America. The executives in charge may be obligated to make money for shareholders, but they have to satisfy consumers in order to meet that goal. In the ideal marketplace, good behavior will be rewarded and bad behavior will be punished. **RF**