

## 150 A Trust Is Born

In the 1870's and 1880's, the rapid growth of American industry was greatly spurred by the trend toward business consolidation, or combination. Companies used this form of business organization to gain control of a large part of the market in a certain industry—for example, oil. When the corporations in an industry joined together into one large trust, they gained many advantages. The large size of the trust enabled it to take advantage of the money-saving techniques of mass production and cheap marketing. The trust also could limit production, fix prices, and secure lower railroad rates. Trusts were so effective that they were able to drive out most competition and establish a monopoly or near-monopoly. The American tobacco trust, formed by James Buchanan Duke, was a good example of how such a giant business combination worked.

### READING FOCUS

1. What methods did Duke use to make his business successful?
2. After the trust was formed, what techniques were used to dominate the market?

It became evident that any business that might develop a wide market for its product would end up in a financier's hands. Entrepreneurs themselves might become financial tycoons, as was the case with James B. Duke. For if money could be made by supplying consumers with goods and services, much more could be made by controlling stocks and bonds. Duke and his tobacco empire are striking not so much for size or importance of product, but because they show the methods that were used in bringing together various branches of a new industry and the way in which a new technology—mechanized cigarette-making—could promote consolidation.

Tobacco had been an important plantation crop before the Civil War. After the war, John Ruffin Green sold tobacco under the trade name of "Bull Durham." (It was named after Durham, North Carolina, the town in which it was processed.) The picture of the bull became a well-known trademark that Blackwell and

Carr, who took over after Green, fought to protect. They learned quickly that testimonials and advertising were essential in convincing the consumer to smoke their tobacco or buy their chewing plug. By 1884 the Blackwell and Carr factory had become the largest in the world. Soon many brands of tobacco were being produced in Durham. Those who processed the tobacco were determined to make the city the tobacco capital of the South.

However, the North Carolina town of Winston, near the sleepy village of Salem, soon began to rival Durham as a center for manufacturing tobacco products. One of the aggressive young salesmen in that area was R. J. Reynolds, who headed a family firm there. Lewis Ginter and John Allen had a thriving business in Richmond. Liggett and Myers was a growing firm in St. Louis. There was a great demand for tobacco all over the nation. Chewing and smoking brands were produced in ever-increasing quantities to satisfy it. Concerned with the protection of their trademarks, which clearly distinguished one brand from another, manufacturers passed out premiums and coupons. They gave rebates to dealers, and paid bribes to put their brands in certain stores.

It was not long, however, before Buck Duke would take over all the others. Born in 1856, James Buchanan Duke was named after the Democratic President elected in that year. Duke's father had been a small farmer before the Civil War. Afterward he returned to the land to grow and sell tobacco. His little tobacco curing factory grew steadily. By 1872 it was producing 125,000 pounds [577,000 kilograms] of tobacco a year. In 1874 the elder Duke and his two sons, James and Ben, moved the factory to Durham. The elder Duke took both boys in as partners to form W. Duke & Sons. To obtain more capital, several partners from outside the firm were brought in.

Cigarettes had been popular in Europe for many years, though in America they could not yet compete with plug and smoking tobacco. But Duke felt that he was hitting his head against the stone wall of Bull Durham. Blackwell and Carr had moved far ahead of their rivals in selling plug and smoking tobacco. Duke knew that he could not compete with them, and so he decided on cigarettes. But these had to be rolled by hand. Although Duke had some of the best workers in the business,

*From The Potentates by Ben B. Seligman.*

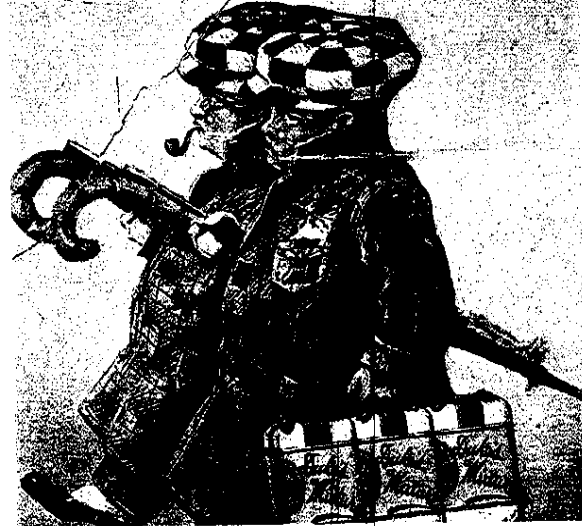
their output was still too small for an expanding market. Then the Dukes obtained a cigarette machine, which could turn out 120,000 cigarettes a day. Realizing that cigarettes were popular in cities, Duke set up a branch in New York. He successfully competed with the better-known firm of Ginter and Allen. He gave premiums and matched Ginter ad for ad. A favorite selling method was to place a picture of a pretty girl in each package of cigarettes. He sent clever salespeople on the road to find business. People were hired to go from store to store asking only for Duke's product. Incoming immigrants were given free cigarettes at ports of entry. By 1890 W. Duke and Company had become first in the tobacco industry.

Meanwhile, Duke was watching developments in oil, steel, whisky, and sugar. All were being combined through trusts. Why not tobacco? But first one had to get into the good graces of financiers. Duke began to negotiate for small thirty-day or sixty-day loans with New York bankers, always paying them back promptly. Soon Duke had established a line of credit with the powers that counted.

Finally, Duke was able to convince four other large companies that they all ought to get together. In 1890 the American Tobacco Company was started, a combination of Duke, Ginter, and three others. This was 90 percent of the cigarette industry. Capitalization was set at \$25,800,000, though the combined tangible assets were just slightly over \$3,000,000. Eight years later another company was formed to handle plug tobacco. Dealers were forced to take other items through tie-in sales. If they wanted cigarettes, they had to also take the trust's tobacco plug.

American Tobacco continued to expand by all means available, some fair, many unfair. Almost absolute control over cigarette-making machinery was worked out. Dealers refusing to take the trust's products were blacklisted and subjected to ruinous price wars. Through all these operations, Buck Duke ruled with an iron hand. He fired his star salesman, Edward Small, when he refused to move his family to Cincinnati. By 1905 American Tobacco and its related Consolidated Tobacco Company, both headed by Duke, controlled three fourths of the smoking-tobacco, and over nine tenths of the snuff, in addition to having almost complete control of the cigarette market.

Four other firms were taken over in the



An advertisement for James Duke's "Trust"

early 1890's. Liggett and Myers was then taken over. In 1899 it was R. J. Reynolds' turn to join the trust.

Stocks and bonds were controlled to yield a profit to insiders. Operations were always carried out in secret. Duke used several techniques to dominate the market. One was price-cutting. Another was to form phony "independent" companies to make it look as though there were competition. Duke also offered premiums and rebates, created rival brands to confuse consumers, and took over more competitors. Once a market had been won, retail prices were kept at the same level, while the jobber was squeezed with higher wholesale prices.

Nor was the foreign market neglected. Duke tried to get his products into Japan, but the government there decided to set up its own monopoly. He bought a factory in England, but the Imperial Tobacco Company was formed so British manufacturers could protect English people against American cigarettes. After several years of conflict, the usual cartel agreement [a cartel is an international trust] was reached. The United States and Cuban markets were given to Duke, Great Britain was given to Imperial, and the rest of the world was shared through the British-American Tobacco Company. The entire industry, with the exception of cigar-making, was now controlled by the "Tobacco Trust."

### READING REVIEW

1. Why was the cigarette-making machine so crucial to James Duke's business success?
2. List the steps and decisions that led to the establishment of the "trust".