

## *John D. Rockefeller:* SOME EXPERIENCES IN THE OIL BUSINESS

THE story of the early history of the oil trade is too well known to bear repeating in detail. The cleansing of crude petroleum was a simple and easy process, and at first the profits were very large. Naturally, all sorts of people went into it: the butcher, the baker, and the candlestick-maker began to refine oil, and it was only a short time before more of the finished product was put on the market than could possibly be consumed. The price went down and down until the trade was threatened with ruin. It seemed absolutely necessary to extend the market for oil by exporting to foreign countries, which required a long and most difficult development; and also to greatly improve the processes of refining so that oil could be made and sold cheaply, yet with a profit, and to use as by-products all of the materials which in the less efficient plants were lost or thrown away.

These were the problems which confronted us almost at the outset, and this great depression led to consultations with our neighbors and friends in the business in the effort to bring some order out of what was rapidly becoming a state of chaos. To accomplish all these tasks of enlarging the market and improving the methods of manufacture in a large way was beyond the power or ability of any concern as then constituted. It could

only be done, we reasoned, by increasing our capital and availing ourselves of the best talent and experience.

It was with this idea that we proceeded to buy the largest and best refining concerns and centralize the administration of them with a view to securing greater economy and efficiency. The business grew faster than we had anticipated.

This enterprise, conducted by men of application and ability working hard together, soon built up unusual facilities in manufacture, in transportation, in finance, and in extending markets. We had our troubles and set-backs; we suffered from some severe fires; and the supply of crude oil was most uncertain. Our plans were constantly changed by changed conditions. We developed great facilities in an oil centre, erected storage tanks, and connected pipe-lines; then the oil failed and our work was thrown away. At best it was a speculative trade, and I wonder that we managed to pull through so often; but we were gradually learning how to conduct a most difficult business.

### *Foreign Markets*

Several years ago, when asked how our business grew to such large proportions, I explained that our first organization was a partnership and afterward a cor-

poration in Ohio. That was sufficient for a local refining business. But, had we been dependent solely upon local business, we should have failed long since. We were forced to extend our markets into every part of the world. This made the seaboard cities a necessary place of business, and we soon discovered that manufacturing for export could be more economically carried on there; hence refineries were established at Brooklyn, at Bayonne, at Philadelphia, at Baltimore, and necessary corporations were organized in the different states.

We soon discovered, as the business grew, that the primary method of transporting oil in barrels could not last. The package often cost more than the contents, and the forests of the country were not sufficient to supply cheaply the necessary material for an extended time. Hence we devoted attention to other methods of transportation, adopted the pipe-line system, and found capital for pipe-line construction equal to the necessities of the business.

To operate pipe-lines required franchises from the states in which they were located — and consequently corporations in those states — just as railroads running through different states are forced to operate under separate state charters. To perfect the pipe-line system of transportation required many millions of capital. The entire oil business is dependent upon the pipe-line. Without it every well would be less valuable and every market at home and abroad would be more difficult to serve or retain, because of the additional cost to the consumer. The expansion of the whole industry would have been retarded without this method of transportation.

Then the pipe-line system required other improvements, such as tank-cars upon railroads, and finally the tank-

steamer. Capital had to be furnished for them and corporations created to own and operate them.

Every one of the steps taken was necessary if the business was to be properly developed, and only through such successive steps and by a great aggregation of capital is America today enabled to utilize the bounty which its land pours forth, and to furnish the world with light.

#### *The Start of the Standard Oil Company*

In the year 1867 the firms of William Rockefeller & Co., Rockefeller & Andrews, Rockefeller & Co., and S. V. Harkness and H. M. Flagler united in forming the firm of Rockefeller, Andrews & Flagler.

The cause leading to the formation of this firm was the desire to unite our skill and capital in order to carry on a business of greater magnitude with economy and efficiency in place of the smaller business that each had heretofore conducted separately. As time went on and the possibilities became apparent, we found further capital to be necessary; then we interested others and organized the Standard Oil Company, with a capital of \$1,000,000. Later we saw that more money could be utilized, found persons who were willing to invest with us, and increased our capital to \$2,500,000, in 1872, and afterward in 1874 to \$3,500,000. As the business grew, and markets were obtained at home and abroad, more persons and capital were added to the business, and new corporate agencies were obtained or organized, the object being always the same — to extend our operations by furnishing the best and cheapest products.

I ascribe the success of the Standard Oil Company to its consistent policy of making the volume of its business large through the merit and cheapness of its products. It has spared no expense in

utilizing the best and most efficient method of manufacture. It has sought for the best superintendents and workmen and paid the best wages. It has not hesitated to sacrifice old machinery and old plants for new and better ones. It has placed its manufactories at the points where they could supply markets at the least expense. It has not only sought markets for its principal products, but for all possible by-products, sparing no expense in introducing them to the public in every nook and corner of the world. It has not hesitated to invest millions of dollars in methods for cheapening the gathering and distribution of oils by pipe-lines, special cars, tank-steamers, and tank-wagons. It has erected tank-stations at railroad centres in every part of the country to cheapen the storage and delivery of oil. It has had faith in American oil and has brought together vast sums of money for the purpose of making it what it is, and for holding its market against the competition of Russia and all the countries which are producers of oil and competitors against American products.

#### *The Insurance Plans*

Here is an example of one of the ways in which we achieved certain economies and gained real advantage. Fires are always to be reckoned with in oil refining and storage, as we learned by dear experience, but in having our plants distributed all over the country the unit of risk and possible loss was minimized. No one fire could ruin us, and we were able thus to establish a system of insuring ourselves. Our reserve fund which provided for this insurance could not be wiped out all at once, as might be the case with a concern having its plants together or near each other. Then we studied and perfected our organization to prevent fires, improving our appli-

ances and plans year after year until the profit on this insurance feature became a very considerable item in the Standard earnings.

It can easily be seen that this saving in insurance, and minimizing the loss by fire affected the profits, not only in refining, but touched many other associated enterprises: the manufacture of by-products, the tanks and steamers, the pumping-stations, etc.

We devoted ourselves exclusively to the oil business and its products. The company never went into outside ventures, but kept to the enormous task of perfecting its own organization. We educated our men; we trained many of them from boyhood; we strove to keep them loyal by providing them full scope for their ability; they were given opportunities to buy stock, and the company itself helped them to finance their purchases. Not only here in America, but all over the world, our young men were given chances to advance themselves, and the sons of the old partners were welcomed to the councils and responsibilities of the administration. I may say that the company has been in all its history, and I am sure it is at present, a most happy association of busy people.

I have been asked if my advice is not often sought by the present managers. I can say that if it were sought it would be gladly given. But the fact is that since I retired it has been very little required. I am still a large stockholder, indeed I have increased my holdings in the company's stock since I relinquished any part in its management.

#### *Why the Standard Pays Large Dividends*

Let me explain what many people, perhaps, fully appreciate, but some, I am sure, do not. The Standard pays four dividends a year: the first in March,

which is the result of the busiest season of the whole twelvemonth, because more oil is consumed in winter than at other seasons, and three other dividends later, at about evenly divided periods. Now, these dividends run up to 40 per cent. on the capital stock of \$100,000,000, but that does not mean that the profit is 40 per cent. on the capital invested. As a matter of fact, it represents the results of the savings and surplus gained through all the thirty-five or forty years of the workings of the companies. The capital stock could be raised several hundred per cent. without a penny of over-capitalization or "water"; the actual value is there. If this increase had been made, the rate would represent a moderate dividend-paying power of about 6 to 8 per cent.

#### *A Normal Growth*

Study for a moment the result of what has been a natural and absolutely normal increase in the value of the company's possessions. Many of the pipe-lines were constructed during a period when costs were about 50 per cent. of what they are now. Great fields of oil lands were purchased as virgin soil, which later yielded an immense output. Quantities of low-grade crude oil which had been bought by the company when it was believed to be of little value, but which the company hoped eventually to utilize, were greatly increased in value by inventions for refining it and for using the residues formerly considered almost worthless. Dock property was secured at low prices and made valuable by buildings and development. Large unimproved tracts of land near the important business centres were acquired. We brought our industries to these places, made the land useful, and increased the value, not only of

our own property, but of the land adjacent to it to many times the original worth. Wherever we have established businesses in this and other countries we have bought largely of property. I remember a case where we paid only \$1,000 or so an acre for some rough land to be used for such purposes, and, through the improvements we created, the value has gone up 40 to 50 times as much in 35 or 40 years.

Others have had similar increases in the value of their properties, but have enlarged their capitalization correspondingly. They have escaped the criticism which has been directed against us, who with our old-fashioned and conservative notions have continued without such expansion of capitalization.

There is nothing strange or miraculous in all this; it was all done through this natural law of trade development. It is what the Astors and many other large landholders did.

If a man starts in business with \$1,000 capital and gradually increases his property and investment by retaining in his concern much of his earnings, instead of spending them, and thus accumulates values until his investment is, say, \$10,000, it would be folly to base the percentage of his actual profits only on the original \$1,000 with which he started. Here, again, I think the managers of the Standard should be praised, and not blamed. They have set an example for upbuilding on the most conservative lines, and in a business which has always been, to say the least, hazardous, and to a large degree unavoidably speculative. Yet no one who has relied upon the ownership of this stock to pay a yearly income has been disappointed, and the stock is held by an increasing number of small holders the country over.

#### *The Management of Capital*

We never attempted, as I have already said, to sell the Standard Oil stock on the market through the Stock Exchange. In the early days the risks of the business were great, and if the stock had been dealt in on the Exchange its fluctuations would no doubt have been violent. We preferred to have the attention of the owners and administrators of the business directed wholly to the legitimate development of the enterprise rather than to speculation in its shares. The interests of the company have been carefully conserved. We have been criticized for paying large dividends on a capitalization which represents but a small part of the actual property owned by the company. If we had increased the capitalization to bring it up to the real value, and listed the shares on the Exchange, we might have been criticized then for promoting a project to induce the public to invest. As I have indicated, the foundations of the company were so thoroughly established, and its affairs so conservatively managed, that, after the earlier period of struggle to secure adequate capital and in view of the trying experiences through which we then passed, we decided to pursue the policy of relying upon our own resources. Since then we have never been obliged to lean very heavily upon the financial public, but have sought rather to hold ourselves in position not only to protect our own large and important interests, but to be prepared in times of stress to lend a helping hand to others. The company has suffered from the statements of people who, I am convinced, are not familiar with all the facts. As I long ago ceased to have any active part in the management of its affairs perhaps I may venture the opinion that men who devote them-

selves to building up the sale of American products all over the world, in competition with foreign manufacturers, should be appreciated and encouraged.

There have been so many tales told about the so-called speculations of the Standard Oil Company that I may say a word about that subject. This company is interested only in oil products and such manufacturing affairs as are legitimately connected therewith. It has plants for the making of barrels and tanks; and building pumps for pumping oil; it owns vessels for carrying oil, tank-cars, pipes for transporting oil, etc., etc. — but it is not concerned in speculative interests. The oil business itself is speculative enough, and its successful administration requires a firm hand and a cool head.

The company pays dividends to its stockholders which it earns in carrying on this oil trade. This money the stockholders can and do use as they think fit, but the company is in no way responsible for the disposition that the stockholders make of their dividends. The Standard Oil Company does not own or control "a chain of banks," nor has it any interest directly or indirectly in any bank. Its relations are confined to the functions of ordinary banking, such as other depositors have. It buys and sells its own exchange; and these dealings, extending over many years, have made its bills of exchange acceptable all over the world.

#### *Character the Essential Thing*

In speaking of the real beginning of the Standard Oil Company, it should be remembered that it was not so much the consolidation of the firms in which we had a personal interest, but the coming together of the men who had the combined brain power to do the work, which was the actual starting-point. Perhaps it

is worth while to emphasize again the fact that it is not merely capital and "plants" and the strictly material things which make up a business, but the character of the men behind these things, their personalities, and their abilities; these are the essentials to be reckoned with.

Late in 1871, we began the purchase of some of the more important of the refinery interests of Cleveland. The conditions were so chaotic and uncertain that most of the refiners were very desirous to get out of the business. We invariably offered those who wanted to sell the option of taking cash or stock in the company. We very much preferred to have them take the stock, because a dollar in those days looked as large as a cart-wheel, but as a matter of business policy we found it desirable to offer them the option, and in most cases they were even precipitate in their choice of the cash. They knew what a dollar would buy, but they were very sceptical in regard to the possibilities of resurrecting the oil business and giving any permanent value to these shares.

These purchases continued over a period of years, during which many of the more important refineries at Cleveland were bought by the Standard Oil Company. Some of the smaller concerns, however, continued in the business for many years, although they had the same opportunity as others to sell. There were always, at other refining points which were regarded as more favourably located than Cleveland, many refineries in successful operation. . . .

All these purchases of refineries were conducted with the utmost fairness and good faith on our part, yet in many quarters the stories of certain of these transactions have been told in such form as to give the impression that the sales were

made most unwillingly and only because the sellers were forced to make them by the most ruthless exertion of superior power. . . .

#### *The Question of Rebates*

Of all the subjects which seem to have attracted the attention of the public to the affairs of the Standard Oil Company, the matter of rebates from railroads has perhaps been uppermost. The Standard Oil Company of Ohio, of which I was president, did receive rebates from the railroads prior to 1880, but received no advantages for which it did not give full compensation. The reason for rebates was that such was the railroads' method of business. A public rate was made and collected by the railroad companies, but, so far as my knowledge extends, was seldom retained in full; a portion of it was repaid to the shippers as a rebate. By this method the real rate of freight which any shipper paid was not known by his competitors nor by other railroad companies, the amount being a matter of bargain with the carrying company. Each shipper made the best bargain that he could, but whether he was doing better than his competitor was only a matter of conjecture. Much depended upon whether the shipper had the advantage of competition of carriers.

The Standard Oil Company of Ohio, being situated at Cleveland, had the advantage of different carrying lines, as well as of water transportation in the summer; taking advantage of those facilities, it made the best bargains possible for its freights. Other companies sought to do the same. The Standard gave advantages to the railroads for the purpose of reducing the cost of transportation of freight. It offered freights in large quantity, car-loads and train-loads. It furnished loading facilities and discharging

facilities at great cost. It provided regular traffic, so that a railroad could conduct its transportation to the best advantage and use its equipment to the full extent of its hauling capacity without waiting for the refiner's convenience. It exempted railroads from liability for fire and carried its own insurance. It provided at its own expense terminal facilities which permitted economies in handling. For these services it obtained contracts for special allowances on freights.

But notwithstanding these special allowances, this traffic from the Standard Oil Company was far more profitable to the railroad companies than the smaller and irregular traffic, which might have paid a higher rate.

To understand the situation which affected the giving and taking of rebates it must be remembered that the railroads were all eager to enlarge their freight traffic. They were competing with the facilities and rates offered by the boats on lake and canal and by the pipe-lines. All these means of transporting oil cut into the business of the railroads, and they were desperately anxious to successfully meet this competition. As I have stated we provided means for loading and unloading cars expeditiously, agreed to furnish a regular fixed number of car-loads to transport each day, and arranged with them for all the other things that I have mentioned, the final result being to reduce the cost of transportation for both the railroads and ourselves. All this was following in the natural laws of trade.

#### *Pipe-Lines vs. Railroads*

The building of the pipe-lines introduced another formidable competitor to the railroads, but as oil could be transported by pumping through pipes at a much less cost than by hauling in tank-cars in a railroad train the development

of the pipe-line was inevitable. The question was simply whether the oil traffic was sufficient in volume to make the investment profitable. When pipe-lines had been built to oil fields where the wells had ceased to yield, as often happened, they were about the most useless property imaginable.

An interesting feature developed through the relations which grew up between the railroads and the pipe-lines. In many cases it was necessary to combine the facilities of both, because the pipes reached only part of the way, and from the place where they ended the railroad carried the oil to its final destination. In some instances a railroad had formerly carried the oil the entire distance upon an agreed rate, but now that this oil was partly pumped by pipe-lines and partly carried by rail, the freight payment was divided between the two. But, as a through rate had been provided, the owners of the pipe-line agreed to remit a part of its charges to the railroad, so we had cases where the Standard paid a rebate to the railroad instead of the reverse — but I do not remember having heard any complaint of this coming from the students of these complicated subjects.

The profits of the Standard Oil Company did not come from advantages given by railroads. The railroads, rather, were the ones who profited by the traffic of the Standard Oil Company, and whatever advantage it received in its constant efforts to reduce rates of freight was only one of the many elements of lessening cost to the consumer which enabled us to increase our volume of business the world over because we could reduce the selling price.

How general was the complicated bargaining for rates can hardly be imagined; everyone got the best rate that he could.

After the passage of the Interstate Commerce Act, it was learned that many small companies which shipped limited quantities had received lower rates than we had been able to secure, notwithstanding the fact that we had made large investments to provide for terminal facilities, regular shipments, and other economies. I well remember a bright man from Boston who had much to say about

rebates and drawbacks. He was an old and experienced merchant, and looked after his affairs with a cautious and watchful eye. He feared that some of his competitors were doing better than he in bargaining for rates, and he delivered himself of this conviction:

"I am opposed on principle to the whole system of rebates and drawbacks — unless I am in it."