

# Jesús M. Zaratiegui, *Caballeros y empresarios. El hombre de negocios victoriano*

Madrid: Ediciones Rialp, S.A., 1996, pp. 176.

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In an interesting article in the *American Economic Review*, May 1998, entitled «Survival and Size Movility Among the World's Largest 100 Industrial Corporations, 1912-1995", Professor Leslie Hannah shows that big enterprises in Great Britain have had a higher survival rate than their counterparts in USA or Germany. Moreover, Professor Hannah states that «only 23 percent of today's US. giants were also in the 1912 top-100 list» whereas «the comparable figures for Germany and Britain are as high as 66 percent and 75 percent, respectively». So, Professor Hannah concludes that «Europe has been the home of Chandlerian stable oligopolies; America has more obviously been the creative (and destructive) dynamo of the Schumpeterian paradigm».

But the idea we are interested in in this review is Hannah's explanation of the success of British giants in the long run. Although the reasons for the mortality rate in German and American firms are clearly different (Germans have had a more controlled economy whereas American capitalism has undergone a sharp Schumpeterian process of creative destruction), «British giants of 1912 were unusually globally minded for their time. The British practiced free trade before World War I... and began their 20th-century life as internationally competitive firms than their rivals». «Moreover, Hannah says, in 1912 German and American giant firms typically had only 10-15 percent of their assets or employment abroad, but British giants already had more than 30 percent of theirs abroad on average and thus were less constrained by home market performance.» Permit me to inform sceptics that the existence of a large colonial market cannot explain these results from the end of the fifties up till now.

So, if the survival of British companies has its origins in their adaptation to a scenario of free trade and orientation towards the global markets, probably the Victorian industrialists (gentlemen and businessmen, as Zaratiegui calls them) had a particular influence on it. And perhaps the high rate of survival in British enterprises has something to do with the particular mentality of the managers who established their businesses in the Victorian Age, as Dr. Zaratiegui tries to show us.

This is *apparently* the thesis of Zaratiegui's book: there was a special kind of managerial intelligence or mind set during the Victorian Age that made possible an increase (which also slows down decline later) in economic activity, and this established the basis for British dominance until World War I. And the continuing decline in its economic position -approximately after 1873- came as a result not of negligence or an indulgent attitude on the part of British businessmen, but because managers did not have real possibilities for action due to legal and institutional constraints. These institutional restraints are not understood in a modern neoinstitutional view, but as the «market conditions and the rigid institutional framework that had been developed during the phase of atomized competition in the 19th Century. Those hereditary limitations prevent them from obtaining the control of markets, imposing their authority in their relationship with the workers, or developing the necessary hierarchy in management control for applying modern methods of mass production.» [pp. 159-160]. So, what Zaratiegui finds missing is greater oligopolistic power in the hands of businessmen.

I say 'apparently' because the reader will not find an introduction or any clear conclusions in the book which explain what is Zaratiegui's idea. There is no proper introduction: instead Zaratiegui devotes eight pages to the social, political and intellectual background. Similarly, there are no conclusions.

In contrast to Hannah, Zaratiegui does not establish this British entrepreneur's special ability as part of a more open-minded or a more international vision of the trade and businesses, but as a combination of genetical inclination for business and educational training: Zaratiegui calls this «empresarialidad» (the quality of managerial ability, that involves leadership, innovation and risk assumption). This term is not clarified until page 127, where he states: «Business ability is understood as a skill in choosing persons that occupy positions as managers and workers at the firm». That is part of the truth, but only a part.

Recalling the article of Alfred Marshall (1907) «Social Possibilities of Economic Chivalry», Dr. Zaratiegui tries to show us, in an elitist vision of the managerial class, that there were a group of men, a class, which possesses above all a genetic quality -although one refined by social (family, education, friends, values, etc.) standards-, given to only a few. And this managerial capacity of individuals in a society is a given amount, ie., a stock or a parameter, at a given time. Zaratiegui maintains that entrepreneurs constitute a separate social class (a group of supermen, such as William Lever, who «had all his business in his head and managed it by means of verbal instructions... Businesses were not only concerned with profits or rational calculations... but also with the possibilities of adventure» [p. 42]).

This might sound like an old exploded theory. And, although it is difficult to get a clear idea about the subject of Zaratiegui's book because the author goes into a lot of subjects and details but never defines his position clearly, Dr. Zaratiegui seems to have forgotten basic modern theories such as human capital or neo-institutionalist theories of the firm. There are working nowadays in this field a lot of people -economists, psychologists, historians, sociologists, etc.-, almost unconnected because of traditional academic isolation.

I think Zaratiegui gives excessive importance to the idea that entrepreneurs have a greater or lesser capacity for business, understood as a genetic quality. It is true that «differences in business ability may produce very different results in economic activity» (p. 146). And it is true too that there have always been some people who started their business without any experience, sense of business, or with the intention of 'taking the money and run' (probably the market will have eliminated most of these). But all of these attitudes have to do with institutions. I do not believe that a British businessman is more efficient, better or more altruistic than an Italian one or less than an American businessman. The problem is not of quality as Zaratiegui thinks (because skills can be learned), but an institutional problem: which are the appropriate institutional frameworks to allow and foster the development of entrepreneurial ability?

So, for example, when Zaratiegui says that «The structure of English industry was a restraint on innovation» (p. 48), he does not stop to analyze why that was so, or why English industry had this kind of organization and not another; or if it was really inefficient or, on the contrary, it was the most

efficient *possible*, that is, given the legal and institutional conditions in that period. We will go further into this problem below.

*Caballeros y Empresarios* is a good book of business history. But it pretends to be also an analytical and conceptual tool, and in that respect the book fails. It is quite singular that a book edited in 1996 does not mention -for example- Arrow, Baumol, Eggertsson, Oliver Hart, Marglin, Nelson and Winter, Douglas North, Herbert Simon, George Stigler, Tawney, Tirole, Toynbee, Max Weber, or Oliver Williamson in the Bibliography, at least referring to their hypotheses in support of or to reject some of the ideas that Zaratiegui touches on.

Precisely because Zaratiegui refers to a lot of analytical subjects, he does not go deeply into any. He gives different opinions or views taken from other authors on many subjects, but he does not clarify his hypothesis nor his conclusions on any subject, adopting an eclectic position every time.

An example of this is when Zaratiegui tries to explain the decline in British economic activity, he uses an old fashioned keynesian hypothesis of the failure of effective demand; studying a probable decline in the export trade (pp. 52-53) he asserts: «exports are not an independent variable in the process: they may be both cause and effect» (p. 53).

Likewise, discussing British industrial organization, specifying and describing different classes of businesses through history (single owners, entrepreneurs and managers) which separates or not ownership and management, he does not enter into details explaining the consequences that these different structures might have had on the British economic position (pp. 32-40; 65). He touches on subjects such as the Agency-problem -including a very interesting text of Marshall (p. 36)-, but his final analysis is too simplistic: although the change in contractual choices made by entrepreneurs from single proprietorship or partnership to corporations was more a «legal subterfuge» than an economical -or real- change (p. 35), the principal reason for business decline was that «the times of magic managerial motivation had passed» (p. 43). Nevertheless, these pages (pp. 32-40) contain good ideas and an interesting approach to the subject.

On this subject, there is a good article, on the 19th-century, by Naomi Lamoreaux, «Partnerships, Corporations, and the Theory of the Firm», published in the *American Economic Review*, Vol. 88, May 1998, where the author argues «that no clear economic boundary distinguished ordinary contracts from those considered by law to be firms... that businesspeople could choose from a range of contractual forms that offered varying degrees of 'firmness', that is, that differed in the extent to which they protected contracting parties against holdup... [and] that increasing the degree of 'firmness' of a contract was not always desirable from the standpoint of entrepreneurs».

Lamoreaux shows that it was not always convenient for owners to adopt a certain organizational form. «In the case of small firms, there appears to be abundant evidence that liability rules in and of themselves did not determine the choice of organizational form... Many British joint-stock companies, for example, could have obtained limited liability by reorganizing under a general

incorporation law passed during the mid-1850's but chose instead to remain as there were». And finally she says: «The corporate form of organization was not always an improvement over the partnership for all of the parties concerned.» All these ideas -already in Forbes (1986) or Hart (1995)- could have given rise to a new line of research, but Zaratiegui ignores this discussion and does not get the most out of his study.

In the same way Zaratiegui refers -although in a more veiled way than Hannah- to the multinational character of British firms when he mentions some examples of mergers and takeovers, referred to as «changes in scale» or «co-operation» (pp. 38-43). Zaratiegui's idea here is that the process of expanding to larger scale production in British firms was slower than in German or American companies because, in contrast to those, the structure of British firms «were not appropriate for efficient cooperation» (p. 39). The conclusion is therefore quite different from Hannah's.

One of the stronger points of Zaratiegui's book is his continual references to Alfred Marshall and his work. Zaratiegui has worked profusely on Marshall's view of industrial organization. He has published more recently, in 1998, an article in the *Barcelona Management Review*, where he treats some of Marshall's ideas on entrepreneurship and managers. In *Caballeros y Empresarios*, Zaratiegui does not enter into the apparent contradiction in Marshall, an economist for whom «*Natura non facit saltum*», but also an economist for whom the entrepreneurs are specifically looking for new, different and innovative ideas which will differentiate them (the '*saltum*') from their competitors. I said apparently because precisely this theory of biological evolution of industrial organization (contained in his famous motto), might contain Marshall's view of the role of the entrepreneurs.

Zaratiegui explains perfectly in chapter IV how, in Marshall's view of the running of business, there takes place a process of bureaucratization in large firms, which inhibits creative ideas, inventive power and experimentation. These bureaucratic methods make communication difficult in the firm, increasing information costs. This is the principal reason why the advantages which come from economies of scale or increasing returns, which give rise to vertical expansion, do not produce monopolies. And this -together with external economies- is the reason why large firms do not destroy their smaller rivals (Zaratiegui raises this last point on page 143, and the whole question on chapters IV and V).

Finally, in general, the reader will notice in the book a certain aversion to the free market, competition, liberalism, self-interest (which Zaratiegui mistakes for selfishness), or the figure of *homo oeconomicus*, all of them considered by Zaratiegui as negative concepts (pp. 68-9, 92, 97-102, 118-9, or 124 are some examples of these confused ideas).

The last minor problem with the book which could have been solved by taking more care and time is the bibliography. Turner's book (1984) quoted on page 115 does not appear in the Bibliography for example. And it does not specify what edition has been used of Marshall's book: in the case of the *Principles of Economics*, in the Bibliography this is quoted in the first edition (1890), but the author then uses the eighth edition (1920).

These are nevertheless minor cavils in a book which contains a great deal of new

information and is obviously the result of much hard work.

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