Activity 24.1
John D. Rockefeller: No One Loves a Competitor

John D. Rockefeller was an entrepreneur who sensed an opportunity waiting to be grasped. To grasp it, he set about bringing organization and efficiency to the emerging U.S. petroleum industry. He did this by figuring out how to cut costs. Cutting costs allowed him to reap personal benefits and pass some of the savings along to consumers. The rewards for his many innovations were great. He became a very wealthy man.

Seeking Less Expensive Lighting

The U.S. petroleum industry became increasingly important during the nineteenth century because it provided substitutes for whale and coal oil then used for lighting. Edwin Drake had discovered that petroleum could be pumped successfully from oil wells. Consumer interest in whale oil, already declining, continued to drop as the desirability of less expensive kerosene, produced from petroleum, increased. By the 1880s, kerosene had replaced whale and coal oil as consumers' fuel of choice.

But the petroleum industry in the 1860s was filled with uncertainty. Prices varied wildly as businesses experimented with ways of drilling, refining and transporting oil. Much confusion existed about which technologies would be best.

Reducing Costs

Rockefeller entered the uncertain environment of the oil business in Cleveland in 1862. He quickly recognized that many cost-savings could be achieved. Soon he bought out the partners of his firm and made changes in production that would reshape the industry.

Perhaps Rockefeller's greatest innovations were in the area of transportation. It was there that he managed to get ahead and stay ahead of his competition. Oil in those days was hauled in barrels. Loading and unloading barrels of oil took time and was therefore expensive. Rockefeller substituted railroad tank cars for barrels to carry oil. Because of his potential to be a high-volume customer, he was able to pressure (or negotiate with) the railroads in order to get favorable prices (rebates) for shipping his oil. These pricing agreements had the effect of reducing his costs and allowing him to sell at prices lower than those of his competitors.

Rockefeller and his associates established Standard Oil Company in 1870. Within a decade, Standard Oil owned major refineries in Cleveland, New Jersey, Pittsburgh and Philadelphia. In 1882, Rockefeller organized the Standard Oil Trust. Standard Oil developed a pipeline system, purchased new oil fields and created new ways to market its products. Rockefeller then controlled most refining and distribution of oil in the United States, and he also controlled much of the world's oil trade.

Because of the innovations Rockefeller employed, Standard Oil's transportation costs dropped like a stone. Prices to consumers followed the same path. The price of petroleum dropped from 36 cents a gallon in 1863 to 8 cents a gallon in 1885.

The Criticisms of Rockefeller

Newspapers at the time portrayed Rockefeller as a cutthroat competitor, and many historians have stated the same criticism. Rockefeller was accused of using ruthless tactics to drive out his competition. Was he a ruthless competitor? Let's examine the logic of the case. If the point is that he was in front of his competitors in finding ways to cut costs and lower prices — if that's being a ruthless competitor — then the answer is a clear yes. Rockefeller and his associates did benefit from undercutting their competitors, but consumers benefited, too. By about 1890, most Americans could afford kerosene lighting.

Some business people claimed at the time that Rockefeller competed unfairly. They accused

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Rockefeller of "dumping" oil or selling it below his costs in order to drive them out of business. Does this charge make sense? Standard Oil owed much of its success to reducing costs. Rockefeller could not have sold oil below his costs for very long. If he had, he would have been forced out of business. Rather, through the use of tank cars and pipelines, he developed ways to reduce his costs sharply. This allowed him to sell oil at prices below those of his competitors. Who benefited from lower costs and prices? Standard Oil and consumers of kerosene and other oil products. Who was hurt from lower costs and prices? Producers unable to compete and consumers who otherwise might have experienced still lower prices from greater competition in the oil industry.

Another charge is that Rockefeller forced other firms to join him. Rockefeller is described as shamelessly selling at lower prices in order to force reluctant firms to join his emerging monopoly. Rockefeller's competitors had little choice, according to this view. This charge overlooks the fact that most of the firms Rockefeller acquired approached him and asked to be acquired. We can speculate about the conditions leading up to these appeals. However, it is clear that Rockefeller's competitors realized that they could not compete successfully with him. His costs were lower. They wanted to avoid going broke. They hoped that in combination with Rockefeller they could stay in business and eventually gain wealth. The owners of these firms concluded that it was to their advantage to join the competition while their businesses were still attractive.

Breaking It Up

The Standard Oil Trust that Rockefeller established was found to be illegal under the Sherman Anti-Trust Act of 1890. The Sherman Anti-Trust Act prohibited businesses from acting in combination to restrict competition. Standard Oil continued to operate as a holding company called Standard Oil of New Jersey until 1911, when the U.S. Supreme Court ordered the firm dissolved.

Giving It Away

While Rockefeller has often been attacked for his business tactics, he is often praised for his generous and far-sighted philanthropy. He gave away $550 million during his lifetime. The legacy of his giving might be familiar to you. He formed the Rockefeller Foundation and Rockefeller University. He helped found the University of Chicago in 1890. He was responsible for the renovation of Williamsburg, Virginia. He funded the restoration of Versailles in France. He acquired the land that eventually became Grand Teton National Park in Wyoming. These are just a few of the endeavors that he supported.

QUESTIONS FOR DISCUSSION

A. What innovations did Rockefeller introduce in the U.S. oil industry?

B. Why is Rockefeller regarded by some as a cutthroat competitor?

C. Do you think the criticism is justified?

D. Rockefeller was praised for his philanthropy. Was this his most important economic contribution?