Conglomerates: A Businessman's View

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The essential question within the context of the conglomerate phenomenon is whether the Government will continue to allow "meaningful" new competition to flourish within our free enterprise system. By "meaningful" I mean adequate and frequent enough new entry into established industries to provide rapid, broad, and effective additions of competition on a scale which will provide economies to the consumer and strength to the economy.

There is an impression in the business community that a large-scale offensive war has been declared on American business growth, business change and business diversification. If this offensive war has indeed been launched, then it has been done without all of the facts, without meaningful and impartially interpreted data, and without consideration of the serious consequences. For example, the recently issued Federal Trade Commission (FTC) Report on Corporate Mergers¹ is a classic example of basically unsupported hypotheses and theory. Even critics of diversified or conglomerate companies concede many virtues to diversification and to diversification mergers. Yet, the FTC Report does not recognize one valuable contribution of these diversified companies, whether old or new. This is hardly the objective approach that is needed. And because this FTC Report is a government-sponsored project, there can be little question of why business has this impression.

In fact, in presenting this report to the Senate Subcommittee on Antitrust and Monopoly, Professor Mueller called for immediate action to curtail diversification of American business.

As I balance the costs of inaction, a policy of wait and see, against the costs of action that subsequent scientific inquiry might prove to be a too zealous policy, I choose the latter course without hesitation or reservation.

For in the present circumstance, should a bold course of action prove later to have prevented some increases in economic efficiency, the matter can be righted by changing policy.²

However, despite this recommendation, the FTC Report presented no evidence demonstrating that diversified companies or diversification mergers actually have an unfavorable effect on competition or the economy. Professor Mueller's statement is therefore a demand for sentence first, verdict afterward, and then, a belated inquiry into the facts, because, per chance, there may be some loss of economic efficiency. On this basis any policy (however damaging to the economy) could be justified, since it could later "be righted by changing policy."

¹ BUREAU OF ECONOMICS, FTC, ECONOMIC REPORT ON CORPORATE MERGERS (1969) [hereinafter cited as FTC REPORT].
What has happened, in my opinion, is that the critics are creating a smoke screen of confusion in order to compensate for the lack of any real information. Confusion arises in the first place from the impression that the issue for public debate is whether conglomerate companies should be permitted to diversify through merger. The real issue, however, is whether any company, young or old, should be allowed to diversify into fields unrelated to its traditional industry position, and by so doing, add competition the economy would not otherwise enjoy.

While there has been much said and written on the point that it is better to stimulate internal growth of competition in new fields, let me state clearly that, as a matter of business judgment, in virtually all situations of real diversification into unrelated business, this is both impractical and uneconomic. It is far better that everyone concerned should know and understand this, for decisions based on erroneous assumptions are invariably incorrect.

Companies can, perhaps, move through internal growth into an industry which is very similar in technology, production know-how and marketing to the company's existing operations. But in real product diversification situations, new entry innovations and growth in production capacity can be accomplished only through acquisition of a reasonably sized company already in that field.

There has been some acknowledgement of this fact even by the Justice Department, which has recognized the need for "foothold acquisitions" as a necessary nucleus of this entry process. Unfortunately, there have been no official guidelines published on this point, and it is our general impression that the word "foothold" will in practice be thought of as a size so small that it will not provide a viable base for the kind of modern management systems and business techniques that a diversified company such as ours can apply in attempting to improve efficiencies and provide meaningful competition.

Therefore, while it is clear that the Department of Justice agrees in principle with the need for diversification mergers, it is unwilling to follow where its own logic would lead in order to encourage really meaningful competition. Simply stated, a policy denying access to change, innovations and new industrial competition by the route of diversification acquisitions of meaningful size, will result in a stagnant status-quo of the existing large companies within an industry—regardless of efficiency, competitiveness or the resulting values offered to the consumer. It prevents the functioning of a market in corporate assets, thereby lowering the efficiency of the industry. In short, it prevents the natural transfer of assets to more efficient managements and deprives stockholders of the real value of their investments.

It is precisely for these reasons that many informed people have concluded that recent trends of our antitrust enforcement with respect to large diversification mergers are, perhaps unintentionally, preventing new and
increased innovation, and are operating to protect industry incumbents from new competition.

An examination of the top 200 or top 500 companies, or even the top 1000 companies, will disclose that an overwhelming proportion of the so-called old line companies are already widely diversified into numerous industries. This is not really a new development, a new trend, or an unusual situation. In fact, it is clear from general published information that most companies, large or small, are, to varying degrees, already diversified — and to use another word — at least partly conglomerate. This fact is readily apparent from the FTC Report itself.

Although diversification has many merits from the standpoint of the nation, the consumer, and the stockholder, there persists an emotional belief that diversified companies are unable to operate in more than one field of business. Overlooked is the fact that such a company has numerous individual specialists and experienced managers in many fields, and that the very untraditional outlook such a company brings to an industry is the key to innovation and new progress. Diversification provides a form of security and insurance, as well as a method of adapting to the quickening tempo of change that we are all experiencing — change in technology, change in markets and consumers, and change in foreign competition. It therefore underlies continuity of employment and unity of corporate effort — it is a constructive influence on our economy. It is a vital necessity to management concerned with the long-term future of its employees, its stockholders, and the communities in which it operates. Diversification is, in short, an "insurance" policy for orderly future growth, and thus has important positive values as a concept in itself.

This does not mean that a diversified company is not responsive to each of the markets in which it operates, or can be indifferent to its profit or loss there. But a diversified company is able to ride out the occasional and unforeseen vicissitudes of a particular market, depending instead on the long-term profit opportunities there. It is for this reason that communities welcome the new plants of a diversified company — plants which are less likely to be shut down because of a short-term hardship or a fortuitous change in the market.

It is for sound reasons such as these — constructive reasons — that we see most of industry, large and small, either already diversified or becoming more diversified. Factually then, what we really have are only "old" or "new" diversified companies — or conglomerates. But just as we have always recognized "well-managed" — or "less well-managed" — companies, so too do we have "well-managed" or "less well-managed" conglomerate or diversified companies. And both the investor and marketplace have always recognized this difference — and have usually rewarded it in kind by valuation and stockholder investment action. This corrective factor can be relied upon; inefficient companies must change and become efficient, or they will wither away.
Therefore, the form and structure of diversification should not be confused with the problem of individual company management. American industry, in fact, provides far more examples of successful diversified companies—old and new—than it does of "unsuccessful" ones. This large group of successful diversified companies should not be lumped together with the few less well-managed ones. Indeed, it is important to remember, that one must consider the value of diversification itself, and not the history of a few particular managements—each of which will differ in methods and performance, as well as in the magnitude of the problems they had to face in their particular industries.

"The American Way of Life"

It is argued that conglomerates and other acquisition-minded companies destroy communities—that in some manner they destroy the American Way of Life. In recent days, the Justice Department has issued statements emphasizing that this is the evil they are seeking to eliminate. You will recall the charge of emasculating the community by moving the decision power of a company elsewhere—the changing of the community to what I think was called a "branch store community."

While I cannot speak for progress, let me note that a great many of the New England mills that shut down did so because of something that happened within that town—and not away in some other city. It was because their managements fell behind the times, and while people speak with concern about the number one man in the town who becomes a number "x" man in a larger company, no one mentions the hierarchy of the sons of forebears who succeeded to the presidency in spite of their incompetence. I can think of a community in New Hampshire that I am familiar with—a community that lived off the town plant. Successions of bad management, mostly oriented to the original family, drove everyone with managerial competence out of the company, destroying the mill and the town with it. Maybe a little "branch office" community, which today would be competitive and thriving, would not have been so bad, at that. But to be fair, is that what the antitrust laws are supposed to prevent? No, it is not. Constructive competition by companies like ITT, with good managements and with branches that do grow, is supposed to take care of that.

The fact remains that diversified companies are constantly seeking good communities in which to build plants and companies—just as good communities are seeking diversified industry. Our operating units which are responsible for the location of their new plants are constantly seeking new area communities. And ITT's operating units receive scores of visits in the course of a year from representatives of villages, towns, cities and states who are interested in having ITT operations in their communities. One of the greatest trends of constructive economy and social uplift that has been seen in this country (far more effective than any local government
could achieve) has been the vast number of plants that have been built in small towns throughout the newer and less developed areas of the country. Far from detracting from community growth, they have added greatly to it. In this respect, large and diversified companies have been fluid and responsive, providing employment and continued community support.

It is against this background that I would like to discuss ITT and its contribution to the economic and competitive stream of our economy.

Diversification: ITT's Objectives

The basic purposes and goals of ITT's diversification efforts are intended for the long-term protection and profit of its family of shareholders. We believe the purposes of such diversification are highly important to long-term stability, as well as to growth. Business is facing an increasingly fast-paced technical obsolescence trend, as well as increasing international competition, which is based on world economies of low labor costs and the constantly increasing technical capabilities within these low labor cost areas. Diversification and the consequent development of broad professional management skills are a necessity for protection and future development. Diversification is therefore a necessary type of corporate insurance which sound management must achieve on behalf of its stockholders, so that the risks of separate sectors are pooled and the alternatives of internal fiscal investment are provided.

The purposes of diversification in our case can be summarized as follows:

1. To diversify into industries and markets which have good prospects for above-average long-term growth and profitability;
2. To achieve a sound balance between foreign and domestic earnings;
3. To achieve a sound balance between high risk, capital-intensive manufacturing operations and less risky service operations;
4. To achieve a sound balance between high risk engineering-labor-intensive electronics manufacturing and less risky commercial and industrial manufacturing;
5. To achieve a sound ratio between commercial-industrial products and services and consumer products and services;
6. To achieve a sound ratio between government-defense-space operations and commercial-industrial-consumer products and services in both foreign and domestic markets; and
7. To achieve a sound balance between cyclical products and services.

Those are our motives and our purposes. They are designed to provide both growth and security for our employees and stockholders.

Diversification: ITT's Methods

There are many kinds of diversified companies — or "conglomerates." There are the old, respectable diversified companies, and there are new diversified companies. There are also different degrees of product and
market diversification. Most significantly, there are differences in management forms and techniques. Some differ in emphasis on operations versus, let us say, simple financial management. Others may be engaged primarily in securities promotion. In making acquisitions, some companies use straight equity securities, while others use warrants, debentures, installment payments and deferred pricing. There are friendly mergers, as well as hostile tenders and proxy fights; there are examples of both retained and replaced managements. There are resulting efficient companies and there are resulting relatively inefficient companies. Unfortunately, all of these differences are being indistinguishably merged into the generic term "conglomerate" which is now being widely and confusedly used. But the important fact is that each company is a different company. For example, diversified or conglomerate companies divide in one essential area. This point of division is whether they operate as a financial holding company or as a coherent operating company; that is, whether they provide within the parent company a broad group of central management skills, applicable not only to the overall corporate areas such as financing, law, and stockholder relations, but also to the operating areas of the company, such as production, marketing, planning, research and development, product development, and foreign operations.

ITT operates as a coherent operating company with a substantial central operating management. In fact, we have slightly over 1,000 industrial and operational specialists in our central management group. We have developed this expert group in order to improve both our competitiveness and our efficiencies, and to support our operating companies in improving operations in those fields, either new or old, which we have entered.

Again, acquisition policies are not the same for all diversified or conglomerate companies. The "pro" and "con" of the legal methods used and the economic justification of even "hostile tenders" have been well-aired in the literature. Let me state — for the record — that we have never made a hostile tender.

Let me point out, instead, the management and business value of friendly acquisitions. With the central management capabilities that ITT has assembled, we can provide receptive and constructive bases for merger — bases that will result in increased efficiency for both parties. For example:

1. We offer an assurance of continued support and growth in an innovative climate, leading to new products and fields through our informed management support of such a company.

2. We offer a concerned, helpful, and invigorating management atmosphere in which the new management members can grow. Opportunities for advancement are created within such an environment; and since these mergers are arrived at with the concurrence of management and stockholders, there is a "mutual accord" on improved objectives from the very start.
3. We can afford to price fairly and to exchange our own equity stocks with the shareholders of an incoming company. We can improve operating efficiencies and profits sufficiently to make this valuation worthwhile to both sets of shareholders. By exchanging equity stocks, the shareholders of the original company continue as equity participants in the family of ITT shareholders. We have used no unusual financial packages to support our growth.

It is significant, therefore, that many of the allegations leveled against a few conglomerates are simply not applicable to us or to the vast majority of diversified companies. These methods and the economic results brought about by the diversified companies such as ITT are thoroughly pro-competitive, pro-growth, and in the national interest. Other allegations which have been leveled against conglomerates include: reciprocity, concentration of power, questionable economic performance of acquired companies, predatory pricing, and finally, the allegation that the decision-making process is removed from the acquired company to the corporate headquarters of the conglomerate.

In considering each of these allegations, I think it well to define the starting place. ITT, like all companies, is in business to earn a fair profit, commensurate with its competitive performance and in full compliance with the law and the responsibilities of good corporate citizenship. We cannot afford to do otherwise.

Reciprocity

Efforts to purchase or sell goods or services on the basis of "reciprocity" violate a basic management principle, i.e., building a business soundly and permanently by being at all times capable of meeting open competition, and by having a trained business organization capable of meeting the challenges and problems created by competition. Only in this manner can a secure foundation and future be developed and built for a company. The theory of "reciprocity" is therefore repugnant as a basic business philosophy. Furthermore, it is my firm belief that efforts to purchase or sell goods or services on the basis of so-called "reciprocity" are completely uneconomical and are, in fact, a very unsound business practice. Such a practice dulls and distorts the efforts of both sales and purchasing staffs, dilutes the management responsibility for profits, and, in the long run, is certain to be costly and enervating to any company that practices it.

I am, of course, aware that there has been considerable talk during recent years about "reciprocity," and that in some companies, certain people have endeavored to create for themselves an executive-level career as a "Trade Relations" director. However, it is my opinion, based upon my 44 years of business experience in a rather wide variety of companies, that reciprocal buying and selling "gains" are largely illusory—and are more often "talked about" or "claimed" by self-serving Trade Relations directors, than ever realized on any significant scale. In addition, I have observed that salesmen, who must often have some excuse for losing a sale, may blame
their failure on what they think they see as reciprocity—where none in fact exists.

Most importantly, within ITT the very structure of our organization and the very wide variety of our products and markets create the necessity for a "profit center" organization in which it is simply impractical to attempt to practice reciprocity.

**Profit Centers**

The structure and organization of each ITT operating unit is a separate "profit center" having its own decentralized purchasing department and its own decentralized sales department. This structure effectively eliminates the motive, as well as any practical opportunity, for any attempt to utilize the volume of purchasing activities of one ITT profit center to benefit the sales activities of another. Since the professional reputation, compensation and, most importantly, the business career progress of the manager and management of each ITT profit center are dependent upon their record of performance (as shown by their own individual profit center), it is clear that these local managements have the strongest possible professional and career motivation to achieve maximum efficiencies in their own purchasing department. Consequently, they would not only strenuously resist any possible attempt to interfere with the efficiencies of their own purchasing departments for any claimed reciprocal benefit to any other profit center, but would consider this as a restraint on their own professional careers. In this day of shortage of executives and unlimited outside career opportunities, no company could afford to alienate its management by affecting their careers in this manner. Moreover, this would be alien to the entire philosophy of performance and efficiency, which is the very basis of ITT's whole management approach.

The practical situation, and the ITT management attitude, is best illustrated by the fact that ITT does not even waste the time or energy to accumulate the purchasing and sales data which would be necessary for "reciprocity" or "reciprocity effect." When the Department of Justice has on several recent occasions asked ITT to accumulate this data for the Department's current investigation, it has been necessary for us to send out special questionnaires to each of the local profit centers, and then specifically to assemble and compile the data to answer the Department's questions. This task was accomplished only after considerable effort and, I might add, complaining by the local purchasing departments about the tremendous waste of their valuable time in assembling, what they considered, useless data. And even the data assembled for the Department will rapidly become obsolete. The reluctance of our local managements and purchasing agents to spend their time in assembling such data further illustrates the complete lack of application of such information in our business operations and the lack of any significance to any allegation of "reciprocity" or "reciprocity effect." I might add that as a matter of corporate policy, when we first as-
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Assembled this type of purchasing information for the Department of Justice in 1966, we established procedures for the careful protection of the resulting list of large suppliers in order to ensure that it was limited to purchasing and legal channels, and was not made available to the ITT personnel responsible for sales or marketing. At the same time, in order to ensure that ITT's corporate policy against reciprocity was fully and clearly understood throughout the System, we issued a formal ITT Company Policy stating as follows:

Reciprocity

The United States Supreme Court has held that reciprocal buying practices or "reciprocity," is "one of the congeries of anticompetitive practices" at which the antitrust laws of the United States are aimed. Reciprocity is also an unsound business practice, since it distorts the market process and the normal development of economic efficiencies and product improvements. Consequently, for both legal and business reasons, it is the policy of ITT to purchase and sell products and services on the basis of the commercial criteria of superior quality, suitability, efficiency, service, and price.

No attempt shall be made to develop sales of any service or product through the use of, or threatened withdrawal of, any existing or potential reciprocal buying leverage or "reciprocity."

In this connection, information concerning ITT System purchases from particular suppliers shall not be made available to personnel who are concerned with developing sales and marketing.

This policy is still in effect, and we have recently taken extra steps to ensure that all ITT System purchasing and sales personnel are familiar with it.

Concentration of Power

Concentration of power is perhaps the subject that is the most misunderstood of any concerning the so-called conglomerate or diversified company. The problem is one of inadequate statistics and of misinterpretation. In the FTC Report, for example, it is stated that merger movements around the turn of the century and in the 1920's "left an indelible imprint on the structure of the American economy," and resulted in "an increase in market concentration." This subject of "market concentration" is, in fact, the only real economic issue. Market concentration does have a bearing on competition because competition or monopoly can only exist in some particular market. The voluminous FTC Report is a massive evasion of the real need for careful and objective analysis of market concentration. The reason so much time is spent in the FTC Report on the irrelevancy of "aggregate" or "overall concentration" or "super concentration" is simply to distract the reader's attention from a very important fact. The figures on market concentration have been so "unobliging" as to have shown no increase since World War II (and since long before then). Indeed, there

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3 FTC Report at 30, 33.
4 Id. at 33-34.
may possibly be some tendency the other way. That is why the FTC Report says very little on the key issue of "market-concentration" and, in fact, provides us with only some very questionable statistics and conclusions — and some truncated comparisons.5

5 For example, in the FTC Report at 214, the statement is made that in industries of high concentration, i.e., where the four leading companies did over 75 percent of total shipments, companies among the 200 largest did 87 percent of the business. In contrast, the largest corporations made only 14 percent of all shipments in industries with four-firm concentration under 25 percent. It takes some reflection before we realize how meaningless these two statements are. In an industry where the four leading companies make at least 75 percent of the sales, one would expect large companies in it to do about 87 percent of the business, and so they do. And in industries where concentration is very low, the participating companies, be they large or small, will do only a small percent of the business.

Much more objectionable is Table 4-1. This is summarized at 216:

For example, in 1958, 48 companies were among the four leading sellers in four or more industries; by 1968, there were 70. On the other hand, five companies in 1958 were leaders in no industries, and 18 were among the leaders in only one. By 1968, all of the 100 largest companies were among the top four sellers in at least one industry. In the short period of five years, the top 100 companies had greatly expanded their positions of leadership. Quite clearly then, the 100 largest companies have increased not only their share of total manufacturing but also their power-base.

The first thing to note is that the reference to "industries" is incorrect. It is the so-called 4-digit product groups which are referred to. If the increase is significant of an increased "power-base," then surely a decrease would have the contrary significance. If one examines the original source of Table 4-1, one finds that for the 5-digit products, which are generally closer to market realities, there is no such trend, or even one to the contrary. That is, 84 companies were among the four leading sellers in four or more product groups in 1958, while in 1968 the number was actually down to 52. In the short period of five years, the top hundred companies had, if anything, somewhat retrogressed. What the FTC Report did was simply to cut out one-half of the table in its source in order to produce a picture to support its argument.

The FTC Report itself shows that in 213 industries there was a decrease in concentration among producer-goods industries, and an increase among consumer goods. What it does not indicate is that if we take all 213 industries as a group, weight the concentration ratio in each industry by its economic importance, value added by manufacturer, we find that the average was virtually unchanged for the five-year period. But this sample of 213 industries comprises only about half of all census industries, which number about 440. Significantly, there was no attempt to show the weighted average for all industries in order to measure the industry concentration weighted average. The 213 comparable industries were those where product and industry definitions had not changed. They were therefore the least dynamic of the 440 industries. Hence, they were not a representative sample but a biased sample. There was no attempt to cover the whole range of industries.

For many years, there have been similar calculations of "aggregate concentration" and its alleged increase, along with prophecies that in a few decades the largest companies would take over the whole industrial economy. A well-known book written in 1932 by A. Berle and G. Means, The Modern Corporation and Private Property, predicted that between 70 percent and 85 percent of all industrial activity would be in the hands of the 200 largest corporations by 1950, and indeed said that within 30 to 40 years practically all industrial activity would be "absorbed by 200 giant companies," i.e., by 1960 or 1970. Id. at 40-41. There has been no such swallowing up of the economy, but this does not prevent other people from making predictions of doom. I believe Professor Mueller himself made such a prediction seven or more years ago. He was wrong then, as he is now.

Also interesting is Figure 3-2, which shows the years 1932-1952 as nonactive merger periods. But in 1947 and 1948 the Federal Trade Commission published two reports on "The Merger Movement" which added more apocalyptic prophecies: that this country would go down the road to Socialism, if the allegedly rapid merger movement was not reversed. FTC, The Merger Movement: A Summary Report (1948); FTC, The Recent
Moreover, there is serious "blurring" of the statistics as used. For example, there is no distinction made between a company such as ITT, which

**TREND OF Mergers AND Acquisitions (1947).** Years later, the truth is out; the *FTC Report* now shows that the 1932-1952 period was actually an unusually low merger period.

We cannot insist too strongly on this basic point: that "aggregate concentration" has simply nothing whatever to do with concentration in any given market. Nor has any change in aggregate concentration any relation to it. In theory, "aggregate concentration" could increase even when market concentration was decreasing in every single industry. In fact, such increase as there seems to have been in "aggregate concentration" has coincided with stability in industry or market concentration. "Aggregate concentration" would only have meaning if it were at far higher levels than is even dreamed of now, in other words, if say five large corporations accounted for all manufacturing, there could then be no more than five sellers in each individual industry, and perhaps only one in each. But as the Census Bureau statistics show, the largest hundred companies in 1966 accounted for only 33 percent of the value added in manufacturing. If this were true in every industry, that the largest hundred companies among them accounted for only one-third of value added, then American industries would be far less concentrated than they are today. Few, if any, industries would show so low a degree of concentration.

**CONCENTRATION RATIOS**

Distribution of the 100 Largest Companies According to the Number of Product Classes and Product Groups in Which Each is 1 of the 4 Leading Producers, 1963 and 1958.

(Number of Companies)

<table>
<thead>
<tr>
<th>Companies according to the number of product classes or groups in which they are the leading producers</th>
<th>4-digit product groups</th>
<th>5-digit product classes</th>
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<tr>
<td>All companies ........ 1963</td>
<td>100</td>
<td>100</td>
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<tr>
<td>1958</td>
<td>100</td>
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Companies among leading 4 producers in—

| 20 or more product classes | 1963 | 1958 | 3 | 10 |
| 15 to 19 product classes | 1963 | 1958 | 1 | 11 |
| 10 to 14 product classes | 1963 | 1958 | 13 | 22 |
| 7 to 9 product classes | 1963 | 1958 | 21 | 20 |
| 4 to 6 product classes | 1963 | 1958 | 32 | 19 |
| 2 or 3 product classes | 1963 | 1958 | 23 | 13 |
| only 1 product class | 1963 | 1958 | 7 | 5 |
| no product class | 1963 | 1958 | 0 | 0 |
has about $4 billion in sales and revenues (about 50 percent outside the United States and spread thinly over some 35 industries) and on this basis is ranked as the 11th largest United States industrial firm, and the company which is ranked 12th — Western Electric — which also does $4 billion, but entirely in the United States and all concentrated in one industry. Nor for that matter do the FTC statistics adequately distinguish between manufacturing activities as contrasted to service activities or the geographic source of income, and the relation of these activities to the so-called "manufacturing assets." In the case of ITT, the FTC statistics commit an error of almost one for one — or 100 percent — by including ITT's worldwide manufacturing and service activities in this sort of exercise. Similar substantial errors result with respect to many other large companies, such as mining, oil, automobile, business machine and other companies with high foreign growth. One must question the accuracy and meaningfulness of these statistics when one considers the rapid growth of services and the rapid growth of overseas activities of all large American companies in recent years.

Perhaps even more important is the fact that the implication of continually increasing aggregate concentration in a small group of companies does not follow from the statistics, since the list of 100 or 200 large companies keeps changing. It is a mathematical certainty that there will always be 100 largest companies, but it is important to recognize that they are not the same companies from period to period. This again indicates the conclusive effects of competition and change. For example, of the 50 largest manufacturing corporations in 1947 as tabulated by the Bureau of the Census, only 25 were among the 50 largest in 1966. Similarly, less than one-third of the top 100 companies in 1909 remain in that category today. What happened to the golden names in the other two-thirds? What happened to the traction companies? What happened to the gas companies? And what happened to the railroads? The emergence of the aviation and electronics industries and other new industries would be part of the answer. But I think the basic answer is in the failure of the managements of these companies to grow, diversify and change along with the economy, or in other words, the effect of competition.

Also disregarded by the FTC statistics is the simple fact that with respect to the growth in assets of the 200 largest companies between 1948 and 1968, only about one-fifth of the apparent aggregate increase in such assets can be ascribed to all large mergers by the 200 largest companies — horizontal, vertical, or conglomerate. Consequently, at least four-fifths of that apparent increase in assets was simply the result of non-merger growth by traditional horizontal companies. It is obvious that practically nothing significant of that apparent increase in assets is attributable to diversification mergers by the "new conglomerate" companies.

The FTC statistics on aggregate concentration also ignore the very important fact that about 85 percent of the assets of the top 100 companies in 1968 are accounted for by companies in the fields of chemicals, oil, primary
metals, fabricated metals, machinery, electrical equipment, automobiles and aircraft. These are all highly capital-intensive manufacturing operations; thus, perhaps all the FTC statistics on the assets of the top 100 companies really tell us is something of the increasing capital costs of heavy goods industries, of off-shore drilling and, of foreign oil investment, and of the growth of the automobile and airplane industries.

It is clear that ITT’s diversification acquisitions do not pose any threat of aggregate concentration of United States manufacturing assets. Although Fortune, and presumably the FTC, rank us as the 11th largest industrial company in the United States, about half of our operations are actually located outside the United States; and a very substantial portion of our activities in the United States are not in the manufacturing area at all, but are in the field of services and financial services. For example, ITT has a total of about 66,000 employees in its manufacturing operations in the United States; this represents about 0.3 percent of the total number of about 20,045,000 employees on manufacturing payrolls in the United States, according to the Bureau of Labor Statistics.

Consequently, I submit that it is unsound for anyone to suggest that ITT represents any kind of “aggregate concentration” threat, or indeed, any other kind of threat to the competitive structure of United States industry. I believe one could properly ask what the furor over increasing “aggregate concentration” has to do with conglomerates—or ITT—or adverse effects on competition? And the answer is clear—almost nothing.

But what are the important stakes for the American citizen and the national interest? We have agreed that excessive concentration within markets is not desirable because it may reduce competition, and competition is what spurs efficiency. We have also shown that diversified mergers do not increase market concentration but do increase competition. Efficiency is always desirable, but never more so than today. America’s position as a world industrial leader is challenged today by the resurgent nations of Europe and Asia, most particularly Germany and Japan. It is more than a coincidence that the two losing nations of the last world war today lead in economic enterprise and in growth of world trade. It is more than a coincidence that the governments of both these countries work very closely in support of their businessmen—a lesson they learned during the period of adversity, following the war, in which they rose to their present competitive strengths.

We can win that competitive struggle tomorrow as we did yesterday, but we must not be hampered with artificial strictures against diversification or size. We must not be hampered by yesterday’s myths when concentrating on today’s needs.

I contend that every year in American industry we can improve productivity better than the past average of 2½ and 3 percent per annum. But is even this enough? We must recognize that American salaries and wages are increasing at twice and three times that rate. We businessmen, almost
alone, must fill this gap! The gap's other names are inflation, balance of payments, taxes, and social unrest. We can fill this gap if we continue to stimulate the competitive drive; but we need the support, not the hindrance, of the government to do this.

Without increased efficiency, it is quite conceivable that the industrial economy of the United States could become second-rate. If we thwart our companies from growing, changing, and becoming more efficient, even when their growth has no effect on concentration within markets, we may be starting on that same downhill road traversed by the traction companies and the other "golden names" from the past.

American know-how is no longer unique. Our increasing deficits in the balance of payments area are bluntly telling the cost of this mounting efficient foreign competition. This same story is being told by the increasing variety and abundance of imported goods within the country.

Detroit's massive production lines are now matched across the world. In Asia, we see the Japanese auto industry, with labor rates one-quarter those of Detroit, rapidly approaching a technologoical level comparable to our own. We see their products in the United States in increasing use. This is a trend. We must now meet the challenges implicit in a world awakened to all of the factors in the economic struggle.

It is not my purpose to object to the flow of foreign competition for the benefit of the American consumer. It is my purpose to point out the need for greater efficiency and performance on the part of our domestic companies, and to point out that better understanding and greater support of the needs of American business by its government is of vital importance to the national interest of the United States — and one of those needs is the ability to diversify and enter new competitive fields.

**The Allegation of Questionable Performance of Acquired Companies**

The recent FTC Report pointed out that it is not possible to measure efficiency from merger by simple before and after comparisons — since prices and costs vary over time; there are changes in product development strategies, capital investment programs, and research and development expenses. There are also important changes in markets, customers, general economic conditions, inflation, taxes and many other factors. Additionally, the FTC Report stated that the recent performance of a few conglomerates indicates that they are not immune from ordinary management problems.

I would like to make it very clear that we do not claim that our form of diversified corporate organization, or our form of open management system, makes ITT immune from ordinary management problems, or any other kind of economic or business problems. We do not claim that our management system provides a cure-all for every problem that may arise

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6 FTC REPORT at 86.
7 See id. at 103-16.
CONGLOMERATES: A BUSINESSMAN'S VIEW

within one of our subsidiaries or profit centers. However, I am convinced from my own 44 years of business experience, and from the experience of the large number of other experienced and capable corporate executives who constitute the ITT management team, that the ITT System can provide the operating units with the maximum assistance that intelligent and responsible professional management can produce.

Keeping in mind the practical problems I have just noted with respect to the lack of direct comparability of "before" and "after" profit performance figures, I believe that the companies which have joined the ITT System have successfully met the problems of drastically increasing labor and material costs, the problems of higher state, local and federal taxes of all kinds, and the problems of increasing competitive pressures in every market we serve, and have generally increased their profits at average annual rates between 10 and 15 percent per year.8

8 In order to gain a rough idea of the magnitude of these practical business problems, one must realize that the U.S. Department of Labor has reported an increase of 56.1 percent in average weekly earnings for United States manufacturing workers during the period from 1958 to 1969, including an increase of 6.1 percent in the last year alone! The increase for contract construction workers was 80.6 percent during the period from 1958 to 1969, including an increase of 9.8 percent in the last year!

Similarly, the Bureau of Labor Statistics recently reported that the nation's unit labor costs have increased by 1.6 percent in the third quarter of 1969, and that the national productivity has actually decreased in this same period by .4 percent. And, therefore, the best the United States economy can hope for during the year 1969 is the poorest productivity increase since 1956.

These increased wage rates are reflected in both our own direct labor costs and in the costs of all the materials and supplies which we purchase.

For example, the U.S. Department of Labor reports the following substantial increases in the wholesale price index for commonly purchased metals and metal products:

<table>
<thead>
<tr>
<th>Product</th>
<th>% Increase 1958-Aug/1969</th>
<th>% Increase 8/68-8/69</th>
</tr>
</thead>
<tbody>
<tr>
<td>Semi-finished Steel Products</td>
<td>13.3%</td>
<td>5.3%</td>
</tr>
<tr>
<td>Gray Iron Castings</td>
<td>30.6%</td>
<td>3.4%</td>
</tr>
<tr>
<td>Copper, Wirebar Electrolytic</td>
<td>64.8%</td>
<td>14.6%</td>
</tr>
<tr>
<td>Copper Water Tubing (in coils)</td>
<td>51.9%</td>
<td>28.0%</td>
</tr>
<tr>
<td>Zinc, Slab, Prime Western</td>
<td>30.0%</td>
<td>7.2%</td>
</tr>
<tr>
<td>Red Brass Ingot</td>
<td>76.8%</td>
<td>18.5%</td>
</tr>
</tbody>
</table>

How have ITT's United States operations and manufacturing units coped with this very serious problem of the cost-price squeeze?

If we take the year 1968, for example, we find that our profit margins have narrowed, yet we have been able to increase our profits through plain hard work, new plant investment, and by achieving cost reduction efficiencies in our plants, increased productivity, increased capacity utilization and increased sales per employee. Vigorous and increasing competition from both United States and foreign competitors makes it impossible to meet this squeeze by trying to pass on the entire increase in our own prices; the results of price increases by United States industry can be seen in increasing imports of foreign steel, autos and electronic products.

But despite these continual problems of inflation, mounting unit costs, increasing competition in all markets, and lower margins, despite the specific problems experienced by any particular ITT profit center along with the other members of their particular industry, and despite the occasional mistakes which will inevitably be made by any company, the performance record of the ITT System as a whole would be outstanding by any
PREDATORY PRICING

I can assure you that, as businessmen, we at ITT do not enjoy losing money, and we do not intentionally price below our cost. Indeed, the managers in charge of our individual profit centers work hard to reduce their costs when they see that their competitors are in a position to sell at lower prices over the long term. I believe that theories that big diversified companies can and will engage in "predatory" pricing, subsidizing one profit center with the earnings of another in an attempt to monopolize a market, are folklore—not fact. Such allegations may be numerous, but the evidence is practically nonexistent. While the businessman who lost a sale on price would like to think his competition is indulging in sales below cost, I have found that, in reality, the rival's lower price means that he is more competitive, and that his costs are actually lower.

THE DECISION-MAKING PROCESS

Insofar as ITT is concerned, nothing could be further from the truth than the allegation that the decision-making process is removed from an acquired company to corporate headquarters. If the decision-making process were removed from the divisional level, we would be unable to retain the excellent management we have been able to assemble to operate our various centers. And it would be impossible to operate them from headquarters.

ITT Headquarters personnel act essentially as an expert management consultant staff. We do not manage any of the line operations from the Headquarters in New York City. Our policy is to have each operating unit do as much of its own work as possible.

The major contribution which ITT brings to the companies which join the ITT System is the approach and atmosphere of a sound and effective modern management system. The ITT management system emphasizes detailed and realistic short- and long-range planning and budgeting developed by individual profit centers, effective controls for the ascertainment and measurement of actual performance in comparison to budgeted performance, prompt ascertainment of problem areas and effective and prompt constructive and corrective action, and the utilization of an effective consulting staff to provide advice and assistance in these and other matters, such as quality measurement and control, cost effectiveness, greater operating efficiencies through industrial, installation, manufacturing and product and value engineering, production and inventory control, transportation and traffic cost control, purchasing techniques, real estate procurement and comparison over a 10-year period. That record is one of a stable, annually compounded increase in earnings-per-share at the rate of about 11 percent over each preceding year for 10 successive years. We believe this 10-year record speaks for itself with respect to the soundness of our form of diversified corporate organization, as well as our management systems and techniques. A 10-year summary of this growth would show an increase in earnings-per-share from 95 cents per share in 1959 to $2.58 per share in 1968 (see Appendix).
CONGLOMERATES: A BUSINESSMAN'S VIEW

Disposition, technical and R&D programs, effective control of accounts receivable, legal, patent and tax advice, personnel recruitment and the many other aspects of business management where the advice of trained, qualified and proven professional experts can be of assistance. We encourage and assist our profit centers in establishing unusually high goals for growth and profit performance — ordinarily a goal of 15 percent increase in net earnings each year — but we also assist and support our profit centers in planning realistic methods and techniques for actually achieving those goals.

ITT could be described as a management cooperative — a group of small companies, each competing in its own industry and each sharing in and supporting the cost of a skilled central management it could not afford alone. We have an “open management” system which 1) stresses flexibility — continuous fact gathering and analysis, and continuous questioning with sufficient flexibility to change decisions and directions; 2) stresses communications — including face-to-face communications on the details of problems, on a continuing basis; 3) is action-oriented, stressing prompt action to solve business problems; and 4) stresses the early recognition and rapid development of individual management skills at all levels of the company.

No form of organization can be effective unless it develops and encourages the necessary management skills in its executives at all levels, offering them corresponding rewards in career progress and compensation. In time, such an atmosphere of assistance and high goals encourages the utmost in hard work and outstanding performance. The wide diversification of ITT provides great opportunity for individuals to move to positions of responsibility, to secure recognition for their own contributions, and to rise in the organization on merit, irrespective of age, seniority, family connections, or other barriers to achievement that are often associated with traditional business. For example, the average age of the executives in ITT’s central management group is about 44 years — as compared to a range of 47 to 52 years in most other companies.

Despite, and perhaps even because of our ability to motivate, train and move able young executives into positions of wide responsibility — and despite our policy to reward high performance, it has become well known in industry that ITT constitutes an effective training school for management executives — and we find that our trained executives are in great demand for the top management positions in other companies. At least seven corporate presidents of substantial companies have come from the ranks of ITT executives in the last few years. While we naturally hate to lose our executives to other companies, we feel that this substantiates the nature of the corporate executive we are training.

ACCOUNTING TECHNIQUES

Other questions have been raised concerning the accounting techniques used by diversified companies. Particularly, there is considerable discussion
of the use of pooling of interest and the amortization of goodwill. Briefly, this is our position on these subjects.

ITT has not utilized any form of unusual accounting techniques to enhance its reported earnings. Our acquisitions involving exchanges of stock have customarily been accounted for as pooling of interests, with no material effect on the current reported earnings-per-share of the combined company; and the principles of pooling permit stockholders and investors to compare the combined company's current performance with the comparable restated earnings of the companies for prior periods, so that there can be no illusory increase in performance.

Extensive discussions have been carried on within the accounting profession during recent months with respect to the most desirable techniques for accounting treatment of mergers and acquisitions. ITT has always followed sound and conservative accounting principles, and we shall continue to do so.

We believe that the business future of ITT is dependent upon the utilization of good management techniques and established business principles, as well as the sound use of available capital resources in order to develop a strong and continuing stream of earnings in growth industries. It is obvious that this type of sound business growth can not be constructed out of other than sound accounting techniques. We believe that merger accounting principles should be neither pro-merger nor anti-merger, but should simply endeavor to reflect as clearly as possible for stockholders and the investing community the effect of a combination of two earnings streams and two sets of economic values. Further, we regard the pooling of interest principles as a convenient and accurate method of accounting for business mergers. And finally, we believe that reasonable provisions can be established by the accounting profession and the Securities and Exchange Commission to eliminate any accounting abuses or deficiencies which may exist, and that the entire business community will support efforts in that direction. It should be noted, however, that there have been no such problems in the diversification mergers made by ITT.

CONCLUSION

In summary, I would like to reiterate that a highly diversified company — like ITT — produces a beneficial impact on the United States economy. Companies like ours contribute directly to economic strength by checking inflation, by decreasing costs through more efficient production, by stabilizing employment, by increasing the financial strength of local communities, and by insuring a fair return to the investors.
## APPENDIX

International Telephone and Telegraph Corporation and Subsidiaries Consolidated

### TEN-YEAR SUMMARY*

(Dollar amounts in thousands except per share figures)

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<tbody>
<tr>
<td><strong>Result for Year</strong></td>
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</tr>
<tr>
<td>Sales and revenues</td>
<td>$4,065,502</td>
<td>2,760,572</td>
<td>2,121,272</td>
<td>1,782,939</td>
<td>1,542,079</td>
<td>1,414,146</td>
<td>1,090,198</td>
<td>930,500</td>
<td>811,449</td>
<td>765,640</td>
</tr>
<tr>
<td>U.S. and foreign taxes</td>
<td>$290,456</td>
<td>204,069</td>
<td>162,179</td>
<td>155,615</td>
<td>120,034</td>
<td>87,345</td>
<td>65,812</td>
<td>54,133</td>
<td>50,266</td>
<td>45,343</td>
</tr>
<tr>
<td><strong>Income before extraordinary items</strong></td>
<td>$180,162†</td>
<td>119,221†</td>
<td>89,910</td>
<td>76,110</td>
<td>68,164</td>
<td>52,375</td>
<td>40,694</td>
<td>36,059†</td>
<td>30,570†</td>
<td>29,036</td>
</tr>
<tr>
<td><strong>Per common share</strong></td>
<td>$2.58</td>
<td>2.27</td>
<td>2.04</td>
<td>1.79</td>
<td>1.55</td>
<td>1.35</td>
<td>1.21</td>
<td>1.09</td>
<td>.98</td>
<td>.95</td>
</tr>
<tr>
<td><strong>Return on stockholders' equity</strong></td>
<td>12.2%</td>
<td>11.7%</td>
<td>11.5%</td>
<td>10.8%</td>
<td>9.9%</td>
<td>9.1%</td>
<td>8.6%</td>
<td>8.0%</td>
<td>7.4%</td>
<td>7.2%</td>
</tr>
<tr>
<td><strong>Dividends per common share</strong></td>
<td>$.87½</td>
<td>.77½</td>
<td>.69¾</td>
<td>.61¾</td>
<td>.55</td>
<td>.50</td>
<td>.50</td>
<td>.50</td>
<td>.50</td>
<td>.50</td>
</tr>
<tr>
<td><strong>Gross plant additions</strong></td>
<td>$362,069</td>
<td>238,141</td>
<td>168,049</td>
<td>145,629</td>
<td>119,536</td>
<td>123,241</td>
<td>114,584</td>
<td>105,311</td>
<td>66,809</td>
<td>84,219</td>
</tr>
<tr>
<td><strong>Provision for depreciation</strong></td>
<td>$158,333</td>
<td>116,120</td>
<td>73,875</td>
<td>63,737</td>
<td>50,713</td>
<td>39,378</td>
<td>30,763</td>
<td>31,341</td>
<td>25,066</td>
<td>27,433</td>
</tr>
<tr>
<td><strong>R &amp; D expenditures</strong></td>
<td>$210,000</td>
<td>210,000</td>
<td>220,000</td>
<td>182,000</td>
<td>174,000</td>
<td>170,000</td>
<td>150,000</td>
<td>131,000</td>
<td>126,000</td>
<td>117,000</td>
</tr>
</tbody>
</table>
APPENDIX (continued)

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</tr>
</thead>
<tbody>
<tr>
<td>Net current assets</td>
<td>$672,567</td>
<td>528,713</td>
<td>318,957</td>
<td>367,012</td>
<td>308,055</td>
<td>338,849</td>
<td>296,155</td>
<td>268,422</td>
<td>269,324</td>
<td>222,269</td>
</tr>
<tr>
<td>Plant, property and equipment (net)</td>
<td>$1,835,793</td>
<td>1,305,829</td>
<td>895,438</td>
<td>789,849</td>
<td>668,240</td>
<td>572,469</td>
<td>462,328</td>
<td>391,347</td>
<td>288,461</td>
<td>355,115</td>
</tr>
<tr>
<td>Total assets</td>
<td>$4,022,400</td>
<td>2,961,172</td>
<td>2,360,435</td>
<td>2,021,795</td>
<td>1,688,853</td>
<td>1,469,168</td>
<td>1,235,781</td>
<td>1,088,310</td>
<td>923,944</td>
<td>932,269</td>
</tr>
<tr>
<td>Long-term debt</td>
<td>$931,772</td>
<td>744,675</td>
<td>483,834</td>
<td>428,124</td>
<td>309,795</td>
<td>293,408</td>
<td>266,815</td>
<td>182,509</td>
<td>148,478</td>
<td>165,512</td>
</tr>
<tr>
<td>Stockholders' equity</td>
<td>$1,652,092</td>
<td>1,143,568</td>
<td>820,007</td>
<td>759,620</td>
<td>659,925</td>
<td>592,429</td>
<td>483,531</td>
<td>465,061</td>
<td>415,814</td>
<td>415,088</td>
</tr>
</tbody>
</table>

YEAR-END STATISTICS

| Orders on hand (Manufacturing) | $1,529,000 | 1,257,000 | 1,233,000 | 1,140,000 | 1,004,000 | 917,000 | 778,000 | 731,000 | 628,000 | 551,000 |
| Shares of common stock outstanding (thousands) | 59,059 | 49,940 | 42,168 | 40,530 | 38,720 | 36,924 | 33,258 | 32,750 | 31,362 | 31,060 |
| Stockholders |
| Employees | 185,184 | 130,671 | 109,203 | 106,298 | 104,413 | 100,269 | 92,362 | 94,719 | 87,818 | 88,230 |
| Employees | 293,000 | 236,000 | 204,000 | 199,000 | 185,000 | 173,000 | 157,000 | 149,000 | 132,000 | 136,000 |

* The above data are as reported in the ITT Annual Reports for the respective years, except that number of shares and per share amounts have been adjusted for 2-for-1 stock split effective January 26, 1968.