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Chapter Title: The Rise of Academic Economists before World War I

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1 : : The Rise of Academic Economists before World War I

Academic economists are so prominent in the making and execution of economic policy that it is easy to take their role in the operation of the modern welfare state for granted. However much of a compliment such acceptance might appear to be, it slights the role of economists as contributors to the creation of the welfare state and as a group of professionals who generated public demand for their expertise. The rise of academic economists to their current prominence in public life did not happen overnight. We begin by describing some aspects of the evolution of the economics profession in the United States and the large role played by academic economists in the design and triumph of the welfare state.

Academic economists had little impact on the economic policies of federal and state governments during the first three-quarters of the nineteenth century. This absence of influence is not explained merely by the prevalence of laissez-faire doctrine. Nor is it explained by the lack of involvement of government in economic matters or the lack of instruments through which federal and state governments might have intervened in economic affairs. Quite the contrary, economic policy was central to politics throughout the nineteenth century. Among the issues debated and acted on were tariffs; taxes on property, sales, and income; banking policy; the promotion of internal improvements (roads, railroads, and waterways); government action to ameliorate business cycles; reduction of the labor supply through control of immigration; pensions for veterans; land distribution; the subsidization

of education; and unemployment compensation, workers' compensation, gender differences in pay and occupations, and other aspects of the alleviation of poverty.

By and large, the theorists of and experts on these issues before the Civil War were not academics but politicians, merchants, bankers, planters, journalists, artisans, and theologians, some of whom had little or no college education. This is not to say that academic economists did not sometimes write books and articles or collect and analyze statistical data. In 1843, George Tucker, a professor of moral philosophy at the University of Virginia, published an estimate of U.S. national income based on the decennial census of 1840 (see Tucker 1843).[1] A prophet of industrialization and population growth, Tucker was involved in politics and served a term in the House of Representatives. The academy also produced a few writers of textbooks on economics. The most widely used text during the three decades before the Civil War, *The Elements of Political Economy* (1837), was written by the Reverend Francis Wayland, the president of Brown University, a principal leader of the Northern Baptist Church, and an advocate of laissez-faire. Its objective, Wayland wrote, was to set forth God's laws, so far discovered, regarding the production and distribution of those products that constitute the wealth of a nation (Dorfman 1946; Studenski 1958).

Property, Wayland argued, was founded on the "will of God," and it was acquired directly as his immediate gift (as with land) or by labor. As for labor, Wayland accepted the general validity of the Malthusian doctrine that the excessive fertility of laborers tended to increase their numbers and reduce their wages to the point of starvation and death. But that tendency was kept in abeyance in the United States because capital increased faster than the population. Hence, distressing poverty was rare except when precipitated by intemperance, indolence, and similar vices. The favorable demand for labor and the lagging supply made it possible for industrious workers to accumulate capital in a relatively short period of time. It followed that combinations

1. Tucker is also well-known as the author of a pamphlet arguing for the freeing of slaves (see Tucker 1801).

of labor (i.e., unions) were not only counterproductive to the interest of labor but also unjust because they deprived laborers of the right to dispose of their labor and, as with legislative interference, they were destructive of industry.

The Response to Industrial Concentration

The widespread embrace of laissez-faire before the Civil War was promoted by an economy that consisted of small producing units. Both rural and urban laborers could believe that by hard work and frugality they would become the masters of their own businesses. After the Civil War, however, new technologies promoted such large economies of scale that many small operations were driven out of competition in one industry after another, including iron and steel, petroleum, meatpacking, milling, chemicals, and banking. Large-scale enterprises arose not only because new inventions required massive investments in plants (as in Bessemer steel) or in grids (as in electricity). They were also promoted by the enormous expansion of urban markets and technologies that drastically reduced the cost of transportation and communication. As a result, efficient firms could compete in distant markets in which inefficient local producers had previously been protected by the natural barriers of high transportation and distribution costs.

The losers in this competitive struggle did not accept their fate stoically but appealed to the government for legislation that would offset their technological disadvantages. Small millers in upstate New York demanded reductions in their freight rates to make them more competitive with large-scale millers in Milwaukee. Small banks that charged higher interest rates in their local markets demanded protection from the eastern banks that began offering comparable services at lower rates. Small refineries called on legislators to prevent Standard Oil from undercutting their markets with what they described as *predatory pricing*. Farmers in Iowa condemned the railroads for charging more to ship a ton of wheat two hundred miles to Chicago than it cost to ship that same ton nine hundred miles from Chicago to New York City.

Thus, the last quarter of the nineteenth century and the first quarter of the twentieth witnessed a fierce confrontation between the new big businesses and traditional businesses. On the one side were multimillionaires, the "robber barons." On the other were small rural and urban businesses, farmers, and those who labored for the robber barons.

Railroads were the earliest and the most persistent target. During the railroad-building booms preceding and following the Civil War, state and local governments outdid each other in offering tax exemptions and other inducements for companies to lay track through their areas. Once the railroads were completed, however, discontent arose with the structure of rates, the quality of service, and the failure of railroads to pay their fair share of taxes. Led by the principal farmers' organization in the Midwest, the Grange, lobbies were successful in passing state laws regulating the railroads, in raising taxes on railroad properties, and in bringing suits in the courts.[2]

Labor also protested, often using its most powerful weapon, the strike. During the Civil War, the first of the great railroad brotherhoods was organized among locomotive engineers, and that example was followed by other groups of workers on and off the railroad. By 1870, there were thirty-two national trade unions, and most of the larger cities had also established trade assemblies and publications. The most violent strike of the postwar era began during July 1877 in response to wage cuts on many of the railroads east of the Mississippi. Trains were halted by workers, and troops were brought out to deal with angry mobs. Buildings were burned and blood spilled in Baltimore, Pittsburgh, and other major railroad centers. By the time the strike was over, about one hundred people had been killed, and the resulting property damage ran into the millions of dollars. The conflict was so bloody it revived fears that America could be visited by a revolution of the French type. Those fears were reawakened in 1892 and again in 1893 when strikes at the giant Carnegie Steel Company and the Pullman Palace Car Company touched off pitched battles and

2. For this and the three preceding paragraphs, see Benson (1955), Hughes (1991), Lebergott (1964), and Temin (1964).

mob violence, and state militias and federal troops had to be brought in to reestablish order. Labor strife led some reformers to doubt the prevailing theories of poverty and to question whether the frontier was still an adequate safety valve for urban labor (Fogel 2000).

The Social Gospel Movement and the Wisconsin Idea

The change in thought is illustrated by the career of the Reverend John Bascom, who taught economics at Williams College and published a textbook in political economy in 1859. Holding views quite similar to those of Wayland, Bascom argued that the tactics of trade unions, especially strikes, were vicious attempts by incompetent workers to prevent workers with "superior intelligence, economy, and integrity" from achieving the benefits of free competition. By the mid-1880s, however, when Bascom was serving as the fifth president of the University of Wisconsin, he deplored the prevailing lack of sympathy for trade unions. Capital, he charged, was combining in ways that made the contest between capital and labor highly unequal. Consequently, government should curb the tyranny of big business and favor labor more. The state, he believed, had to become a vehicle for social improvement, including a mild redistribution of income from the rich to the poor (Dorfman 1946, 967 [quote]; Curti and Carstensen 1949; Henderson 1993).

Bascom was one of the pioneers of the new reform movement that historians refer to as the "Social Gospel." Although his change of economic heart was typical of many of the leaders of this wave of reform, it would be a mistake to presume that the evolution reflected a change in underlying spirit, from complacency to compassion. The reformers of the "Second Great Awakening," the name that historians have given to the reform movement that began during the antebellum era, could hardly be called *complacent*. They were imbued with the ethic of benevolence. Their ambition was to make the world "a fit place for the imminent return of Christ." They were committed to the "universal reformation of the world" and to the "complete and final overthrow" of "war, slavery, licentiousness, and all such evils and abominations." But they were slow in recognizing a new set of issues precipitated by

the rise of big business (McLoughlin 1978, 128 [quotes]; Fogel 2000; Curti and Carstensen 1949; Henderson 1993).

Although the Social Gospel movement arose out of the theological currents of the Second Great Awakening, it was transformed by the deepening economic and social strife of the 1870s and 1880s, by the intensification of corruption in the rapidly growing cities, and by the intellectual turmoil precipitated by the new findings in geology and by the Darwinian controversy. In this context, Social Gospel leaders argued that, if America were to revitalize itself, it would have to change not only its creed, its theory of man's relationship to God, but also its ethics. It would have to make poverty not a personal failure but a failure of society, and evil would have to be seen not as a personal sin but as a sin of society. According to these radicals, it was the obligation of the state to improve the economic condition of the poor by favoring labor and redistributing income, reforms necessary to put an end to urban corruption (Fogel 2000; Curti and Carstensen 1949; Henderson 1993).

Bascom was not only one of the earliest academic expositors of Social Gospel theory; he was also a highly influential teacher who put an indelible stamp on the culture of the University of Wisconsin and, in time, on the state government of Wisconsin. Bascom's influence at the university was intensified and extended after 1891 by Richard T. Ely, the most prominent economist of the period and the most ardent academic expositor of Social Gospel theory. Hired to head the new School of Economics, Political Science and History, Ely sought to create a program that would do for the civil service what West Point had done for engineering. He quickly hired two of his former students from Johns Hopkins University and developed a large number of courses on such topics as the history of political economy, recent economic theories, statistics, money, and the distribution of wealth (Henderson 1993; Furner 1990; Curti and Carstensen 1949).

Three events made it possible for Ely to pursue his vision of academics as partners with politicians in the creation of a welfare state. The first was the election of Robert M. LaFollette, a disciple of Bascom's, as governor of Wisconsin in 1900. The second was the accession of Charles R. Van Hise, another disciple of Bascom's and a classmate of

LaFollette's, as university president in 1903. The third was the arrival of John R. Commons, a student of Ely's at Johns Hopkins and a zealous Social Gospeler, as professor of economics in 1904. Commons, who had had a good deal of experience with government and business, had learned that it was necessary to tone down the religious rhetoric. He also emphasized that his arguments for reform were aimed not at undermining capitalism but at regulating the abuses of big businesses. Commons recognized that the case for change had to be based on careful empirical analysis of the organization of business and the operation of labor markets. This approach became known as *institutional economics* (Henderson 1993; Furner 1990; Curti and Carstensen 1949).

When LaFollette needed advice on the implementation of his legislative agenda, he turned to Commons. Commons drafted legislation for a civil service bill (which based employment on competitive examinations) and for a bill establishing a Wisconsin state commission to regulate railroads, both of which were enacted in 1905. He was subsequently involved in designing the state's programs for regulating public utilities, workmen's compensation, and apprenticeships. Other university economists who were involved either in consulting with the government or in serving on regulatory commissions included Thomas S. Adams (a specialist in public finance and taxation) and Balthasar H. Meyer (a specialist in railroad regulations). Beyond economics, members of the faculty were drawn to serve on state commissions from such diverse fields as geology, bacteriology, agronomy, and engineering. In 1908, about one-sixth of the university faculty had appointments on government commissions (Henderson 1993; Furner 1990; Curti and Carstensen 1949).

The "Wisconsin Idea," as LaFollette called it, for a partnership between academic and political reformers was duplicated in other states. At local and state levels of government, where constitutional scruples against government intervention in the economy were relatively weak, many politicians saw the advantages of using nonpartisan academic experts to investigate the issues reflecting popular discontent, while academic reformers, such as Ely and Commons, believing that the facts were on their side, saw such investigations as powerful in-

struments in rallying public and legislative support for proposals they embraced. Of course, belief in the efficacy of particular policies need not undermine fruitful, objective research, as the career of Commons illustrates. Everything depends on the investigator's turn of mind, on his or her dedication to professional standards.

The Entry of Economists into the Making of Federal Policy

The idea of a partnership between academic and political reformers that was so strong in Wisconsin was not easily transferred to the federal level. Although other universities had religiously driven economists who wanted to turn the federal government into a welfare state, the majority of economists outside Wisconsin were orthodox in their economic principles. They believed that, although there was a legitimate role for government to play in addressing market failures, that role had to be lightly exercised. Otherwise, the government might become a serious obstacle to the effective performance of the economy. Another and perhaps more formidable barrier to the penetration of the federal government was the absence of a strong demand for economists among members of Congress and officials in the executive branch. Prior to World War I, the demand for the advice of economists in the making of federal policy was as modest as the supply of economists who sought to influence federal policy directly.

Nevertheless, between 1880 and World War I, economists did become increasingly involved in federal policymaking. Three factors drove this evolutionary process. The first was the rising tide of unrest over economic conditions among workers, farmers, and small businessmen, particularly the periodic outbreaks of violence by railroad and industrial workers. These outbreaks stirred alarm in Congress, which took measures to obtain more information about real wages and other aspects of the economy. The second factor was the emergence of a small corps of economists with expertise on the issues of concern to Congress and the president. As late as 1900, there were hardly seventy economists in the twenty-two top research universities of the nation. Some of these experts were largely self-taught, without doctorates in economics. This was, for example, true of Charles F.

Dunbar, the first person appointed to a chair in economics at Harvard, whose only earned degree was an A.B., awarded in 1851 (Parrish 1967). The third factor, especially after 1900, was the determined effort of Social Gospel economists to project their program for the transformation of the federal government into a welfare state. Fewer in number than mainstream, orthodox economists, the Social Gospelers were able to gain an audience in Congress and among other opinionmakers, partly because of their considerable expository skills, and partly because of the large role they played in amassing empirical evidence on the wretched conditions of life among a large proportion of industrial workers.

An important step in the transformation of the federal government into a welfare state was the establishment of an agency to systematically collect information on labor conditions. The U.S. Bureau of Labor Statistics (BLS) was established in 1885 with Carroll D. Wright, one of the self-taught economists and statisticians, as its first commissioner, a post he held until 1904. Although Wright (who taught at Johns Hopkins, Columbia, and Harvard Universities) was much closer in his economic analyses to such orthodox economists than he was to Ely, he believed that the rise of big business and the growth of an industrial labor force had produced injustices that required illumination. He had earlier pioneered the collection of data on the earnings and expenditures of working-class families and was one of the propounders of the so-called Engel curve, which purported to show, from cross-sectional data, how consumption of various items changed with income (Stigler 1954; Furner 1990). Although many of the projects undertaken by the BLS were dictated by requests for information by Congress, Wright launched many studies on his own initiative.

Data on changes in wages and prices for the entire period 1840–91 were collected at the request of the Senate Finance Committee, headed by Nelson Aldrich of Rhode Island. Using data obtained directly from the payrolls of eighty-eight companies and covering various occupations in twenty-one industries, the BLS was able to chart the progress of nominal wages. It also obtained data on the wholesale prices of two hundred articles going back to 1860 and of retail prices for a more limited period. These raw figures were converted into wage and price

indices, initiating an important new statistical procedure. Out of this research was developed the first cost-of-living index, with weights obtained from a study of the household budgets of 2,561 working-class families (Furner 1990; Aldrich 1892, 1893).

The BLS also launched studies of wages and living standards in key industries and investigated the changing structure of the labor force, focusing on the problems of such groups as women, children, blacks, and railroad labor. Wright, who supported the development of craft trade unions, conducted surveys on labor laws in European countries, outlining existing and incipient entitlement programs, including workmen's compensation. Domestically, the BLS collected statistics on the impact of unions on wages and surveyed the annual number of strikes and lockouts. Such studies suggested, in one historian's assessment, "that unions exercised a restraining influence during depressions and actually helped to stabilize disorganized industries. . . . The BLS made no direct effort to assess the impact of strikes on distributive equity, but consistently implied that organized action was necessary to achieve a just division, and that aggressive wage demands supported necessary consumption" (Furner 1990, 252).

Economists were also drawn into the making of federal policy through the increasing number of commissions established by Congress to investigate pressing policy issues. The U.S. Industrial Commission (USIC), which operated between 1898 and 1902, was the first government agency to bring together a staff of trained economists in the federal government. Responding to the complaints of the Populists, leaders of small businesses, and labor, this commission investigated such issues as the impact of immigration on wages, the pricing policies of railroads, and industrial concentration. Edward Dana Durand of Cornell and Stanford Universities, who served as secretary of the commission, hired a number of young economists—including John R. Commons, Emory R. Johnson of the Wharton School at the University of Pennsylvania, and William Z. Ripley of the Massachusetts Institute of Technology—who would later gain national stature. The commission produced nineteen volumes of reports and testimony that influenced subsequent antitrust policies and legislation on immigration. The empirical evidence collected by the USIC and

the analysis of the data were on a high level. On the whole, the reports recommended negotiations between unions and trusts as the best way to stabilize labor markets, ensure high levels of economic activity, and provide relatively high wages (Furner 1990).

Other congressional commissions that involved economists and that had a significant impact on economic policy included the Commission on Industrial Relations (CIR), which operated between 1913 and 1916, the National Monetary Commission (NMC) of 1908–12, and the U.S. Immigration Commission of 1909–15. Each of these was a response to political unrest touched off by business cycles. The findings of each commission provided the foundation for subsequent legislation. The Federal Reserve Act of 1913, for example, which established the Federal Reserve System, closely followed the recommendations of the NMC. Similarly, the forty-one-volume report of the Immigration Commission laid the basis for legislation enacted in the early 1920s ending unrestricted immigration and establishing quotas aimed at sharply limiting the entry into the United States of immigrants from Southern and Eastern Europe (Hughes 1991; Dorfman 1959a).

The papers and reports that did the most to promote the welfare state were those emanating from the CIR. With a research staff of fifty, mostly economists, the CIR produced papers that characterized the effect of big business on living conditions along lines much closer to the views of Ely than to those of Wright. The commission found that six major banking groups controlled three-quarters of the railroads and a quarter of manufacturing and that half "the wage-earners' families in the United States lacked sufficient income for adequate subsistence and health." These reports called for federal and state intervention on the side of unions and helped establish such government programs as labor exchanges, retraining schools, and public works. These programs were described as a prerequisite for ending labor unrest and for achieving distributive justice. They also outlined social insurance schemes covering sickness, unemployment, and old age to which employees, employers, and the government would jointly contribute (Furner 1990, 277).