

"THE INCIDENCE OF
ADVERTISING
COST"

by

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PREFACE

The following analysis of the incidence of advertising cost was undertaken in hopes of clarifying some of the existing confusion regarding this problem. In making this study I have drawn heavily upon the works of others and wish to hereby make my acknowledgements. While attempting to find and use as much statistical evidence as possible, I have been compelled to fall back upon the deductive method to a large extent. This necessity arises from the scarcity of satisfactory objective data. My approach has been first, an examination of the effects of advertising upon production and marketing costs, followed by a consideration of the influence of advertising upon demand. This analysis of the direct relation of advertising to prices has been supplemented by an examination of the more indirect influence of advertising upon economic values, such as the relation of advertising to the stabilization of demand, to standardization, to market research, to monopoly, and finally its relation to the allocation of economic resources. A concluding section has dealt with the potential efficiency of advertising. As a result of this study the following conclusions were reached.

In the first place it was found that in many cases advertising was able to lower production costs. But this reduction in costs was seldom the result of mere increase in

output--the usual explanation. In fact we found that for certain types of goods, greater production in and of itself tended to cause increasing or constant cost. We were obliged, therefore, to explain the fact that advertising was accompanied with falling costs on another basis, namely improvements in production technique. In the discussion regarding marketing costs the conclusions were similar: Advertising has had little opportunity to lower total distribution expense. We found that with an increase in the scale of operations, there was a very strong tendency for distribution costs to rise--a trend which advertising was not able to counteract. Any tendency for marketing expenses to fall seemed to be due to better methods of distribution. It ought to be added, however, that there is reason to believe that advertising is a more economical, efficient means of demand creation than any other substitute agency. As a result, if advertising is used to build up sales, costs are kept from rising as high as they might otherwise go. This amounts to a relative reduction of marketing expenses.

In the next chapter the effect of advertising upon demand was analyzed. While it was found that advertising has accomplished a great deal in educating the consumer to a better standard of living, it was also pointed out that this educational force often operates in the wrong direction, namely in developing more or less pernicious wants. On the

whole advertising tends to offer a rather serious interference with the consumer's guidance of production. The section following has dealt with the influence of advertising upon the existing economic system. These results of advertising, although they do not bear directly upon prices, tends to alter the economic system in which prices are determined, and hence influence values or prices in the end. In this discussion it was pointed out that advertising was a potent factor in many cases in stabilizing demand, and in furthering market research and standardization. Advertising's influence upon competition, however, was problematical. It might be argued, for example, that advertising makes for better competitive conditions because it supplies the producers and consumers with marketing information--thereby causing a closer approximation of a perfect market. On the other hand, it is contended that advertising tends to destroy competition and to create monopolistic conditions. The arguments are inclusive on either side; but it should be pointed out, however, that in actual practice the "monopolies" which advertising tends to establish do not give the advertisers much power. Finally, we analyzed advertising's effect upon the allocation of our economic resources. It is true that a justification of directing over a million dollars' worth of our factors of production into the advertising business, might be made upon the grounds

that such an expenditure increases our productive efficiency. It is difficult, however to defend the influence advertising has had upon society's use of resources in other directions. Not only does advertising draw upon the limited resources of mankind for its own purposes, it is also a factor in helping consumers decide what goods and services will be produced. Some of the decisions do not seem socially desirable.

In the final chapter the future of advertising was considered. The aim was to determine whether advertising would tend to have a more salutary influence upon prices in the future. With this in mind the various possible sources of improvement were discussed, together with a brief consideration of the newer trends in advertisements. An analysis of what part the government might take in the solution of the advertising problems, lead us to the conclusion that the improvement of advertising will come as a result of the natural forces at work in the present competitive regime.

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THE INCIDENCE OF ADVERTISING COST.

I. Introduction.

"All national advertising tends to create vicious chains in which the increases in national advertising appropriations by manufacturers tend to increase the price level of all goods." (1) This arraignment is but an expression of a current belief held by many people that advertising tends to increase prices. On the other hand, there are those, particularly advertising men who are of an opposite opinion. "Not only are goods better because of advertising, they are better distributed, lower in price, and the labor of selling them has been reduced", (2) is the verdict of one eminent authority in the field. Here are two diametrically opposed views, one implying that consumers bear the advertising costs in higher prices; the other that there is no increased cost to bear. It would seem that, since both sides could not be correct the subject calls for clarification. It will be the purpose of this dissertation, therefore, to attempt an analysis which will throw some light

(1) Borsodi, Ralph, "The Distribution Age", D. Appleton and Company, 1927, page 247.

(2) Calkins, E.E, "Reading With A Purpose: Advertising", American Library Association, 1929, page 21.

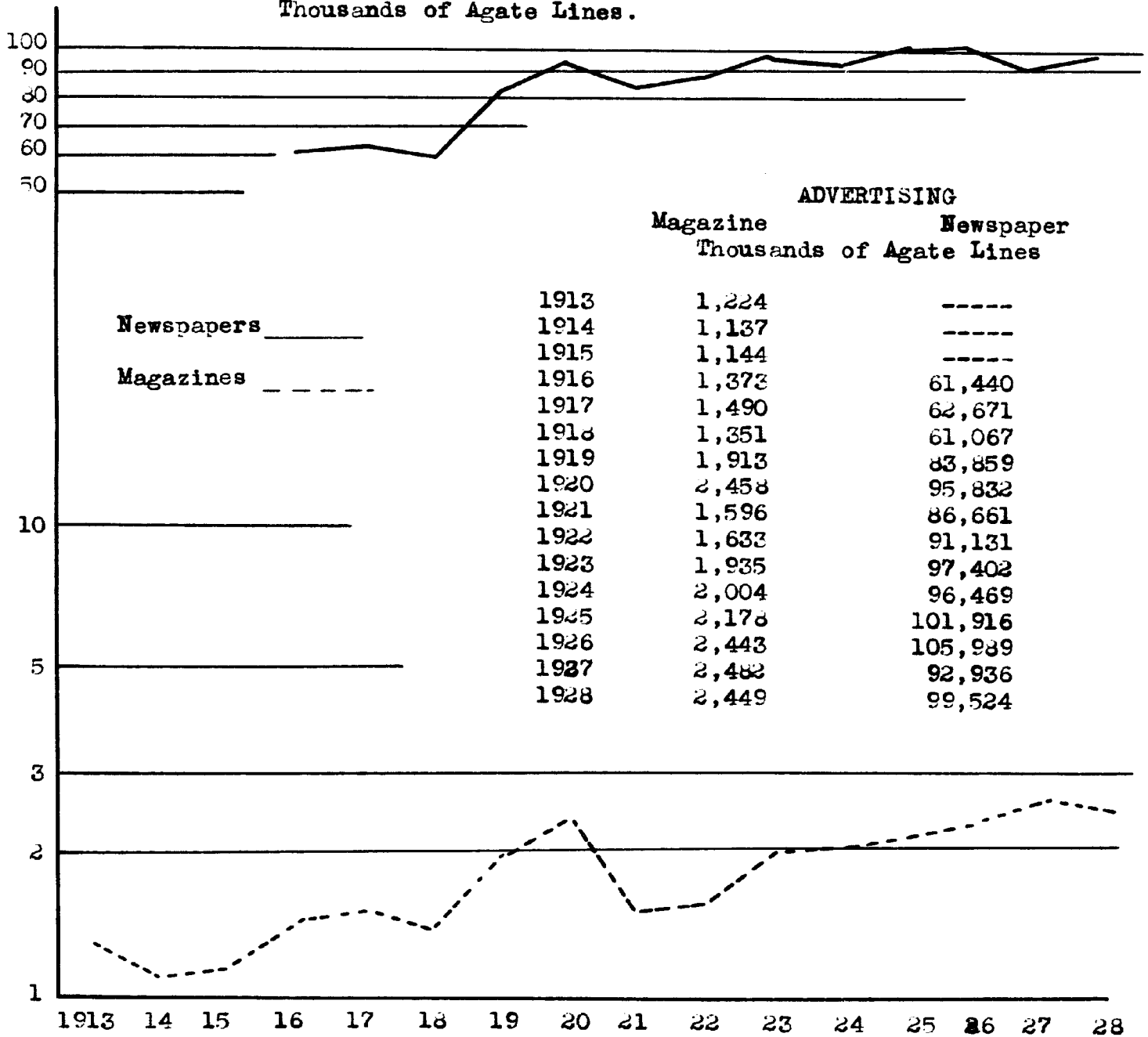
upon this controversy, (1) regarding the incidence of the cost of advertising. Before entering into this discussion it may be well to briefly consider the growth and general status of the advertising business. The Survey of Current Business, published by the Department of Commerce reports monthly averages of agate lines used in magazines and newspapers since 1913. Charting these a graphic picture is obtained of the growth of advertising since the pre-war period. (See Chart I) In both cases there has been a fairly steady increase in the number of lines used except perhaps for the considerable relapse during the depression of 1920-21. As for the amount spent upon advertising every year, The Market Data Book for 1928 makes the following comments: "Exact statistics regarding the total amount spent annually on all varieties of advertising in the United States are not obtainable, but a recent estimate places the sum at not

- (1) This controversy about advertising is not a recent one, but is as old as the industry itself. The following excerpt from an early article is a defense of advertising which might well have been written in 1930. "Advertising, is indeed, one of the great developments of the century. It has revolutionized business, and made it possible to accomplish in a few years what otherwise would have taken generations to compass. Nor has this advertising benefited the seller only. It has brought to the knowledge of the buyer the hundreds of improvements and articles by which life can be made more pleasant, by which the health can be preserved, the palate gratified, the intellect fed and satisfied. It is no exaggeration to say that no force has contributed more to knit the world more closely together. 'It is but the simple truth to assert', says a recent (Continued on page 4)

Chart I.

Magazine and Newspaper Advertising. (1)
1913-1928

Thousands of Agate Lines.



less than \$1,250,000,000. Moreover, there are 600,000 men directly connected with the advertising business. The amounts spent on each form were divided as follows in 1926:" (1)

TABLE I

ADVERTISING SPENT IN 1926 ON SEVEN TYPES(1).

1. Street Car Cards	\$ 15,000,000
2. Outdoor Advertising	65,000,000
3. Farm Papers	30,000,000
4. Business Papers	100,000,000
5. General Magazines	177,000,000
6. Direct Mail	300,000,000
7. Newspapers	<u>736,000,000</u>

TOTAL FOR THESE SEVEN TYPES \$ 1,423,000,000

Thus there seems every indication that the advertising industry is not languishing; that fact of itself might seem to some, who are accustomed to reason that economic forces tend to weed out inefficient instruments of production, a priori evidence that advertising might be economically defensible. Whether it is or not becomes an affair of more than passing interest in view of the fact that the industry is making a rather large

(1) (Continued from page 2) writer, 'that the loss of information which the advertisements furnish would be one of the greatest imaginable misfortunes to civilization'. Printers' Ink, October 11, 1899.

(1) Grain, Jr. G.D., The Market Data Book, 1928. Chicago, Illinois.

drain upon our productive resources.(1)

Perhaps it may be important before proceeding to the analysis of our problem, to explain what is meant by advertising. In ordinary usage the word seems to mean the paid-for publicity which helps to market the goods and services of business. As George P. Rowell in his book "Forty Years an Advertising Agent" puts it: "Advertising is publicity, a means of causing it to be known what service you or I can render, what wants we can satisfy; and the reasons why that service should be sought at our hands." Most individuals would agree to some such definition, though there will probably never be a definition that would gain universal acceptance, since advertising is continually changing. There are some writers, who expect advertising to signify much more than merely the effort to sell goods.(2) In their opinion advertising should be widened in its use to include such publicity as announcements of Community Chest Fund drives, and propaganda in support of other civic, political, health and religious organizations. While it is legitimate to designate such activities as advertising, nevertheless, the present discussion will refer to the narrower

- (1) It is estimated, for example, that the 600,000 men employed in advertising constitute about 1.5% of those gainfully employed.
- (2) For such a usage see Cherington, Paul T., "The Consumer Looks at Advertising", Harpers, 1928.

definition, publicity which is used as a selling agency in business.

Not only must the definition of advertising be circumscribed in this limited sense for our discussion, but a further discrimination must be made between two radically different concepts of advertising which are exceedingly prominent in present-day writings. As one author has expressed it, "Advertising may be of two sorts. It may be either informative or competitive". (1) While the present writer would quarrel with such a division as being illogical - for reasons that will be brought out later - yet the idea of designating carefully what is meant by advertising is sound because part of the controversy over advertising is traceable to the absence of such a precaution. The antagonists of advertising have in mind one concept of advertising and the protagonists another. "Competitive" advertising is a misnomer, if the purpose is to earmark a certain type of advertising, because all advertising is and should be competitive in the true sense of the word. What is meant by the term is that kind of publicity which accentuates brand competition. Advertising of this nature, it

(1) Vaile, R.S., "Economics of Advertising". Ronald Press Company, New York, 1925, Page 130.

is thought, tends to befog the consumer and make him buy foolishly. Nor is the term "informative" advertising a helpful notion for this discussion, since the connotation of the phrase suggests that such advertising is good, educating the consumers to be better buyers. But the truth of the matter is that neither is the so-called "competitive" advertising to be censured in the manner it is, nor is the "informative" type to be acclaimed as all good. This point has been well stated as follows: "The fact is that much of the worst advertising is of the informative type. Peruna, unsound stock issues, and in fact the great bulk of illegitimate advertising is distinctly of the informative type. So also I believe that the so-called competitive advertising is a distinction very largely supported by people who know little of the merchandising processes. The fact that two stores in the same town are competing for trade and are spending more money in doing so than (those) who know nothing about their problem would approve is no evidence that this advertising is illegitimate either as guidance to the consumer, as stimulation to their efforts at production, or even as cost reducing influence with the organizations themselves."(1)

Another manner of classifying advertising -- as part and parcel of high-pressure marketing -- needs to be commented upon in the endeavor to clarify what should be meant by advertising. Critics have in mind that such a designation in and

(1) Moriarty, William D., author of "Economics of Marketing and Advertising."

of itself condemns advertising, but such is not the case. There is nothing socially or economically wrong about the use of powerful advertising methods to win a large sales volume for an industry. In fact, the test of whether advertising is economically justifiable should rather be: Does it create a relatively large amount of economic utilities with a given amount of resources? Man is in a position in which he has limited economic factors or resources from which to produce goods and services for his unlimited wants. In order for advertising to fit into such a productive system it must be able to accomplish some part of the productive process, such as demand creation, with a smaller drain upon society's resources than any alternative method would occasion. If it does this, it will tend to give man more economic goods and hence will react favorably upon economic values. The measuring rod of the economic value of advertising is by no means the amount spent upon it. Millions used for high-pressure advertising does not necessarily condemn it; in fact it might be discovered that such a use of resources is a wise employment of them in view of the results obtained from the standpoint of both the producer and society at large.

If it seems, therefore, that defining advertising as "competitive" or as part of high-pressure selling, is not very helpful, what should be our recourse in this dissertation? When advertising is said to lower or to raise the cost of merchandising, or some other economic consequence is commented

upon in attempting to determine the incidence of the cost of advertising, what kind of advertising will be meant? Certain out-and-out predatory types of publicity such as that for nostrums and bogus stock and of fly-by-night concerns will be excluded; but in the main, we will take advertising as it is used in industry and attempt to determine who bears its cost. In order to do this we must examine the effect of advertising upon prices. Let us now proceed to this discussion.

PART II

THE EFFECTS OF ADVERTISING UPON
THE COSTS OF PRODUCTION.

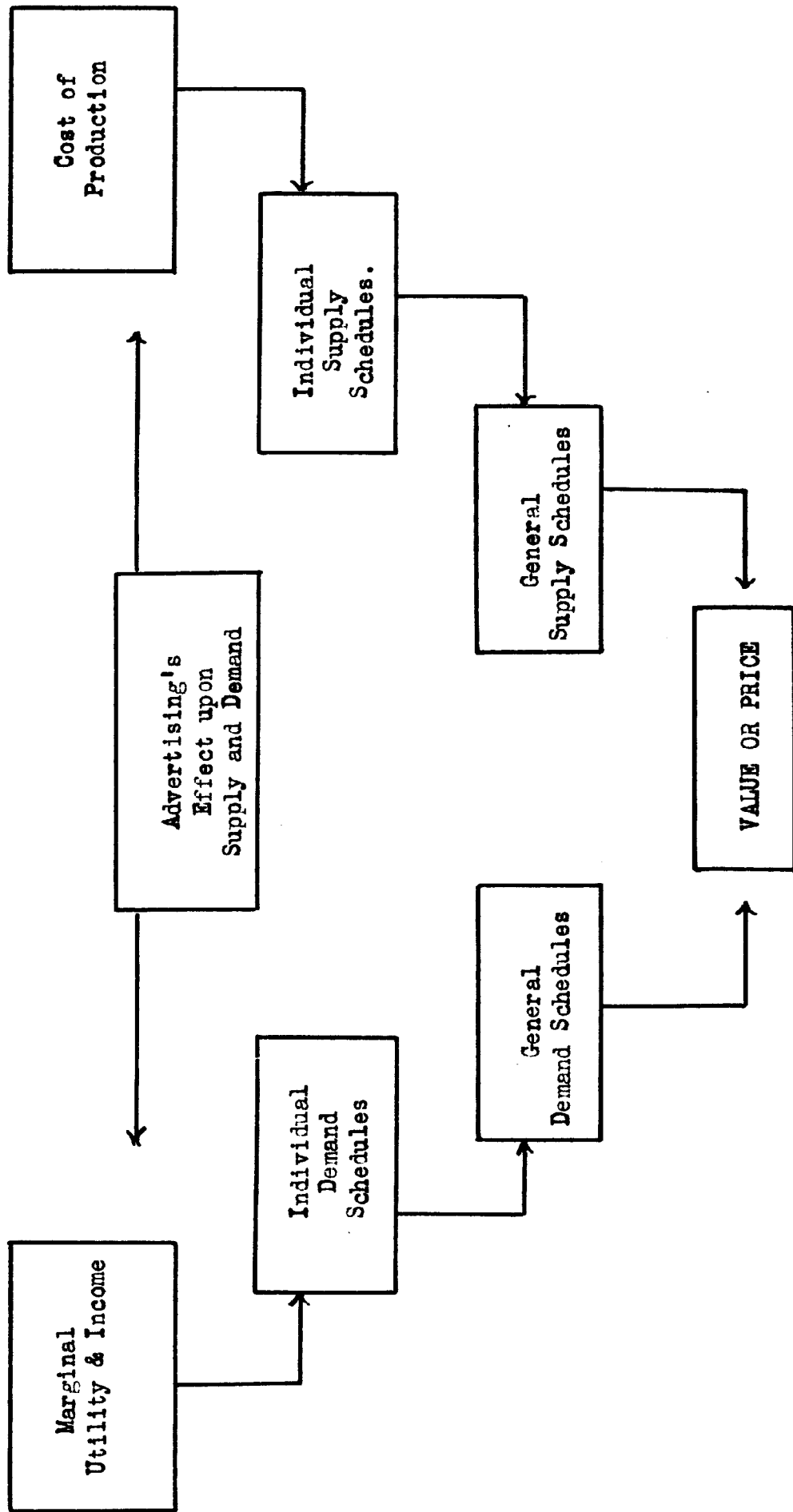
In the last section it was brought out that in order to determine the incidence of advertising cost it would be necessary to analyze the effects of advertising upon price. Since price or economic value is the outcome of the demand and supply forces of the market, our problem becomes one of analyzing the influence of advertising upon these determinants of price. Price may be considered either from the immediate or from the long run point of view. In the first case, price is determined by the market supply and demand schedules -- those which result from momentary, temporary forces, such as weather, rumors and the like. While an analysis of the effect of advertising upon market price might be fruitful, the present work will deal with normal price, which is an outcome of the more permanent supply and demand elements.(1) By Supply is meant the amount which sellers stand ready to dispose of at each of a series of prices and likewise by demand the amount buyers are willing and able to buy at each of a series of prices.

In a normal supply schedule it is marginal cost of production which determines what quantities are forthcoming at

(1) For a discussion of these forces see Taylor, F.M., "Principles of Economics, Chapters 24 and 25. Also, Marshall, A., "Principles of Economics", Book V.

every price. On the other hand, behind normal demand lies the marginal utility of the goods to the consumer, and the income of the demander. This sequence of causation has been schematically arranged in Chart II. in order to make the presentation clearer, and also to show wherein lies our field of inquiry. Thus in the main our method of approach will be to investigate the effect of advertising upon the supply of goods and its effects upon the demand for goods. We will find, however, that all the economic consequences of advertising do not fall squarely into these two divisions of the work. For example, there remains a family of problems such as the effect of advertising upon the business cycle, upon concentration in industry, upon resource costs, which do not deal directly with entrepreneur's immediate cost of production more with the attitudes of the buyers. These questions, however, have important bearings upon economic values, and will be treated in a separate section forming a significant part of this appraisal of the economic efficiency of advertising. It will be the work of this chapter, however, to take up the effect of advertising upon costs of production. Cost as used in Chart II refers not only to the money outlay of the manufacturer for production but also to his marketing expense, as well as to all of the expenditures of the middlemen who handle the goods until the consumer buys them. But in the following discussion this cost of production will be broken down into its component parts

CHART II.



and each investigated separately.

The first consideration will be the effect of advertising upon the producer's cost of production, leaving the effects of advertising upon marketing costs to another part of the paper. The protagonists of advertising are accustomed to reason upon this point as follows: Advertising lowers the cost of production because it increases sales volume which allows the industry to operate on a larger scale and consequently to effect a lower unit cost. It is questionable whether such a general representation of the powers of advertising is justifiable; but before any definitive conclusion can be reached it will be necessary to interrupt with a presentation of the theory of cost variation, which is the study of the effect of changes in output upon costs. Such an explanation of what increased production does to unit cost will enable us to judge whether or not advertising actually lowers costs when it stimulates sales and hence production.

In the investigation of these cost variations, two points of view must be kept in mind, the immediate and the normal. In the former case the question is what will happen to costs as a result of passing conditions of a more or less transient character such as the circumstances present at various stages of the business cycle. While it is necessary to take cognizance of such forces it is the normal conditions of the industry which are important, and it is chiefly these which

will be examined. Costs are often divided into the two classes, fixed and variable.(1) Under the heading of fixed or overhead costs are classified such items as interest on the fixed capital investment, insurance on plant and equipment, salaries of administrative officials and general office expenses; in short such expenses as must continue whether the plant or industry produces much or little. Current or variable costs, however, including expenditures for raw materials, supplies, advertising, labor and such other expenses as are usually connected with the concept of circulating capital, vary with the amount of production.

It is obvious that such costs must be incurred in varying proportions in different industries,(2) and it is on the basis of these typical variations in cost that the economists have classified variable supply industries.(3) But a theory of cost variation must also involve something more than the mere distinction between the proportions in which fixed and variable costs appear. In the first place it is necessary to study each industry to determine the typical cost stage in

- (1) These two classifications are sometimes called prime and supplementary costs. See Marshall, A.. "Principles of Economics." Book V, Chapter IV.
- (2) For a discussion of the percent of fixed Assets to total wealth for various industries see the report of the Federal Trade Commission, "National Wealth and Income", page 141. Washington D.C. 1926. Gov. Printing Office
- (3) For the orthodox analysis of cost variation see Marshall A., "Principles of Economics", Book V, Chapters 12 and 13; Taylor, F.M., "Principles of Economics", Chapter XI; Taussig, F.M., "Principles of Economics", Chapters 12, 13, and 14.

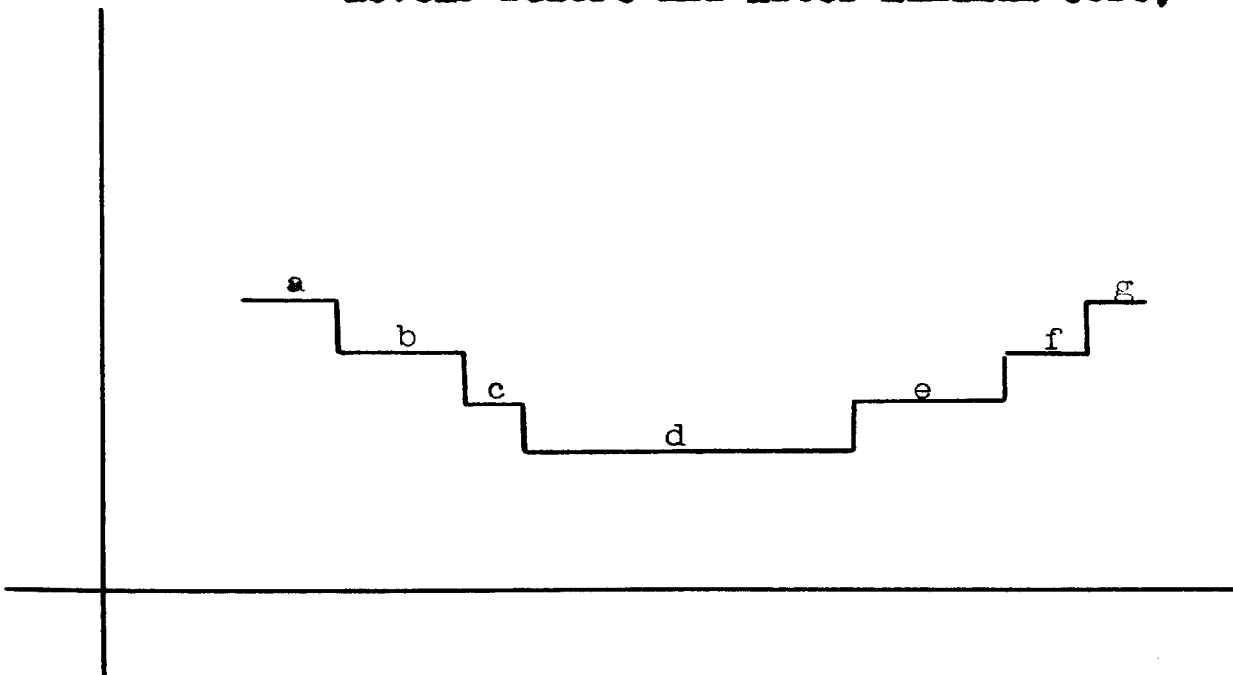
which the more important of the factors of production are customarily operating. This involves a preliminary knowledge of which factors are dominant in an industry, fixed capital, or circulating capital. Again it is essential to consider the effect on cost of replacing or duplicating these chief factors. For if an industry is to continue to supply a product or service, the replacement of worn-out equipment and duplication of plant and machinery to permit enlarged activity must be ignored. Finally it is important to know the exact extent to which the industry may profit by the application of those conditions which contribute to productive efficiency. To what extent may the principle of specialization and the benefits of large scale production be utilized? Is it possible by means of integration of either the horizontal or vertical type to gain further economies?

Once an industry is analyzed in the light of the above considerations it becomes possible to determine the typical supply schedule of that industry and hence the unit cost of production and under competitive conditions the unit selling price of the product. Whenever an individual establishment can increase its total output and at the same time reduce its unit cost it is said to be operating in the stage of diminishing cost. Similarly if it can increase its total output only by increasing its unit cost it is called an increasing cost industry, and finally, if a business organization is producing at

maximum efficiency and can bring forth more product without increasing or decreasing unit cost it is said to be operating at constant costs. Before leaving this discussion of the theory of cost variation it will be helpful to clear up several minor difficulties. One is that there is a concept of "constant cost" other than the one just given which might confuse our coming discussion if not explained here. At any given cost it is usually true that quite a quantity of product can be brought forth without any change in unit cost; that is actual cost does not change for every unit increase in output. Thus the graphs for the normally decreasing and increasing cost industries become series of descending and ascending steps. A graph perhaps may make this clearer. (Chart III)

Chart III

Graph Illustrating the Constant Cost Levels Before and After Minimum Cost,



A business which is operating at the "b" level or "e" level of costs in this chart may be said to be a temporary constant cost establishment, which means that a substantially large amount in view of the demand, can be produced at the same unit cost for the time being. However, when a business is said to be a normal constant cost one, it means that the long run forces such as have been set forth above in the theory of cost variation are functioning so as to bring the business to "d" in the chart and to keep it there.(1) In order to avoid any difficulty in this matter such establishments shall be designated as constant cost ones, while a firm maintaining itself for a while on a plateau of costs will be referred to as a temporary constant cost business.

Another difficulty which often occurs in the discussion of cost variations is the mistake of confusing decreasing cost with increasing returns and increasing cost with diminishing returns. That the two concepts are distinct is shown by the fact that it is possible for business to be in the stage of diminishing returns in physical output and at the same

- (1) Marshall expresses the same idea in the following fashion: "Taking a case at the opposite extreme, (from fixed supply) we find some commodities which conform pretty closely to the law of constant return; that is to say, their average cost of production will be very nearly the same whether they are produced in small quantities or in large." Marshall, A. "Principles of Economics", Book V, Chapter III, Section 7, Page 349.

time in the stage of diminishing costs. For all industries save the extractive ones, the point of least cost is not reached until after the point of diminishing returns has been passed. (1)

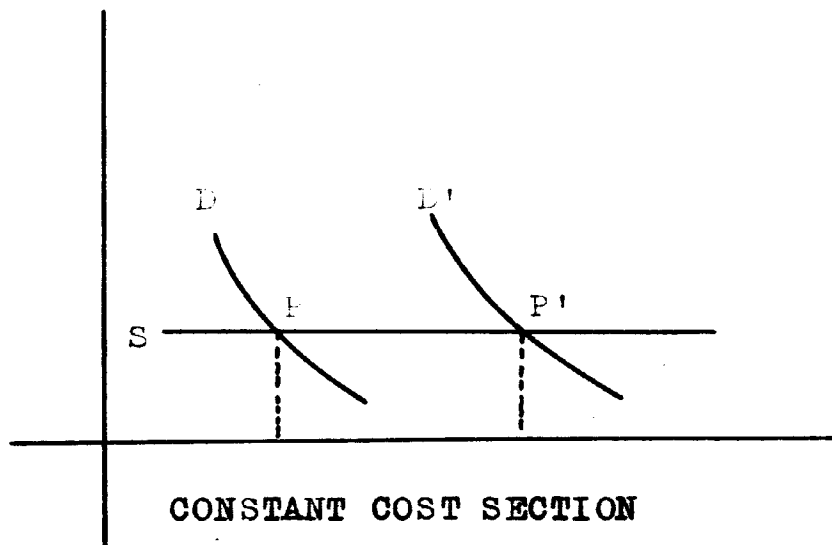
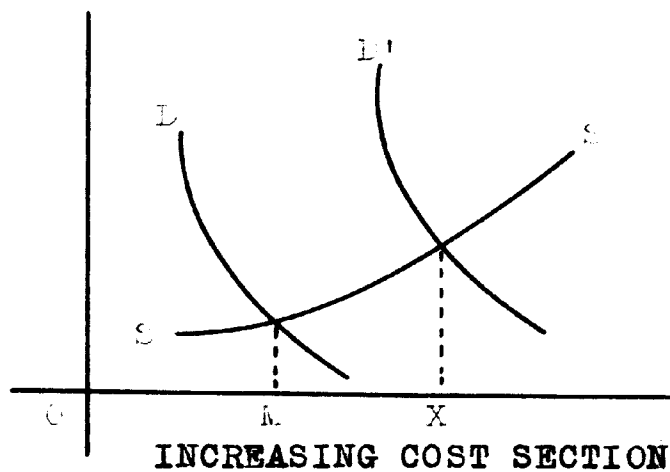
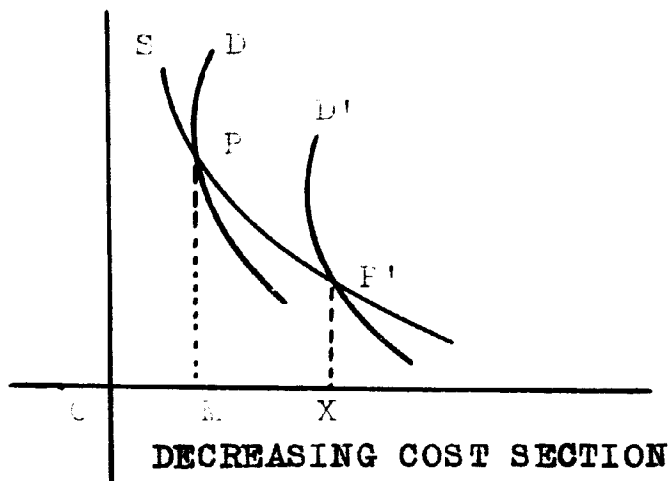
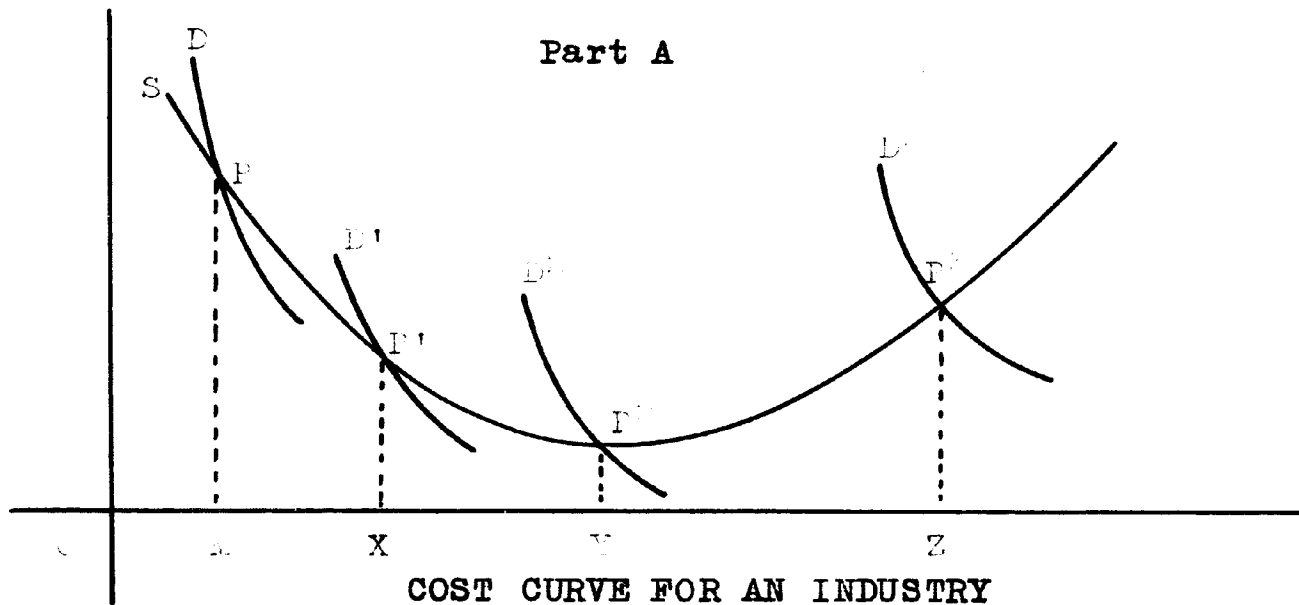
Still another caution is necessary, namely the necessity for drawing the distinction between the cost analysis which is applicable at any given time and that which holds true over a period of time. The criteria established in the theory of cost variation will indicate the typical, long-run or normal cost situation for a given plant. Likewise since industries are but composites of individual firms the analysis applies to entire industries. At any given time, however, individual business units may show cost conditions different from those typical for their industry. Indeed, temporary conditions such as changes in demand which are responsible for this condition may throw whole industries into an abnormal cost position.

Keeping in mind this analysis of cost variation the next task will be to study the effect advertising tends to have upon the costs of the different types of variable supply goods. A set of graphs, Chart IV, given on the following page may serve as a help in this discussion. Part A. of this chart is a picture of the cost stages through which an individual concern must pass if attempts are made to get more output from it. If the amount of output produced is small in relation to the size of the business unit -for example, the quantity

(1) Taylor, F.M. "Principles of Economics", Chapters IX, X and XI.

CHART IV

Part A



OM, cost would be somewhere near "P", a cost which could be lowered to p' if the quantity OX were produced, since the equipment would be more fully utilized. Moreover, if the plant were worked still more intensively there would come a situation in which least cost is reached represented in the chart by "p²" with the quantity OY produced. After this point any increased output must be obtained at increasing cost since maximum efficiency has been passed. (1)

Some business units for the reasons discussed above in the theory of cost variation are normally operating before the point of least cost and would have supply curves similar to the one given in Part B of this chart; others would normally work beyond the point of maximum efficiency having cost curves like the third illustration; and finally there are businesses which would operate under constant cost and would have supply curves which as the one in Part D of Chart IV. Our next step will be to analyze these three types, in order to see what kind of products fall into each category, since it would seem that advertising's effect upon the prices of any goods, would depend largely upon the cost stage in which that commodity was being produced.

The decreasing cost industries will be studied first

- (1) A point that needs to be mentioned in this connection is that from a very long run point of view all industries tend to be increasing cost industries, due to their dependence upon scarce natural factors of production -- a fact which will have some significance later in our study of the incidence of advertising cost.

-- those industries which have normal supply schedules as illustrated in the second part of Chart IV. If advertising is used to stimulate the sales in such a cost situation, the contention which is heard so much that advertising lowers cost of production appears to be verified. That is, if the curve SS in this graph is taken to represent the cost curve, and "D" assumed to be the original demand curve, under competitive conditions cost and price would tend to be near "p". If then an advertising campaign were launched and sales were stimulated so that the demand curve became D', the cost and price per unit would drop to the neighborhood of p', provided of course that there was free competition.(1) Advertising is thus seen to be a possible contributing cause of lowered price under such conditions.

The outstanding examples of decreasing cost industries are the public utilities.(2) In such industries an elaborate and costly plant is an antecedent condition to furnishing any quantity, however small, of a given product or

- (1) It is assumed for the purposes of this discussion that advertising tends to increase demand. The relation of advertising to demand is examined in a subsequent chapter.
- (2) Not only are public utilities decreasing cost industries, but any manufacturing unit may also be, provided the demand for the product is distinctly limited while the minimum sized plant capable of producing the product has capacity far in excess of this maximum demand. The industries which are ordinarily considered decreasing cost examples, however, are the railroads steamship transportation, street car service, grain elevators; wharves; electric, water and gas supply and the telegraphs and telephones.

service; or in other words it is impossible to keep the proportions between fixed and variable costs at a desirable ratio. Once the large investment has been committed more units of product can be produced at a lowered cost per unit, since increased output permits of a fuller utilization of the expensive equipment. In a true decreasing cost industry, minimum cost could never be achieved, however, for any length of time, because the increasing demand would require the expensive necessity of duplicating plant and equipment which would again leave the industry with large unused capacity. Advertising would seem to be the very tool which was needed in such a cost situation to stimulate sales and thereby effect a decreasing cost per unit.

An examination of the advertising experience of a few public utilities might prove helpful at this point.(1) It will be impossible, of course, to establish the truth of the conclusion that advertising has a tendency to lower price by

- (1) It might be objected here that even if advertising did lower the cost of production it would be hard to measure the effect of advertising upon the prices of the services of public utilities, since most of them have their prices controlled by the state. If cost of production were changed by an increased output there would be no competition to force price down to this lowered cost. In a public utility monopoly regulated by the government the practice is usually followed of fixing rates upon the basis of costs. Undoubtedly there would not be an exact correspondence between cost and price for the reason that the rate-making bodies act slowly being hampered by red tape, but prices would doubtless respond quickly enough to changes in cost to make it true that if advertising could effect increased sales, prices in the end would drop since the new production would be obtained at lower cost of production.

such a method. Even if reduction of costs appear with the use of advertising there is no justification for attributing the result to the use of advertising since the mere appearance of two phenomena together establishes no causal relationship between them. An unusually prosperous year may be due to a good production manager, or to changed demand situation outside the control of the business, or to any number of factors other than to advertising. It is said that when first the General Motors Research Corporation was operating under President C.R. Kettering new improvements were forthcoming every month in order to establish the worth of the institution. Advertising being used conjointly at that time might have been adjudged by an enthusiastic advertising representative as the cause of the increase in sales and the decrease in costs which accompanied such a period of growth.

Although it would seem that no direct causal relation could be established by an inductive study, still it is said "That when two or more instances of the phenomenon under investigation have only one circumstance in common, this circumstance is the cause or effect of the phenomenon".(1) Applying this method of logic to our problem, we can say that if in investigating the costs of various business houses, we find that the presence of the "circumstance" of advertising tends to be

(1) Minto, William, "Logic: Inductive and Deductive", Chapter V, quoting from John Stuart Mill's "Methods of Logic".

accompanied by the "phenomenon" of lowered costs of production, then we can conclude that there is some causal relationship existing between them, even if other circumstances are present in every case, but all changing in each case except the one of advertising. For example some firms would find themselves possessed of an unusually plentiful supply of capital; others with an efficient labor supply and so on; but advertising would be the only circumstance that would always be present. Some likelihood, at least, that advertising was one of the causes for the lowered costs.

The data which are available for the decreasing cost industries are very scanty. One reason for this is that most public utilities are under governmental supervision and hence, must be very careful as to the information they release. Public utilities usually make use of at least two types of advertising, institutional advertising and what they commonly call "merchandise" advertising.(1) The primary object of the latter is, of course, to increase the sale of their goods and services and would be the kind which would most directly influence prices. The other type, the good-will advertising is employed for its political effect, as well as for its influence

(1) The Advertising Committee's Report for 1926-27 of the National Electric Light Association says on this point: "The purposes for which advertising was directed were grouped under four general headings: (1) Appliance or merchandising; (43%) (2) Service building (10%); (3) Good will or institutional (37%); (4) Sale of securities(10%)". Another discussion on advertising objectives for a public service company is to be found in Printers' Ink Monthly, December, 1923, page 34.

upon volume of business and is of considerably more importance in the eyes of the industry. There is nothing disparaging about this comment, for if the people can be made to understand the vital part a public utility holds in community life it is less in danger of being made a foot-ball of selfish and aspiring politicians.(1) One does not need to look far to get examples of the latter type of publicity. In the local papers, the Detroit City Gas Company make continuous use of advertisements which are obviously designed to build up good will. To quote from one of their recent advertisements: "Your Gas Company constantly maintains a flying squadron known as Minute Men who are trained to give quick repair and adjustment service ---- The people of Detroit enjoy gas rates which are lower than those existing in any other similar city in America".

When such copy is used which has no definite merchandising appeal, it might be questioned whether advertising could build up sales volume. The few statistics given me by this company, however, show an increase in sales of more than 100% since 1918. (See Table II). Whether the advertising which increased by more than ten times during the same period helped to build up this growth in sales, it is impossible to

(1) There is, of course, no justification for certain types of propoganda carried on by public service interests.

TABLE II

STATISTICAL INDEXES
OF THE DETROIT GAS COMPANY
SHOWING THE VARIATIONS IN THE QUANTITY
OF GAS SOLD, THE AVERAGE RATE RECEIVED FOR
GAS SOLD, THE VARIATION IN OPERAT-
ING COSTS AND VARIATIONS IN
THE AMOUNTS EXPENDED
FOR ADVERTISING.

Base: 1918 = 100

<u>Year</u>	<u>Gas Sales Cubic Feet</u>	<u>Receipts per M Cubic Feet Sold (1)</u>	<u>Operating Expense</u>	<u>Total Expen- ditures for Advertising.</u>
1918	100.00	100.00	100.00	100.00
1919	105.62	100.94	114.60	215.83
1920	127.67	101.18	137.69	476.51
1921	101.91	115.61	162.28	183.38
1922	119.71	106.99	143.66	220.15
1923	143.69	104.83	148.13	424.39
1924	166.20	108.09	136.10	870.18
1925	187.93	109.57	126.91	743.11
1926	207.39	109.80	127.33	1065.28
1927	211.31	109.77	125.97	1266.73
1928	233.84	109.11	115.60	1034.98

(1) The increase in average receipts per unit of gas sold during the past few years results chiefly from the extension of service to suburban communities where slightly higher rates are in effect.

determine.(1) The facts can be pointed out, namely, that advertising increasing by so much has been accompanied by an increase in the sales of the company and by a decrease in operating expense since 1921, (2) but there is no justification for imputing a causal connection between these phenomena.

Other public service corporations, though presenting fewer statistics for analysis have made public some very definite statements regarding the effect of their advertising. The advertising committee of the National Electric Light Association of America for example reports that the companies of that industry spent approximately \$10,000,000 in 1926 and that the expenditures tended to lower their prices.(3) The local light and power company, the Detroit Edison, has made relatively small

- (1) A great deal of the increase would be attributable to growth in population, which is said to have increased from 994,00 to 1,700,000 in the years from 1920 to 1928. "Detroit's Growth" by Detroit Times.
- (2) The fourth column of Table II indicates this decrease. Moreover, from material given me at the same time regarding the rate changes from 1918 to 1929, it was observable that there was on the whole a tendency for for rates per cubic foot per month to fall.
- (3) "Had advertising not been practised in the past, present rates undoubtedly would be higher than they are and this would have been the case for years." Convention Reports of the Advertising Committee of the National Electric Light Association, 1926-27.

use of advertising. The business has grown, however, for in 1915 the gross revenue was about 7 millions, a figure which had climbed to 52 millions by 1928. This is more than a seven fold increase in growth and covered a period during which advertising increased from \$98,000 to \$400,000. Coincident with these increases has come a fall in the prices of the services of this company as shown by the following data. Here as in the other cases, however, there is no way of determining how much of the increased production and hence the lowered cost is due to advertising.

Table III.

Residence Service Charge for the
Detroit Edison Company.

(Average charge per kilowatt hour)(1)

1913	5.81	1921	6.12
14	5.87	22	5.79
15	6.04	23	5.36
16	6.00	24	5.29
17	5.87	25	5.28
18	5.82	26	4.82
19	5.56	27	4.72
20	5.64	28	5.52

Another public utility for which there is meager data

(1) From material given me from the statistical department of the Detroit Edison Company.

is the Michigan Bell Telephone Company. On the whole the telephone companies are not considered decreasing cost industries. The growth in the number of telephones is said to occasion increasing costs due to the fact that enlarged demand calls for additional fixed as well as variable charges. The telephone toll service, however, is an illustration of diminishing cost. In this case the cost varies inversely with the volume of business, since the fixed costs are not increased proportionally and the variable charges are relatively small. The experience of the Michigan Bell Telephone Company with their advertising of toll service confirms the principle under discussion, namely that advertising tends to lower the prices of decreasing cost goods. They report that advertising has been so successful in building up demand that they have "had to discontinue certain toll advertisements because the circuits had become occupied to capacity, pending the building of new circuits." As the result of the increased business very material reductions in the charge per message has been effected from time to time.(1)

The next task will be to determine if possible what advertising tends to do for products which are typically increasing cost goods, such as those of the farm, the mine and the extractive industries generally. Such industries are increasing cost businesses because of their absolute dependence

(1) Material furnished me by the Commercial Department of the Michigan Bell Telephone Company, Detroit, Michigan.

on the natural factor land, the best of which has long since been utilized.(1) To increase the output of goods coming from the extractive industries, therefore, must be to face increasing cost since the present equipment, the land, must be worked still more intensively which will cause each unit of output to have a greater marginal cost. Recourse to poorer lands will not avert this tendency. There is very little unused land to be had at any price and what remains is of inferior quality either with respect to fertility or to location. But it may be asked, is there not some way to stave off this ever-mounting cost? -- can we not call into play the principle of specialization, the advantageous methods of large scale production and other factors designed to increase productive efficiency and thereby reduce

- (1) The following discussion makes use of the analysis set forth in the theory of cost variation in the first part of this section. This theory of course assumes no change in the "state of the arts". Actually an increase of agricultural products has come in the last decade or so at decreasing cost due to the increasing effectiveness of labor and machinery. The reader may question the advisability of analyzing the effects of advertising upon increasing cost goods, which are in actual practice produced at falling costs. This matter is discussed later in detail, but it might be well to anticipate that discussion by a brief comment at this point. The analysis of the various types of goods is designed to show what would be the effect of advertising upon prices if there were no change in the state of the arts. It is true that we may never have to face such a predicament, yet it is well to know the limitations to advertising's power to lower cost if such were the case. We ought to separate the cost changes which result from mere increases in output from those due to changing methods of production.

or at least retard the increase in cost? Admittedly something can be done in this direction but the nature of the extractive industries is such that there are found to be decided limitations upon the use of such means. That there are such limitations in at least one of the extractive industries has been supported by the findings of the Agricultural Service Department of the United States Chamber of Commerce in a recent survey of large and small farms for the purpose of determining which of these is more profitable or successful. The report reads that farms whether large or small, show profits and losses "with the same variations in efficiency discernible in agriculture as a whole." Farming not lending itself to exploitation by large-scale production methods must remain a typical increasing cost industry. (1)

Part C of the chart on page eighteen illustrates the supply situation for an individual plant which is working under increasing cost. If advertising is employed to stimulate the sales of such a business and is successful, the unit cost of production would rise. For example, referring to the chart, if demand were changed from "D" to D', cost would rise from "p" to p', since quantity OX would have to be produced to meet

- (1) See Marshall, Alfred, "Principles of Economics" XI, x, 8, Page 651 ff. for a discussion of this point. See also a discussion by E.G. Nourse in "Recent Economic Changes in United States", Volume II, Chapter VIII, which indicates a trend towards a larger scale of agricultural operations.

the increased demand.(1) Therefore advertising arousing dormant demand for an agricultural product would tend to raise costs and prices for two reasons. In the first place the unit cost of production would be greater, and again there would be the added burden of the advertising to bear. Under ordinary competition the consumer would bear both increases.

The conclusion must be, therefore, that advertising cannot lower the cost and hence the price in the case of agricultural products - at least not for the reason usually given, namely, by merely increasing the demand. If it is true that advertising causes better methods of production to be used as a result of the increased demand, in other words if a new "state of the arts" is effected, then advertising may be accompanied by falling costs. Insofar as advertising is responsible for the better technique then it might be said that

- (1) For an individual business the increased volume might come from absorption of existing plants, and cause no rise in unit cost. Expansion of this nature could not go on indefinitely without meeting with increasing cost. If plants can be duplicated at the same cost we have a constant cost industry which will be discussed presently. But for industries in which land is the most important factor, any expansion which can come without raising cost is a temporary condition, unless there has been a change in the state of the arts. As was brought out in an earlier connection, it is possible to have individual plants within an industry not true to type, because of temporary conditions, but in the long run the normal forces will tend to assert themselves.

advertising lowers costs. With the assumption of constancy of the arts, however, there are decided limitations upon advertising's power to lower cost, -- limitations which should not be overlooked in this discussion. The analysis of the normal forces at work under static conditions gives us an idea of what would happen if improvements were not forthcoming, always a possible contingency.

If attention is turned to actual cases of increasing cost goods to see what affect advertising has had upon prices it is found that the data are scarce and inconclusive. The forestry products, those of the fruit and nut growers of California, salt, coal and mining products generally, would be cases in point if facts regarding them could be collected. From the walnut producers of California we have this information, namely, that "Since advertising started nine years ago, production and consumption have both trebled, but prices since 1920 average 75% higher than they did when advertising started." (1) Likewise the cranberry growers of New England report that they have been able to raise the prices of their product through cooperative advertising. It is also noticeable that the forestry associations of which there are a dozen or more in

(1) Soc. Bul. of June 15, 1925. Periodical Publishers' Association. These higher prices may be partly due to limitation of output. The effect of the changing price level may also be mentioned. Since prices in general have declined considerably at the same time that walnut prices have increased 75% the actual increase in the latter has clearly been much more than 75%.

America never give advertising credit for lowering prices, although a great deal is said about how much demand has been increased. Nothing at all conclusive can be learned from such bits of information, but they might lead one to think that advertising had not lowered prices for these extractive industries. Evidently the improved methods of production and marketing which may have developed have not been adequate to offset the tendency towards increasing cost.

There is, however, another example of increasing cost industries, citrus fruit production, for which we have information which allows us to make more of an analysis. The California Fruit Growers Exchange has advertised continuously for twenty-two years, spending during that time some eleven million dollars. It is considered that this merchandising work has increased the American consumption of oranges from 2.67 dozen per capita to 5.67 dozen per capita.(1) This almost threefold increase in consumption of citrus fruits throughout the country, however, has come without increasing the prices. The situation seems to be this, that advertising has greatly increased the consumption and production of citrus fruits, apparently without raising prices.(2) This seems a flat contradiction of the

(1) W.B.Geissinger, Advertising Manager, California Fruit Growers Exchange. Printers Ink, December 19,1929.

(2) Advertising has probably been used in part here as a defense measure - to dispose of ever-increasing surpluses. In this way, advertising may be socially justifiable regardless of its effect upon cost and prices.

principle which was developed at the beginning of our discussion, namely that advertising tends to increase the prices of increasing cost goods. The probable explanation is that the methods of farming and marketing have so materially changed from time to time that great economies have been effected and the whole industry has experienced a falling trend of cost. The growers themselves feel that their expenses have been lowered because better methods were evolved, as shown in the following quotation furnished by them: "The extreme economy in marketing which has been developed by the aid of advertising has helped to keep down the price of oranges and lemons so that the actual cost to the people in most parts of the country is no more than it was thirty or forty years ago. When it is considered that the average commodity prices are 200% or 400% higher than thirty years ago, this achievement becomes the more striking." (1) (2) While we may be able to show that certain agricultural industries have been successful in obtaining increased output at

- (1) Success Bulletin of January 4, 1927. #51. Periodical Publishers' Association, New York City.
- (2) Whether or not advertising can justifiably be credited with the power of lowering marketing costs will be considered in the next section of this paper. The point to be made here, however, is that improved methods have apparently kept prices from increasing in an agricultural industry and hence have counteracted the influence of advertising to raise price.

lowered cost, this does not set aside the normal forces at work, which will assert themselves if continued improvements in production are not developed.

Although from a theoretical viewpoint it is well to determine what effect advertising will have on increasing cost goods, from a practical standpoint it makes little difference because the advertising expenditures for goods produced under increasing costs are relatively small. The following table shows that the bulk of the expenditures is for manufactured articles.(1) It would seem, therefore, that the next analysis, the effect of advertising upon constant cost goods ought to have more significance. The products of manufacture are typical constant cost goods because in a manufacturing plant it is usually possible to combine the factors of production in such a way as to permit of maximum efficiency in their utilization.(2) Moreover, in such establishments there is frequently the

- (1) Some of the classifications in Table IV such as "Food and Food Beverages" might seem to fit into the increasing cost class because of their connection with agricultural products. In most cases, however, the raw materials constitute but a small fraction of the value and they are more correctly classified as constant cost.
- (2) "The real problem is thus not whether price is in strict conformity to a cost of production uniform for all competitors, but whether there is a rough approximation to this situation and a tendency toward its full attainment in a static state. And such a tendency, to repeat, exists over a very large part, probably the larger part of the field of industry." Paussig, F.W. "Principles of Economics" Volume I, page 173. See also Taylor, F.M., "Principles of Economics", Chapter XI, page 158: "In general manufacturing industries classify as constant-cost industries."

Table IV.

Amount spent in Advertising in National
Magazines during 1928 in Various Classes of
Business Listed in National Advertising
Records. (1)

Automotive Industry	22,936,931
Building Materials	9,816,329
Cigars, Cigarettes & Tobacco	5,220,286
Clothing and Dry Goods	7,534,713
Confectionery & Soft Drinks	3,722,483
Drugs and Toilet Goods	30,013,924
Financial and Insurance	2,968,696
Foods and Food Beverages	27,283,967
Garden	1,268,268
House Furniture and Furnishings	17,999,043
Jewelry and Silverware	4,949,531
Lubricants and Petroleum Prod.	3,316,986
Machinery and Mechanical Supp.	2,308,779
Office Equipment	2,705,385
Paints and Hardware	3,675,155
Radios, Phonographs & Music, In- struments	5,384,280
Schools, Camps and Correspondence courses	3,271,975
Shoes, Shoe Furnishings, Trunks, and Bags	3,503,291
Soaps and House Supplies	8,721,362
Sporting Goods	3,886,344
Stationery and Books	5,676,433
Travel and Amusement	6,231,135
Miscellaneous	2,791,292
TOTAL EXPENDITURE	<u>185,204,588</u>

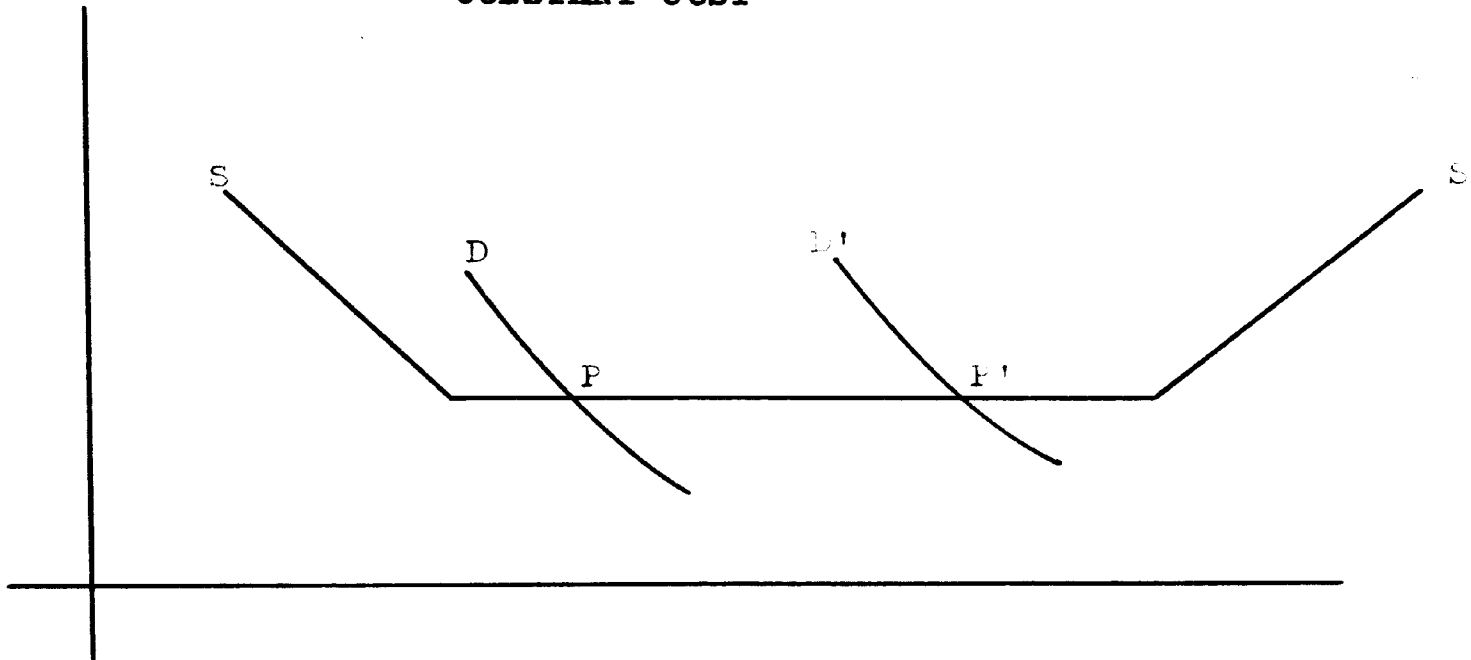
(1) Though these figures cover only the amounts spent for national advertising, our purpose is served, since there would probably be little change in the classifications, even though newspaper and other types of publicity expense were added.

possibility of introducing specialization and large-scale methods with noteworthy results. Furthermore expanding demand does not oblige manufacturers to incur increasing costs since the increase in output can be obtained from new plants which cost no more than the old ones. In other words if another factory must be built to accommodate a new demand situation, it may be erected at substantially the same cost as formerly; machinery can be purchased at similar rates; and there is a tendency for wages and capital charges to be alike. Hence there are real forces at work to keep costs constant for most factory products.(1)

If advertising is used in such a cost situation what opportunity has it to lower costs? If ^{the} diagram in Chart V is taken as representative of the cost curve of a typical constant cost business, what will happen to costs and prices if advertising is successful in changing demand from "D" to D'? (2) There would be a tendency for them to rise since although cost of production would remain the same, the new

- (1) The only exceptions are those businesses, which because of dependence, for essential factors of relatively great importance, upon either diminishing or increasing cost industries are thereby themselves thrown in the diminishing or increasing cost class.
- (2) Although Chart V does not represent the cost situation for any one plant, it does illustrate the cost condition of a given business unit, consisting perhaps of a number of plants. Moreover, it would apply to the normal situation in a given manufacturing industry.

CHART V.
CONSTANT COST



advertising expense would be an added cost burden. Of course in some businesses advertising expenditure would not constitute a very large proportion of the total cost of production (see Chart V) and it might be temporarily absorbed without any rise in price.(1) On the other hand if the figures in Table VI are examined it is seen that the total advertising expenditures for some of the manufacturers of the country amount to almost as

(1) A certain flexibility exists no doubt in one of the elements of cost, namely in profits. It might serve as a sort of bumper in that increases in advertising would not result in increased prices. This would, of course, be impossible in the long run.

Table V.

Percentages of Sales Expended for Advertising:
By Manufacturers(1)

Arrow Collars	3.5
Baker-Vawter System	3.5
Berry Brothers' Varnish	4
Cadillac Automobiles	1
Champion Spark Plugs	7
Cloth-craft Clothes	1.5
Colgate's Preparations	2
DePree Chemical Company	6
Evinrude Motors	8
Fatima Cigarettes	5
Globe-Wernicke Cabinets	3
Great Northern Railroad	1.8
Hudson Automobiles	1.3
Ivory Soap	3
Kewanee Boilers	2.5
Kodaks	3
McCray Refrigerators	7.5
Markham Air Rifles	5
Northern Pacific Railroad	1.9
Old Dutch Cleanser	10
Packard Automobiles	1.1
Phonographs	5
Reo Motors Cars	1
Rund Heaters 2.5 to	3.5
Santa Fe Railroad	2.5
Saxon Automobiles	2.6
Sears, Roebuck & Co.	10
Sherwin-Williams Paint	3.5
Stromberg Carburetors	3.5
Studebaker Automobiles	2
Union Pacific Railroad	2.5
Universal Portland Cement	2
Velvet Tobacco	6
Welch's Grape Juice	10
Wooltex Clothes	2
The median expenditure is 3%	

(1) From Daniel Starch, Principles of Advertising (1923), p. 49. (A.W. Shaw Company.)

Table VI.

ADVERTISING EXPENDITURES OF SOME
LEADING COMPANIES. (1)

(Newspapers and Periodicals Only)

	Amount for Advertising in 1928.	Dividends Paid in 1928
Canada Dry Ginger Ale #	1,000,000	1,963,370
Chrysler	8,992,181	11,747,307
Hudson Motors	4,423,125	8,178,862
Postum	6,626,904	10,100,908
Radio Corporation	1,813,245	1,370,196
Wm. Wrigley ##	1,030,686	6,741,646

#Periodical lineage not included.
##Newspaper lineage not included.

(1) The Magazine of Wall Street.

much as their dividends. If such is the case a company is not apt to absorb the cost of publicity but will pass it on to the consumer, if possible, since it is part of the cost of production.

If corroborating data from the business world be sought to verify this conclusion that advertising tends to raise prices for manufactured articles, little information is

forthcoming; in fact, it is found that most business houses are ready to testify that advertising lowers their costs. The following is a typical cost and price analysis made by business men to convince themselves that advertising lowers price. "Our advertising expenditures have advanced 50%, our price to the jobber, in the face of the great increase in raw materials (more than 100%) has advanced only 17% approximately, while our sales have increased 100%. Had it not been for our increasing sales brought about by better merchandising methods, including our larger advertising expenditures we believe that our advance in price to the jobbers would have been at least 30% instead of 17%. In 1913 advertising cost per bottle was 2-1/5 cents of a 30 cent price; in 1928 1.4 cents of a 40 cent price. It would cost at least 57 cents to make a bottle of vanilla at home, and this without counting labor costs. The critics are wrong when they say advertising increases prices." (1)

The experience of the Campbell Soup Company has also been such as to lead them to believe that advertising can lower the cost of production of this type of product. This firm spends according to its own statements 17/100 of 1% of the selling price of each can of soup for advertising.(2) It is thought that such merchandising has enabled the company to sell

(1) Printers' Ink Monthly, March, 1928.

(2) Printers' Ink Monthly, March, 1923, Page 17.

a high quality article for about one third of what it would cost to make it at home, and that the cost of production would be higher if advertising were eliminated. Since this is the kind of information business men generally furnish concerning the results of their advertising, it would seem that our analysis regarding constant cost goods was incorrect. This apparent discrepancy between the facts and the theory calls for some explanation. Before taking up this discussion, let one more example of the constant cost type be examined.

The automobile trade would normally be called a typical constant cost industry, easily meeting the tests of such a classification. Large-scale production methods can be widely used; in normal periods the equipment would tend to be well utilized; and lastly if more output were needed it could be produced in factories which cost substantially the same as the plants already in use. If such are the conditions inherent in the automobile business it would seem certain that, according to our reasoning, advertising would make costs and prices of cars higher.

If, however, we turn to the available data published regarding this industry little evidence is to be procured indicating that advertising has done anything of the kind. In fact most of the information is of an opposite nature. Automobile manufacturers are among the firmest supporters of advertising and on every occasion affirm that advertising has

been a miracle worker in reducing their prices. Doubtless their opinions judged in the light of their actions should have some weight, for there is no reason why hard-headed business men should spend thousands of dollars for advertising if it does nothing but augment their expenses. Of course this type of argument could be carried too far so that all advertising could be justified. Nevertheless, there is some point to the comment that the bulk of the great advertising expenditure cannot be the result of misjudgment by so many producers. The natural reaction of business men towards spending money for advertising is doubtless antagonistic. Theodore F. McManus says in his book "The Sword Arm of Business" that J.T. Dodge at first loathed advertising. Little by little, however, this prejudice was overcome and he became a consistent advertiser on a large scale. If business men can be prevailed upon to use so much of their money for advertising what effect will there be upon costs? If for example the General Motors Corporation spends, on the average \$15.00 per car, will the consumer have to pay more or less for his automobile?

Tables VII and VIII on the following pages give the retail sales and advertising expenditures of thirty or more passenger car manufacturers for the years 1927, 1928 and 1929. A glance at the figures for the sales of these companies reveals the fact that the bulk of the business is divided among

TABLE VII

YEARLY RETAIL SALES FOR LEADING PASSENGER CAR MANUFACTURERS.
1927-1929. (1)

<u>Make of Car.</u>	<u>1927</u>	<u>1928</u>	<u>1929</u>
Ford,	393,424	481,611	1,310,058
Chevrolet	647,810	763,226	780,009
Dodge	123,918	146,092	115,765
Hudson-Essex	225,468	223,303	254,013
Buick-Marquette	232,428	194,713	172,278
Chrysler-Plymouth	154,234	170,260	169,480
Oakland-Pontiac	157,049	219,899	190,089
Willys-Overland	139,406	229,656	199,681
Nash	109,979	113,783	105,117
Studebaker-Erskine	194,839	106,077	82,838
Oldsmobile-Viking	48,573	73,398	93,462
DeSota		14,609	59,621
Graham-Paige	18,256	58,347	60,478
Hupmobile	33,809	54,977	44,342
Durant	56,781	71,037	47,728
Cadillac-LaSalle	29,719	36,559	35,233
Packard	31,355	42,546	44,632
Marmon-Roosevelt	10,095	14,568	22,344
Reo	22,144	21,163	17,332
Auburn-Cord	9,835	11,090	18,660
Franklin	7,526	7,364	10,712
Pierce-Arrow	5,836	5,621	8,398
Peerless	9,872	7,581	8,332
Lincoln	6,460	5,939	6,159
Jordan	6,357	4,188	2,243
Stutz-Blackhawk	2,906	2,426	2,974
Chandler	18,445	15,296	7,374
Moon	4,180	2,752	1,572
Gardner	3,290	3,153	2,059
Stearns-Knight	927	1,183	1,395
Miscellaneous	18,617	12,748	5,832

(1) National Registered New Car Sales 1929.
Cram's Automotive Reports, Inc. Dec. 1929.

TABLE VIII

ADVERTISING EXPENDITURES FOR LEADING PASSENGER CAR MANUFACTURERS
1927-1929 (1)

<u>MAKE OF CAR</u>	<u>1927</u>	<u>1928</u>	<u>1929</u>
Ford	183,400	729,400	1,171,560
Chevrolet	1,184,446	1,201,434	1,228,975
Dodge-Graham Bros	952,661	956,748	452,200
Hudson-Essex	925,710	923,125	1,121,560
Buick-Marquette	1,059,784	752,144	1,510,600
Chrysler-Motor Corp.	1,415,117	1,268,883	1,333,899
Oakland-Pontiac	659,900	623,950	559,205
Willys-Overland	1,066,700	721,600	877,480
Nash	438,990	311,450	350,860
Studebaker-Erskine	356,102#	82,942	699,519
Oldsmobile-Viking	452,046	309,000	794,340
DeSota		243,250	261,280
Graham-Paige	411,225#	297,175	292,450
Hupmobile	690,625	586,550	604,200
Durant	101,940#		
Cadillac-Lafayette	819,635	680,810	700,980
Packard	938,110	840,550	819,040
Marmon-Roosevelt	322,245	389,800	
Reo	611,000	507,000	485,600
Auburn-Cord	367,872	253,914	315,970
Franklin	308,610	298,300	350,400
Pierce-Arrow	59,750#	54,950	275,800
Peerless	47,700#		
Lincoln	134,335	187,975	175,945
Jordan	64,650#		
Stutz-Blackhawk	49,468#		
Chandler	225,620#		
Moon	16,000#		
Gardner	78,025#		
Stearns-Knight	49,800	50,925	11,500
Miscellaneous			

(1) Denny Publishing Company, From 150 Leading Advertisers. "National Advertising Records" January 1929 and January 1930.

Leading Advertisers 1927, Curtis Publishing Company.

a few of the leaders. In 1927 and in 1928 over thirty percent of the cars sold were Fords and Chevrolets, and in 1929 the Ford sales alone amounted to one-third of the total business. These two leading companies and the half dozen or more corporations which are close seconds have also been the large advertisers in this trade. It is impossible, of course, to say what part advertising has played in the concentration of this huge business into the hands of a relatively few concerns, but there are many who feel that it has been a prime factor, (1) and that a wider dispersion of sales would come if advertising were not used. (2) On the other hand it must be remembered that it has probably been advertising which has kept the ten or fifteen small manufacturers of this group alive. About a dozen of these firms have outputs of less than ten thousand cars per

- (1) Ford, it is true was able to gain a commanding position in the field without advertising, although it appears that to hold it he has had to turn to large scale publicity methods.
- (2) A fuller discussion of the effect of advertising upon concentration in industry will be taken up later in this thesis, but the comment might be made that there seems some evidence that advertising has played an important part in this movement. The following quotation shows the degree of concentration which advertising has apparently brought to one industry: "Practically all, if not all, automobiles are originally equipped with one of the five batteries that are nationally advertised. And of this amount, practically 70% of the automobile manufacturers equip their cars with Willard Batteries." Success Bul. #58 Revised January 15, 1927.

year, and advertising may have been as valuable in preserving their business as it has been to the larger companies in expanding theirs. It seems, however, that the amount of business going to these small companies has been dwindling away for in 1927 they sold about 2% of the number of the cars retailed, while in 1929 this percentage had fallen to approximately 1%. (1)

While it appears that there is some indication that the bulk of the business is going to the large advertisers in this industry, little correlation between expenditures for advertising and sales is to be found in individual cases. This lack of correlation may be due to the fact that there are interfering forces at work. For example if a successful company tried to market an extremely unpopular model, even a very material increase in advertising expenditures might not increase sales. Some of the companies for which we have information given in Tables VII and VIII, however, have found that sales corresponded to changes in advertising. For example, in 1929

- (1) The tenacity of the cars remaining in this lower group may be accounted for in some other fashion, as for example their absorption by successful companies. It is a well-known fact that Ford took over the Lincoln after failure was imminent. Moreover, Stearns-Knight is owned by Willys-Overland and Pierce-Arrow by the Studebaker Corporation.

the Reo Motor Car Company having reduced their advertising to 80% of what it had been in 1927, found that sales took the same course and dropped to 78% of the 1927 volume. During the same years, however, the Packard Company, decreasing their advertising appropriations from \$938,110 to \$819,040 experienced a growth in sales of approximately 40%. (1) In the same manner all the sales and the advertising figures could be compared for each company, but without more data than we have the analysis would lead to no definite conclusions regarding advertising's effect upon sales.

Individual automobile manufacturers, however, are not so chary about drawing conclusions regarding their advertising. They bear ready testimony to the doctrine that advertising has increased their sales and lowered their costs. In talking with the advertising manager of one of the largest car manufacturers in Detroit I was told that if this company should decrease their advertising expenditures from \$7.50 a car, which is the amount they now spend, to \$1.00 a car the "Selling price would be up between \$100 and \$200 per car, since the cost of production would rise. Advertising has decreased the price of automobiles and has increased their quality". The manufacturers who spend a great deal for advertising either directly

(1) These figures as given in Tables VII and VIII are for magazine advertising only, and therefore the growth in sales might possibly be accounted for by an increased use of other kinds of advertising.

or through their retailers feel that they are making a more economical use of this agency than the companies which spend very little in the aggregate but a large amount per car or per dollar of sales. There is the opinion in the trade that the percentage spent on advertising is smaller for the companies who spend the greatest sums on advertising.(1)

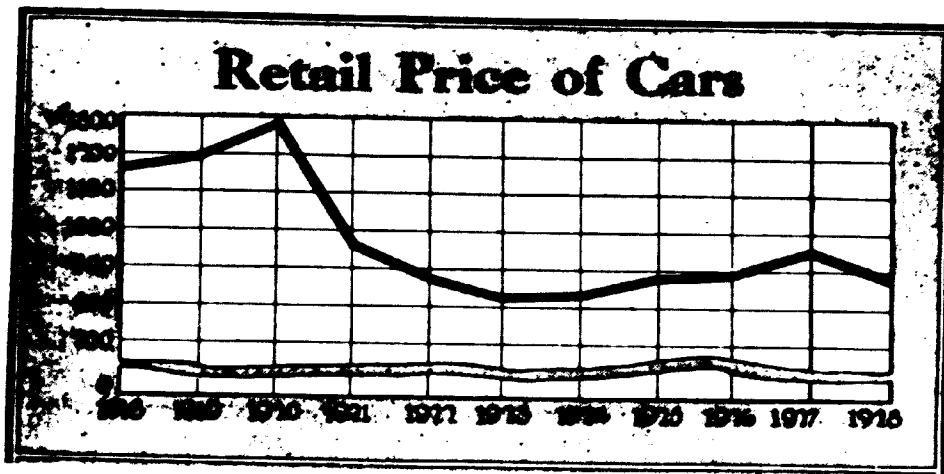
While there is no way to substantiate the opinion that advertising has caused lowered prices in this industry, there seems no question as to the tendency for prices to fall whatever the cause may be. The following chart shows that the average retail price for passenger cars is much lower than it was in 1920, although there has been a slight rise in the

- (1) Mr. H.A. Mitchell of the Bureau of Business Research, University of Michigan, has secured the following information for me: "Chevrolet appropriate about \$10.00 a car for all forms of advertising; Essex appropriate \$15.00 and Hudson, \$25.00. With Chrysler it also varies from \$10.00 to \$35.00 per car, the lowest sum being on the cars with the largest production. We know of manufacturers who spend as much as \$150.00 per car for advertising. These are the companies that have limited production, of course." This information was furnished by Joseph R. Scelaro, Detroit, Michigan.

As a whole, these amounts, however, tend to show percentages of total sales which fall in a very narrow range for all companies.

In fact, the opinion has been expressed that a fixed ratio around 3% for all companies is more nearly the case. See Article in Advertising and Selling, December 11th, 1929 "How Automobile Manufacturers Assess Dealers for Local Advertising."

Chart VI. (1)



past few years. (2) This general tendency for prices to come down in the automotive trade seems to be contrary to the conclusions, based upon our analyses which showed it to be a constant cost industry. Thus for the third time we have found difference existing between such facts as are available and the theory advanced. It now becomes necessary for us to explain these seeming discrepancies between fact and theory. Once these differences have been adequately explained, a brief justification of our method of analysis, namely, examining the incidence of advertising cost upon the three main types of goods will be attempted. Proceeding to the first of these

(1) "Automotive Industries", February 23, 1929, Page 258. Philadelphia, Pennsylvania.

(2) This slight rise might be accounted for by the fact that the average car is by far a better product than it was in former years.

two tasks there are at least two possible explanations of the fact that individual businesses may show costs which are not typical or normal for their industry. These are temporary conditions of demand, and changes in the state of the arts in production and marketing. An example of the first is the influence of the business cycle upon costs. In a business boom firms are apt to overbuild their equipment and push beyond the point of maximum efficiency in their operations. For the time being, therefore, there would be a tendency for costs to rise. Advertising used in such a situation could not lower costs. However, when the recession came and the individual firms were thrown back into a stage of decreasing costs, advertising might be invoked to increase demand. Costs would tend to be reduced in this case.

But this over-expansion of industry sometimes appears to be more than a temporary situation. It is difficult to obtain estimates of the extent to which business in general is over built, but in some cases there are data available for given industries. For example, figures published in the Annual Statistical Reports of the American Iron and Steel Institute enabled me to make an estimate that there was a difference of about 20% between the actual output of steel and the possible output in view of the equipment. While this percentage may not be typical for other industries, yet the feeling is general that American business has considerable "Over-capacity

for production".(1) To the degree that this is true, there is a possibility for advertising to lower costs.

There may be some who would object to giving advertising even this modicum of praise. Such critics would rather say that advertising was the cause of the over-expanded condition of business and that it should be given no credit for pulling industry out of the hole. It is doubtful whether this wasteful condition of business can be laid at the door of advertising, for it would seem that the cause of the maladjustment between supply and demand was more fundamental. However that may be, once the business is over expanded it would seem that advertising could help adjust the demand to the supply and thereby effect lowered costs of production.(2)

A manufacturing firm is sometimes operating before the point of least cost in the stage of decreasing costs for other reasons than those connected with the business cycle or chronic over-expansion. For instance when a business is

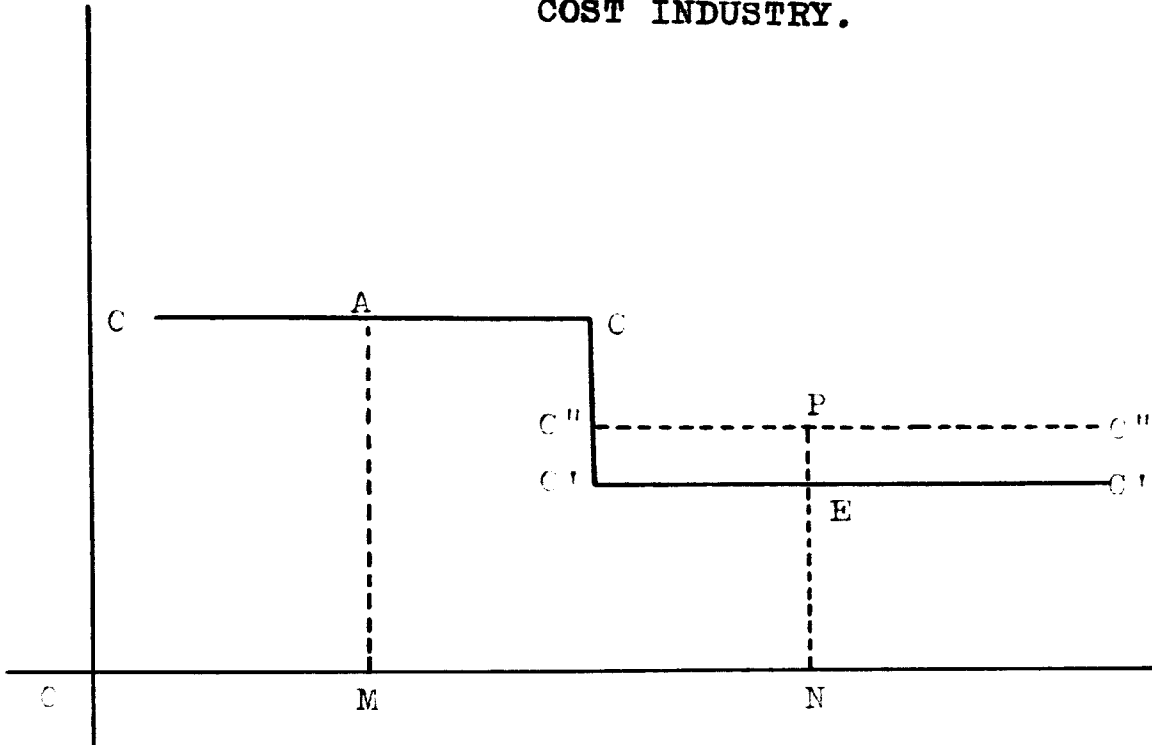
- (1) One writer has estimated that our steel plants in 1927 were equipped to produce 70% more steel than the normal requirements of the market; the shoe factories 80%; our copper smelters, 100% and even the automobile industry about 80%. - a general picture which might hold true for any year. Bersodi, Ralph, "The Distribution Age", Appleton, 1927, page 43. These figures no doubt overstate the general condition in the United States.
- (2) The effect of advertising upon the business cycle and over-expansion will be discussed in a later chapter.

just starting up, demand is often so small that the cost of production is much higher than it would be if greater output could be produced. Temporarily, the business acts like a decreasing cost industry; and if advertising were used to increase sales, unit costs would tend to drop. An illustration of such a situation which came to my attention was the experience of the Iodent Chemical Company of Detroit. In the beginning of their tooth paste business they found costs so high for the small output, that they arbitrarily set the selling price below cost, at 50 cents, and then depended upon advertising to build up sales to the point where costs would enable them to make a net profit on such a price.(1) This is an extreme example of what advertising can do for industries which have been unable to operate at maximum efficiency. The following diagram, Chart VII, may make clearer the role played by advertising in such a business.

With the quantity OM demanded and produced the firm would be able to supply the trade at a cost equal to AM; however if advertising were employed so that the quantity demanded became ON the cost of production would be reduced to EN, without the advertising expense. Adding the advertising the total cost would be PN. What effect has advertising had upon

(1) Another example of such a method of using advertising is to be found in Printers' Ink Monthly, June, 1924, regarding the merchandising of Cresley Radios.

CHART VII.
INCIDENCE OF ADVERTISING IN A CONSTANT
COST INDUSTRY.



costs? If comparison is made between the original cost, AM and PN then the verdict will be that advertising has lowered costs; if on the other hand EN and PN are contrasted it seems that advertising has raised cost. Perhaps the former comparison is the right one. This is true if there is any reason to think that without advertising the lower level of cost represented by C'C' could never be attained otherwise. This raises the question of the most effective method of demand creation -- a question which we will presently analyze in some detail. Suffice it to point out here, that if advertising is an

effective and economical method of increasing sales then it can be said to be a factor in lowering costs and hence prices.(1) This is but a temporary condition, however, and it is our purpose to examine the more permanent situation. From this standpoint the apparent discrepancy between fact and theory may be resolved by an explanation of the two meanings which are confusedly applied to the term diminishing costs. In our use of the term we have had in mind a static assumption; namely constancy of technical conditions. It is only under such an assumption that industries clearly indicate the three distinct cost stages discussed. The second meaning of diminishing costs refers to actual dynamic conditions, to the trend of costs over a period of time. While a perfectly legitimate concept this use of the term is confusing and had better be supplanted by a more exact expression such as falling costs or historical decreasing costs. It is true that in the mind of the individual business man there is no distinction between "historical" diminishing costs and real diminishing costs. Therefore he is very apt to impute to advertising that reduction in costs which may be actually due in large part to technical improvements.(2)

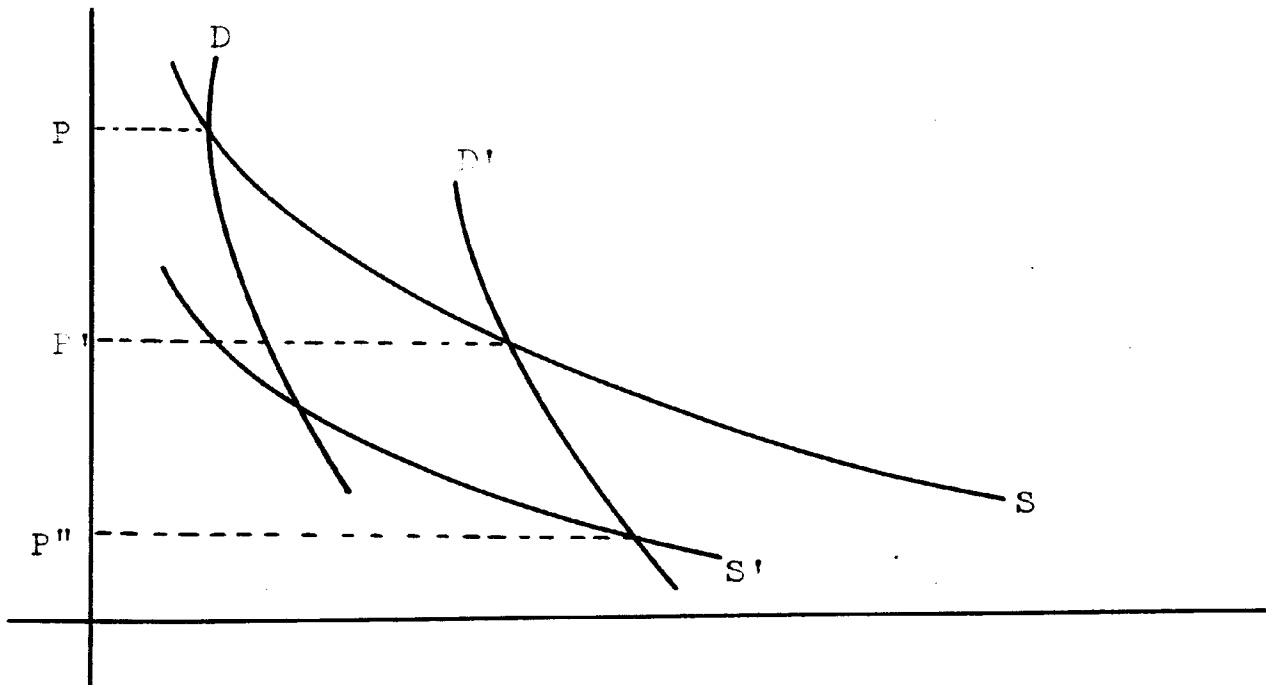
(1) For a discussion of the relative advantages of advertising and other selling agencies see A.W.Shaw's "An Approach to Business Problems." Chapter XIII.

(2) It is true that the changing methods of production may be due, to some extent to advertising; In large part, however, they are determined by other factors.

The following chart VIII may be helpful in distinguishing between these two results. Let "D" and "S" represent the original demand and supply curves with the resultant price of "P". If demand were increased by advertising to D' without any change in costs of production price would drop to P'. However if there is a concomitant change in the state of the arts so that the cost of production drops to S' then price will tend to be P". The fall in price from P to P' is due to advertising, provided it were the means of increasing the sales. The drop in price from P' to P", however, is due to the changing technique.

This is of course an illustration of a falling price or a downward trend of price and might be true of all three

CHART VIII.
FALLING COST.



types of industries over a period of time. For the individual business man this "historical" diminishing cost means that he can increase his output with a falling unit cost provided he can count upon continuous improvements. Even industries which had been fortunate enough to reach maximum efficiency with a given state of the arts would under the new conditions find themselves in a situation of falling prices with the new least cost point still to be achieved. Although advertising may have no large part in bringing about these changes in productive efficiency, (1) yet once the change is at hand, advertising may exert a potent influence on costs, since it may be the tool used to attain the new lower cost levels. And with the technique of production continually improving, one low level of costs is no sooner attained than new changes put another within possible reach.

In circumstances like these advertising has had wonderful opportunities to stimulate demand without increasing prices. This does not invalidate the economic principle that advertising tends to increase prices if it is used for increasing or constant cost goods. Such a principle is only true under static conditions, and would apply only if the state of the arts remains unchanged. It does raise a question, however, as to the utility of the method employed in this paper of

- (1) Later an attempt will be made to see whether or not advertising may help to speed up productive efficiency, or in any way be responsible for a change in the state of the arts.

analyzing the effects of advertising upon the basis of a classification which apparently disappears in real business conditions. A question of major importance is, therefore, whether the tendency for costs of production to fall is so strong as to supersede the other influences in the market. There are three sets of forces at work in any cost situation; first the temporary conditions of demand which we have discussed above; second the normal forces, which constitute the basis of the theory of cost variation analysis; and finally the influence exerted upon costs as a result of changing methods of production. The latter would tend to make all industries manifest falling costs, while the first two forces would tend to make some industries operate under increasing costs, some under constant and only a few under decreasing cost. At any given time will the influence of the changing technique of production wipe out the effect of the other forces? I think not. At any given time production is being carried on with a particular state of the arts, and with those methods some firms are in one cost situation and some in another. In the long run costs may fall, but for the time being individual business men are committed to certain investments and methods, are working with certain conditions of demand, and costs are just as apt to be increasing or constant as decreasing.

For example if we refer to the previous discussion about the automotive trade it will be remembered that there

seemed evidence enough that costs had fallen in this industry in the last decade or so. This had been due no doubt to the improved processes utilized by these manufacturers. Thus the resultant downward movement of prices seems to have supplanted the constant cost tendency caused by the normal forces. At any given time, however, there is reason to think that some of the firms within this industry are not working under decreasing costs. It is true that the very small companies, those which produce less than ten thousand cars per year (Table VII) are apt to be in a decreasing cost situation, but among the larger manufacturers there must be some who have made the best use of latest methods of production and who would, therefore, be working under constant cost, that is, they would be able to turn out a substantially greater amount of product with practically the same unit cost of production. Furthermore, there might be some, who under the stress of circumstances might have pushed beyond the point of maximum efficiency at times, into increasing costs. Thus the advertising used by one manufacturer in this industry might react upon costs in an entirely different manner from the advertising used by another. It will not suffice to point out the tendency for costs to fall, and thereby conclude that advertising will lower costs for all makes of cars. What is true in the automobile industry is true for all industry. A cross section of the business world no doubt would reveal some plants working in one cost stage and some in another;

and advertising used by them would have varying results upon costs. Since producers must of necessity be faced at any given time by a definite set of conditions, a thorough-going explanation of the cost situation determined by these conditions is surely justifiable. The producer has no means of knowing what improvements may be developed or, indeed, that any new methods will be forthcoming. Consequently a theory which indicates the particular limitations of a given cost situation may well serve to safeguard him from unwise policies.(1) Before leaving this point, one final explanation is necessary. The success of advertising in lowering costs depends upon the possibility of production being turned out at decreasing or falling costs. If there is any prospect that our inventive genius may wane, the theory of cost variation becomes of decided significance.(2) Since all production in the final analysis is dependent upon natural resources which are scarce, any failure to increase our efficiency in utilizing these factors must tend to bring increasing cost. In such a case advertising is clearly powerless to effect a reduction in cost.

- (1) It is needless to emphasize but worthy of mention that the cost analysis under discussion would have distinct significance to the student of economic theory even though it had little practical importance.
- (2) It is true that historically we have had steady and rapid improvements, and while we may hope for their continuance, yet there is no assurance that such will be the case.

In summary then the conclusion must be that advertising tends to increase the costs of some goods and to decrease those of others. Insofar as advertising influences costs of production, it will tend to affect prices in the same direction, competitive conditions assumed, of course. Price, however, is the result not only of costs of production in the narrow sense, but of marketing expenses as well and advertising's final effect upon prices will depend upon its influence upon both elements. We now turn, therefore, to a discussion of the effect of advertising upon marketing costs.

PART III

AN ANALYSIS OF THE EFFECT OF ADVERTISING
UPON MARKETING COSTS.

In the last section which dealt with the effect of advertising upon costs of production the conclusion was reached that advertising has tended to reduce such costs in cases of diminishing cost industries and to some extent in all industries in which a downward trend of costs is found. In and of itself this reduced production expense would tend to lower the consumer's price. Price however is a product not only of production costs but of marketing expenses as well; hence it is necessary to investigate the effect of advertising upon selling expenses, since advertising may increase these expenses so much that any reduction wrought upon the production costs would be completely wiped out. On the other hand marketing expense may be reduced as a result of advertising.

Before entering upon the discussion of the effect of advertising upon expenses of distribution, it will be necessary to examine briefly marketing costs. There has been an insistent cry that too great a percentage of the consumer's dollar goes for the marketing work; that too much is being paid for the transportation, storage, grading, selling and demand-creation functions of the middleman. In 1921 the

government made a study of several phases of marketing and distribution. The results of the investigation appeared in a report of the Joint Commission of Agricultural Inquiry (1) and contained many enlightening bits of information. The general conclusion of the inquiry seemed to be that there was "a very definite need of an improvement in the process of distribution." (2) It was pointed out that the manufacturers of certain food products took, as their operating expenses, about 40% of the dollar received from the wholesaler; (3) who in turn retained a little less than 10% of the dollar he received from the retailer; (4) and that finally the retailer of groceries kept a 20% gross margin from the dollar the consumer paid him for the merchandise. (5) What is true in this trade seemed to be typical for other industries studied by this commission, namely that the percentage paid for marketing amounted to a goodly share of the consumer's dollar.

Other studies have corroborated these statements. For example, a few years ago a summary of published statistics

- (1) "Marketing and Distribution". Report of the Joint Commission of Agricultural Inquiry, Part IV, 1922.
- (2) Ibid, page 210.
- (3) Ibid, page 117.
- (4) Ibid, page 158.
- (5) Ibid, page 173.

relative to the cost of merchandise distribution for the years 1913-1923 was compiled -- from what we have taken the following data, Table IX.(1) These statistics show that of the average dollar which the consumer spends for commodities, approximately 41 to 43 cents goes to the wholesalers, and retailers for their services in distributing merchandise. This does not include the amount the manufacturer spends upon marketing which for some articles would be more than the costs of retailing and wholesaling. It seems, therefore, that the consumer has been paying quite a sum for the marketing work done for him; some students, however, believe that he will be paying still more in the future. One writer, for example says that "In the fifty years between 1870 and 1920 the cost of distributing the necessities and luxuries which we consume has nearly trebled."(2) He points out that this rate of progression is maintaining itself so that society will soon be devoting more energy to distribution than to production per se. This tendency for marketing costs to rise is partially illustrated by Table X which gives the gross margins in percentages of net

- (1) "Review of Published Statistics Relative to Cost of Merchandise Turnover, and Fluctuations in Manufacturing Employments in the United States." 1913-23. Prepared by Niles and Niles, Certified Public Accountants, 60 Broadway, New York, N.Y.
- (2) Bersodi, Ralph, "The Distribution Age", Appleton, 1927, page v. This author points out that one reason why costs of marketing have mounted is that the service of distribution has become more elaborate.

TABLE IX

SUMMARY OF ANALYSES OF THE CONSUMER'S DOLLAR
FOR VARIOUS KINDS OF MERCHANDISE.

Class of Merchandise.	Producer	Distributors		
		Wholesaler	Retailer	Combined
Automobiles	\$.730270
Clothing	.675	..	.325	.325
Coal	.444	.198	.358	.556
Dairy Products	.464	.386	.150	.536
Dental Supplies	.730	..	.270	.270
Drugs	.546	.114	.340	.454
Electrical Supplies	.530470
Fruits and Vegetables	.503	.226	.271	.497
Furniture	.564	..	.436	.436
Groceries	.729	.088	.183	.271
Hardware	.580	.163	.257	.420
Jewelry	.600	..	.400	.400
Lumber	.454	..	.546	.546
Meats	.708	.094	.198	.292
Shoes	.552	.158	.290	.448

Composite Averages of the Consumer's Dollar

1. For Fifteen Classes #1	.587	.413
2. For Eleven Classes #2	.586	.414
3. For Seven Classes #3	.578	.422
4. For Nine Classes #4	.568	.322

- #1 A simple average for the fifteen classes of Merchandise.
- #2 A simple average for the eleven classes of merchandise which are most frequently purchased by the average consumer.
- #3 A simple average for the seven classes of merchandise which are most frequently purchased by the average consumer, but excluding food products which are more perishable than the other classes of merchandise.
- #4 A simple average for nine classes of merchandise including food (dairy products, fruits and vegetables, groceries, and meats) apparel (clothing and shoes), and shelter (lumber, hardware and coal).

TABLE X

GROSS MARGINS IN PERCENTAGE OF NET SALES (100%).

I. For Retail Jewelry Stores: (1)

Years:	1919	1920	1921	1922	1923	1924	1925	1926	1927
	32.3	32.7	43.5	38.6	38.3	39.5	39.6	40.9	40.9

II. For Department Stores with Net Sales over \$1,000,000: (2)

Years:	1923	1924	1925	1926	1927
	32.0	32.1	32.2	32.6	33.1

III. For Department Stores with Net Sales less than \$1,000,000: (3)

Years:	1923	1924	1925	1926	1927
	28.2	28.5	28.6	28.9	29.7

IV. For the Wholesale Grocery Trade (4)

Years:	1916	1917	1918	1919	1920	1921	1922	1923
	9.5	8.77	9.1	9.1	9.0	11.5	11.1	10.6

(1) Bureau of Business Research, Harvard University, Bulletin #38 and #76.

(2) Ibid, Bulletin #74

(3) Ibid, Bulletin #74

(4) Ibid, Bulletin #40. In this case total expense figures were used because there were losses in the years 1920 and 1921.

sales for the wholesale grocery trade, and for jewelry and department stores. For the latter the trend upward is marked; for the wholesale grocery business, however, while total expense was higher in 1923 than it was in 1916 there has been no definite rise from year to year. Wider investigations among wholesalers, however, would probably bring to light increasing expense ratios for many of them since the competition of the chains and the changes in retail trading areas has affected the position of numerous jobbers.(1)

On the other hand if we turn to an analysis of the retail grocery business we find that there is some indication that marketing costs have fallen in this field. It is said that chain store competition here has tended to lower the average mark-up of retailing. Statistics, however are too few to enable one to demonstrate the truth of such a conclusion; the nearest approach to such a proof would be to compare the scanty material which is available regarding the chain store costs with the results of early studies made of general grocery retailing. In 1923 the Harvard Bureau of Business Research reported a figure of 19.1% of net sales as the average gross margin for the retail grocer for that year; (2) they gave 11.3% as the mark-up of the wholesale groceryman.(3) These

(1) "Recent Economic Changes" National Bureau of Economic Research. 1929 page 421.

(2) Harvard Business Bureau, Bulletin #52.

(3) Harvard Business Bureau, Bulletin #40.

successive margins amount to an aggregate mark-up on the basis of the retailer's selling price of 28.7%. On the other hand most of the chain systems show costs which run well below 20%. For example in 1923 the Piggly-Wiggly stores had a gross margin of 16.20% of net sales.(1) For a later year, 1928, the Kroger Grocery and Baking Company reported that their gross mark-up was 16.2 per cent of its sales.(2) It seems, therefore that the conclusion, "That the chains offer and have realized economies by comparison with the unit grocery stores seems hardly open to doubt"(3) is justified and that for some lines of business, at least, there is a tendency for marketing costs to drop. In this connection it is noteworthy that the chains have made a much larger use of advertising than have the independent wholesale and retail grocers, a fact which may in part explain their lowered marketing costs.

Another new factor in grocery marketing which may effect the cost of distributing such products is the recent trend toward mergers among food manufacturers. The belief is

- (1) Engle, N.H, University of Washington, 1926, Master's Thesis. "Some Economic Aspects of Cash-and-Carry Grocery Marketing of the Pacific Northwest."
- (2) American Management Association, Marketing Executives' Series: No. 65, p. 9-10 "The Chain Store of Tomorrow" by G.M.Lebhar.
- (3) C.E.Griffin, Associated Grocery Manufacturers of America, Inc., Addresses of 21st Annual Convention, November, 1929, page 23.

in some quarters that the new companies will effect economies which will lower costs considerably; others are not convinced, however, that the new giants will be able to accomplish that end. One writer has said that, "The chief promise of economies in these later mergers lies in the field of distribution and more particularly in the costs of obtaining the aggressive selling services which modern business demands." (1) Analyzing these possibilities, however, he came to the conclusion that these promises of reduced marketing expenses might be unfulfilled.

It is one matter, however to establish the point that marketing costs have been high and will probably continue to be high relative to production costs, and quite another to determine whether or not these costs are too high absolutely. When it is pointed out for example that it costs "approximately an average of 63 cents of the consumer's dollar to distribute 37 cents' worth of corn flakes" (2) this does not necessarily indict the present system of marketing. It may be possible for production costs to average only about one-third of the total selling price because so much has been spent upon advertising and other means of cultivating the market. It costs money to widen the market but the gains ensuing may outweigh the rising expense. That is, as was pointed out in the last section, the costs of production for some kinds of goods may be lowered if the market is enlarged since certain economies of large scale production are sometimes obtainable when the demand is such as

(1) Ibid, p. 23.

(2) "Marketing and Distribution" Report of the Joint Commission of Agriculture, Part IV. p. 210.

to warrant producing a larger output.

For illustrative purposes let it be assumed that the breakfast food mentioned above were produced and sold locally for every community. A package of corn flakes which under the present system of production and marketing sells for 12cents probably would if produced under small scale methods sell for much more than this price. Whereas the marketing costs would no doubt be somewhat lower if the goods were sold nearer the source of production, still they could not drop to zero. At the same time the production costs which were formerly about 4 cents-to use the ratios supplied by the government study would probably increase. What the resultant price to the consumer would be is impossible to determine but it might well rise to 20 cents even though marketing costs were reduced from 8 cents to 4 cents, because of an increase in production costs -- say to 16 cents. It is of no benefit to the consumer to have the marketing costs lowered if production costs are raised by an amount which more than offsets the difference.

Thus there is to be found some justification for undertaking the costly work of developing the market. That it is costly no one would be inclined to deny; but it is maintained that it is not lost energy since production costs are thereby lowered. This argument is so often and so glibly advanced apparently without much thought given to the basis upon

which it rests that it might be worth while to attempt to clarify this point.

The underlying reason why marketing costs can sometimes lower production costs is that the marketing mechanism effects cooperation in production. It is the marketing system which makes possible the high degree of specialization which characterizes the present production methods. Without a wide market it would be impossible for any individual to specialize; it would be impossible for men to work together to supply each other's wants. Thus one method of defending this "distribution age" is to point to the fact that a wide market is a necessary antecedent condition to a widespread use of specialization (1) which in turn is the primary condition of productive efficiency.(2) Or to put it briefly a wide market tends to give

(1) There might arise some question here whether the wide market was the cause or the effect of specialization or large-scale methods. Did the wide market, made possible by improved transportation, stimulate large-scale production, or did the new methods of production come first with mass distribution following as a consequent development? The fact is that probably they are reciprocally dependent; in any event which way the line of causation runs is a matter of small importance. We know that the two phenomena, the large market and mass production must appear together, and advertising as part of the process of mass distribution helps to determine the conditions of production.

(2) All the other conditions of productive efficiency such as the introduction of capitalistic methods of production, large-scale production, integration of industries, unification of industries(Continued on p.72)

man more economic goods.(1)

This constitutes quite a strong defense of the present distribution processes, but there are other functions performed by the market which are just as essential as that of making possible cooperation. I refer to the regulatory functions of exchange. It is through the buying and selling in the market that the right prices are worked out, and the function of price is to regulate production and consumption. If too much is produced in view of our limited resources, prices will drop. This drop in prices will set up two reactions, an increase in consumption and a decrease in production, the two results which are needed under the circumstances. If too little is produced the opposite reactions take place righting production and consumption. Thus it is through the exchange mechanism, the market, that consumption and the quantity, quality, the regularity and the continuity of production are regulated. Since the marketing system performs such important functions it is necessary therefore that the marketing work be well done; that the market be of sufficient scope to let the forces of competition establish the "right" price which will

(2) (Continued from page 71) are in the main reducible to nothing more than a wider use of specialization. For a discussion of the conditions of productive efficiency see Taylor, F.M., "Principles of Economics" Ronald, 1925, Chapter VII.

(1) Insofar as some types of industries are not able to make use of large-scale production methods, the normal advantages of advertising in widening the market can not come to them from a use of publicity methods.

regulate our cooperation properly. A well-developed market of some extension will probably support a better production system than would markets which are scattered and unconnected. Since advertising is used to develop the market any defense that can be built up for the present marketing system is likewise a partial defense of advertising.

In view of this importance of the market it is a question whether the costs of marketing are too high. The middlemen are responsible for the creation of certain utilities which are as necessary to the consumer as are the ones supplied by the so-called "producer". There has been inherent in political and economic thinking a belief that for some reason or other the work of the farmer, the miner, the baker, the manufacturer is more productive than that of the retailer, wholesaler, merchant and middleman in general. Actually this is implied when it is pointed out that so much goes to the middlemen out of the consumer's dollar. Forty cents of every dollar is paid to middlemen! This seems to indicate to most people that there is something wrong; it may be, however, that the most important services rendered for the consumers are performed by the middlemen. At least it cannot be over-emphasized that the marketing functions of selling, assembling, transportation, storage, standardization, financing, and risk-taking are as vital and as necessary a part of the productive

process as are the "production" functions themselves, since the creation of time, place, ownership utilities are as important as the creation of form utilities by the manufacturer and the farmer.

These marketing tasks should be performed as efficiently as are the production functions. If it is true, as it is often said, that attention in the past was directed too much to the making of goods and not enough to the selling of goods, it is time that attempts were being made to improve the system of distribution. But business men are as much interested in reducing marketing costs as they are in lowering production expenses; and they can be depended upon to work in every way to gain that end. Advertising may in fact be said to illustrate one method which is being employed with this end in view. But let producers and middlemen make marketing as efficient and economical as possible, still it may remain true that the consumer must pay 40% to 50% of his dollar to the middlemen. Whether or not marketing costs are too high can only be determined in the light of the importance of the marketing functions.

But, admitting for the sake of argument that distribution costs are too high, what is the solution? Will it help matters if the scale of operations is enlarged or contracted? What kind of costs will be encountered if marketing operations are decreased or increased in size? The question

calls for an analysis of whether or not the principles of large-scale production are applicable to marketing. We are interested in this question because the effects of advertising upon marketing costs depend in the main upon the nature of marketing costs. The concensus of opinion seems to be that marketing is only a decreasing cost industry in its very early stages and that it soon meets increasing costs. L.D.H.Weld in an article entitled "Do Principles of Large-Scale Production Apply to Merchandising" comes to conclusions which are generally accepted. The following statements are taken from his discussion: (1)

"The principle of decreasing costs applies to retail merchandising to a much greater extent than our first examination of costs by size groups seemed to indicate."

"The principles of large-scale production do not apply so definitely to wholesaling as to retailing."

"There is a point, however, beyond which a retail store cannot go without incurring additional expenses in order to attract customers and to provide proper management and supervision in a departmentized business. The point where overhead costs begin to increase with the size of the store is apparently reached in relatively much smaller units in retail trade than in most manufacturing industries."

(1) American Economic Review Supplement, Volume XIII, March, 1923, pp. 185-97

A decreasing cost industry may result among other causes (1) from conditions in which the fixed capital, the plant and equipment is relatively expensive compared with the variable expenses, such as labor and materials. Whenever the ratio of fixed expense to circulating capital costs is high there are apt to be unused capacities and an increase in output which permits of better utilization of equipment will effect a lower unit cost. In such cases increasing the size of operations will bring decreasing costs because least cost is reached only if a large amount is turned out.(2) But marketing is not handicapped with a heavy investment in fixed capital, in fact, labor, which is decidedly a variable expense, is usually the main cost in marketing. When the cost for the constant factors is relatively low as is the case in marketing the point of least cost comes very early.(3) Retail stores and jobber establishments or even manufacturers trying to

- (1) For a discussion of the causes of decreasing cost see earlier analysis in the first part of last section.
- (2) Least cost point would be near the end of the Stage of Diminishing Output or Returns; thus the increasing cost stage would be late to set in.
- (3) Least Cost point would be near the Point of Diminishing Returns here, and consequently increasing costs would come very soon after the Point of Diminishing Returns had been reached.

market goods in so small a volume that the work is carried on before this least cost point will find that if the volume could be increased the cost per unit of output would drop; but for stores which are medium-sized already, expanded sales are not apt to bring decreasing costs. The optimum size has been reached.(1)

When, however the attempt is made to support these conclusions by statistics it is found to be impossible. Table XI gives the total expense item, the advertising expenditures, and the total salaries and wages in terms of percentage of net sales for a number of retail and wholesale firms according to volume of sales. In the light of the arguments developed above we should expect that neither the smallest nor the largest units would have the lowest expense. But examination of the figures does not show any such tendency. In three cases out of the twelve the small plants have the lowest total expense; in three others the middle-sized stores; and finally for half of the firms the most efficient size seems to be the ones in the group having the largest sales. Several explanations may be offered perhaps, but the first one is that the statistics are inadequate as the groupings are too large. For example in some cases the concerns are thrown into only two classes, which gives us no chance to

(1) This optimum size may be determined in part by the limits of large-scale management as well as by size of plant.

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ag expense was found to be for the stores under \$250,000, the smallest department stores. Conclusions of a more definite nature were reached in a study of retail distribution of clothing made in 1922 by the Bureau of Business Research of the Northwestern University School of Commerce, namely that "When the amounts of selling expense are measured in terms of sales, they increase with the size of the store". (1)

Table XII shows statistics for a different type of business, the expenses (in percentage of net sales) of grocery manufacturers in distributing their products. In every case the expenses of the companies who tried to sell on a larger scale were greater than those for the concerns which market a smaller volume of goods. The comments made regarding these figures are as enlightening as the statistics themselves. Speaking of the third group of products, the canned and bottled foods, it was remarked that "total marketing expense tended to be distinctly higher for the nine companies which sold

(1) "Selling Expenses and Their Control" Horace Secrist, 1922 Prentice-Hall. page 406.

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determine whether or not the middle-sized units are more economical. Yet in the case of the 508 department stores studied, where seven classes are given there is no tendency for cost to be high first, to fall to a low point and then to rise again. The lowest operating expense was found to be for the stores under \$250,000, the smallest department stores. Conclusions of a more definite nature were reached in a study of retail distribution of clothing made in 1922 by the Bureau of Business Research of the Northwestern University School of Commerce, namely that "When the amounts of selling expense are measured in terms of sales, they increase with the size of the store". (1)

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Table XI.

Total Operating Expenses and Advertising and
Total Salaries and Wages in % of Net Sales
Net Sales 100% (1)

Type of Business	Advertising Expense	Total Salaries and Wages	Total Operating Expense
Retailers and Wholesalers.			
508 Department Stores, 1927, #74			
Less than 250,000	2.0	15.7	28.7
250,000-499,000	2.2	15.8	29.3
500,000-\$1,000,000	2.7	16.1	30.8
1,000,000-1,999,000	3.3	16.2	31.2
2,000,000-3,999,000	3.3	16.7	31.5
4,000,000-9,999,000	3.1	16.4	31.9
10,000,000 and over	3.1	16.5	30.6
499 Retail Shoes Stores, 1923, #43			
Less than \$30,000	1.5	15.7	27.8
30,000 to 49,000	2.0	13.6	25.5
50,000 to 99,000	2.2	13.7	26.7
100,000-249,000	2.3	15.1	27.5
250,000 and over	3.8	16.6	32.0
230 Retail Jewelry Stores, 1927, #76			
Less than 20,000	2.4	17.3	38.4
20,000-49,000	3.2	18.5	40.3
50,000-90,000	3.9	17.7	41.2
100,000-499,000	4.2	17.3	38.9
500,000 or over	3.9	17.1	38.2

(1) These statistics were gathered from the Harvard
Business School Reports.

	Advertising Expense	Total Salaries and Wages	Total Operating Expense
151 Wholesale Automotive Equipment Firms, 1924, #51	.2	9.7	24.3
Less than \$500,000	.3	8.8	22.0
500,000-999,000	.3	8.6	24.4
1,000,000 and over			
88 Automobile Tire and Accessory Retailers, 1923 #48	.9	13.1	25.6
Less than \$75,000	1.0	11.8	23.1
75,000 and over			
213 General Stationers, 1928, #80			
Less than 100,000	1.2	18.7	34.3
100,000-299,000	1.6	17.5	32.2
300,000 and over	1.6	18.8	33.5
54 Wall Paper Wholesalers for 1927, #73			
Less than \$175,000	.9	9.2	40.7
175,000 and over	1.1	6.1	35.2
62 Paint and Varnish Wholesalers, 1926 #66			
Less than \$400,000	1.1	6.7	24.1
\$400,000 and over	.7	5.7	23.0
134 Plumbing and Heating Supply Wholesalers, 1927, #71			
Under \$500,000	.3	5.20	21.9
\$500,000 to \$1,000,000	.3	5.03	20.7
Over \$1,000,000	.25	4.05	18.5
288 Lumber, Mason Materials and Coal Dealers, 1927 #75.			
From \$94,000	.35	1.09	20.80
To \$262,000	.80	2.20	25.52

Table XII.

Marketing Expenses of Grocery Manufacturers, 1927 (1)
(Net Sales 100%)

Interquartile Range. Range of Middle 50% of
Comparable Figures.

	FROM	TO
7 Flour Manufacturers, 1927	\$4,000,000	\$7,500,000
Advertising and Sales Promotion	.32	.44
Total Marketing Expense	5.06	7.21
Total Salaries and Wages	1.66	3.07
9 Meat Companies, 1927	\$12,000,000	\$35,000,000
Advertising and Sales Promotion	.04	.23
Total Marketing Expense	4.99	9.14
Total Salaries and Wages	1.76	3.16
13 Canned and Bottled Foods and Similar Products Manufacturers	\$725,000	\$2,000,000
Advertising and Sales Promotion	.38	2.99
Total Marketing Expense	15.42	19.64
Total Salaries and Wages	3.49	5.67
15 Coffee, Tea, Chocolate, Extracts and Spice Manufacturers	\$500,000	\$950,000
Advertising and Sales Promotion	1.43	3.36
Total Marketing Expense	15.83	20.46
Total Salaries and Wages	4.57	8.28
14 Cereals, Crackers, Macaroni, Salt and Preserves Manufacturers	\$425,000	\$10,000,000
Advertising and Sales Promotion	3.06	7.95
Total Marketing Expense	23.69	29.76
Total Salaries and Wages	4.37	11.11
11 Soaps, Cleansers, Polishes, and Disinfectants Manufacturers	\$150,000	\$300,000
Advertising and Sales Promotion	3.32	21.25
Total Marketing Expense	30.63	47.87
Total Salaries and Wages	7.02	11.28

(1) Harvard Business School Report #77. "Marketing Expenses of
Grocery Manufacturers, 1927.

nationally than for the three which restricted their sales activities to less extensive areas."(1) On the other hand it was pointed out that for the manufacturers of soaps, cleansers, polishes and disinfectants, "Those companies which sold nationally commonly showed distinctly lower total marketing expense ratios than did companies which sold sectionally".(2) Likewise for the coffee, tea, chocolate, extract and spice producers it was stated that "in general companies with the larger sales volumes commonly showed slightly lower total marketing expense ratios than did the smaller companies."(3)

From a statistical approach it seems impossible to reach definite conclusions regarding how far distributing processes are subject to the law of decreasing returns. There are, however, facts of a different nature which may be commented upon as giving some indication of what might be the optimum-sized unit in certain marketing fields. For example it was recently pointed out in an article in a business paper that "Chain companies close branches which sell less than \$250 worth of goods a week."(4) Evidently, it is felt that there

(1) Harvard Business School Report, #77 "Marketing Expenses of Grocery Manufacturers, 1927, p. 8.

(2) Ibid, page 14.

(3) Ibid, page 10.

(4) Business Week, September 21, 1929, page 13.

is a lower limit to the best-sized plant. Likewise an upper limit may be implied by the fact that chains usually scatter their stores over the entire city area rather than attempt to sell the community from one or two centrally located shops. Competition of the other chain systems no doubt plays a part in the placing of new units.(1) It is true that probably the sales volume of some of the present chain stores could increase considerably before the "right" size was reached. A recent news item says that for the 11 months ended November 30, 1929, average sales per store unit in the Kroger grocery chain system were \$46,833 which was an increase of 25.8% over the same period of 1928, while the increase in the number of stores was only 11.3%.(2) Though the chain systems may encounter increasing costs relatively early with regard to the size of the store, when it comes to their other functions, such as the buying, the advertising work, the management, transportation and storage, such work might possibly be carried further with the assurance of concomitant decreasing costs.

A summary of the above discussion must lead to only one conclusion, namely that the principles of decreasing cost are of limited application in the marketing field. If this

(1) The density of the population, the size of the tributary area and the type of merchandise handled would all be factors determining the actual size of the average store.

(2) "The Facts in Food Distribution" Dec. 21, 1929. The American Institute of Food Distribution, Inc. p. 12.

is true then advertising used to establish and build up vast markets cannot be credited with helping to lower the cost of marketing. Insofar as increasing costs are encountered with the widening of the market, advertising is a factor in raising price to the consumer. The belief that large-scale methods are always better than smaller operations has permeated American thinking to such an extent that it is hard for people to believe that bigger marketing units are not more economical. It cannot be concluded, however, that very small stores are the best size; the optimum sized plant probably lies somewhere between the smallest and the largest stores. As one writer says, "This fundamental principle ---namely that a marketing enterprise may remain too small or may grow too large to be operated at minimum costs per unit of product handled, applies to all middlemen alike." (1)

Doubtless many industries in attempts to gain more business have gone beyond this optimum size. In a recent government bulletin issued by the Bureau of Foreign and Domestic Commerce uneconomic expansion was scored and an instance was cited "of a textile factory near Chicago which tried to increase its volume by extending distribution into Texas. A subsequent check on operations there showed that it cost the

(1) Theodore Macklin "Efficient Marketing for Agriculture" The MacMillan Company, 1922, page 39.

company \$1.25 for every dollar's worth of goods sold in that territory."(1) Insofar as advertising has encouraged such marketing policies it has certainly been increasing the cost of merchandising, since it has pushed individual firms beyond the point of highest efficiency. It is the opinion of many that advertising tends to do this. For example in the government study, "Marketing and Distribution" referred to above, it is said in one place, speaking of the struggle of manufacturers to win markets: "This competition is further complicated by the fact that manufacturers are constantly striving for national markets and make vast expenditures to enter communities already sufficiently supplied by manufacturers of similar products. In this effort large advertising appropriations are made. ----This entire situation tends to increase the total cost of selling and distribution."(2)

Such criticism seems to imply that marketing costs have risen because the sales were developed in places too distant from the factory, in other words because there had been an extensive cultivation of the field. But the same tendency for selling costs to rise seems to be encountered if the increased sales volume is obtained by an intensive working of

(1) Domestic Commerce Bulletin, September 30, 1929, page 145.

(2) "Marketing and Distribution", Report of the Joint Commission of Agricultural Inquiry, Part IV, page 214.

the home market. A study made by Leverett S. Lyon of the Institute of Economics regarding the small order problem in 1928 reveals the fact that marketing costs rose as individual orders became smaller. The report says: "In statements from 104 manufacturers concerning whether there has been a significant increase in the proportion of small orders received in the past ten years, 76 percent of the total indicated that there had been such an increase. Furthermore 68 manufacturers out of 94 stated that the cost of securing orders had increased."(1)

Another phase of this same question is the relation of advertising to other selling expenses. Judging from the general reports about the potency of advertising it would be expected that the use of advertising would lower the other necessary marketing costs. But this does not seem to be borne out. The study in the retail distribution of clothing mentioned in a previous connection brought out the fact that for the clothing industry at least "the amounts of selling expense per \$100 of total net sales increase as the amounts of advertising per \$100 of total net sales increase."(2)

Table XIII taken from this study brings out the truth of this

- (1) "The Small Order Problem and How it is Being Met."
American Management Association, 1928. pages 5-7.
- (2) "Secrist, Horace, "Selling Expenses and Their Control"
Northwestern Bureau of Business Research, 1922, p.171.

TABLE XIII

Amount of Selling Expense per \$100 of Total Net Sales and Per \$1 of Advertising for Stores Classified by Size and by Amount of Advertising per \$100 of Total Net Sales, 1919.(1)

Classified Total Net Sales (in 000's)	Amount of Advertising Per \$100 of Total Net Sales.	Number of Stores	Amount.
Total (Average)	Under \$1	79	7.07
	\$1 to \$2	100	8.46
	\$2 to \$3	66	11.62
	\$3 & over	37	12.55
Under \$40	Under \$1	15	5.01
	\$1 to \$2	14	7.12
	\$2 to \$3	2	5.27
	\$3 & over	2	7.11
\$40 to \$60	Under \$1	43	5.77
	\$1 to \$2	37	7.34
	\$2 to \$3	20	9.32
	\$3 & over	6	13.23
\$60 to \$180	Under \$1	18	8.74
	\$1 to \$2	39	8.47
	\$2 to \$3	26	11.63
	\$3 & over	15	13.12
\$180 & over	Under \$1	3	7.93
	\$1 to \$2	10	9.56
	\$2 to \$3	18	12.07
	\$3 & over	14	12.12

(1) Ibid, page 171.

statement. Apparently advertising can do little to lower selling costs. Likewise if the data given in Table XI on a preceding page is analyzed it is found that increasing advertising expenditures do not always bring lower total operating ratios. In only four cases out of ten did the lowest total expense of the group accompany the highest percentage spent on advertising; in fact in four other instances the lowest total expense ratios came with the lowest percentage of advertising expenditures. Thus there seems no correlation between high selling costs and either large or small advertising expenses. Moreover if the advertising expense items are subtracted from the total expense ratios in this table, Table XI, figures are obtained which put the stores in the same relative positions regarding total expenses as they had before. In other words, the same-sized companies have the lowest ratios of selling expense whether advertising is counted in or not. It would seem, therefore, that advertising has little effect upon other selling costs taken together. Total marketing costs seem to rise with increased volume irrespective of advertising expenditures.

But it is not enough to point out that with the increase in advertising expense total marketing costs have risen. This accompanying rise in selling expense does not refute the contention that advertising may be a factor in lowering

marketing costs. It is probably true that marketing costs are increasing costs, but it may also be true that advertising by raising the level of marketing efficiency keeps these costs at a lower level than they might otherwise attain. If this is true advertising may be said to check the rise of marketing costs, which is tantamount to a relative reduction of marketing expense. For example, if we refer to that part of Table XI which shows both advertising and total marketing ratios increasing we find that total marketing expense for department stores increased from 28.7% of net sales for firms selling less than \$250,000 per year to over 30% for firms having sales of a million dollars and over, the highest figures being 31.9% for the \$4,000,000 to \$10,000,000 group. At the same time, advertising costs rose from a little over 2% for the lowest group to a figure as high as 3.4% for the last group above mentioned. It might appear from this that advertising had not only not contributed to lower operating costs but rather the contrary. However, any other means of achieving the same volume of sales might very well have caused a higher expense ratio, perhaps as much as 40%. Any increase above the maximum that would otherwise have occurred indicates the possibility that advertising has actually kept costs down. If there is reason to believe that there is no other equally economical means of widening the market, advertising has lowered costs even though they have absolutely increased somewhat.

But while advertising may not be able to reduce total marketing costs absolutely, it should have a more positive influence in lowering salesmanship cost. The primary function of advertising is to create demand and as such can be looked upon as either an agency to supplant or to supplement the work of the salesman. The mail order houses, or companies selling by direct mail advertising are illustrations of the former method. In some other cases, also, advertising is not to be considered as an alternative method of demand creation since it sometimes does work that could not be done otherwise. In sparsely settled communities or where the buyers are scattered advertising can build up sales where the costs of doing it by salesman would be prohibitive. Then again advertising can often reach customers when they are off-guard, and educate them, perhaps to their own benefit, when it would be hard for a salesman to approach them.(1)

Perhaps in most industries however advertising is used to support the efforts of the selling force. The

(1) This argument has been well put by A.W.Shaw in his book "An Approach to Business Problems" in the following way: "It (advertising) has been developed not solely to take the place of the middleman or salesman in demand creation but as a means of doing quickly, cheaply, and effectively much of the work these other agencies have done in the past and much which neither could profitably undertake at present." page 199.

relative importance of personal salesmanship and advertising in any business is a matter difficult to determine. There seems to be the opinion that usually these two selling agencies ought to be employed together, since a nicely balanced use of both will bring better results than either used alone. Of course the type of product to be sold and the extent of the territory covered will have direct bearing on the proportion of each of these types of selling effort to be applied. Undoubtedly business men are striving to make use of the best combination of their marketing factors, but there is much which stands in the way of accomplishing that end. In the first place the results of advertising in most instances are indeterminate. The owner of a business knows that he has spent so much for publicity and that sales increased by so much. Whether or not a different combination of factors would have brought better results he cannot tell. In time perhaps business research and market analysis will form a basis upon which advertising can be measured, but until then, a hit and miss method of experimentation will have to suffice. But it pays to experiment until the most economical proportions are hit upon; in other words the principle of substitution is at work which means that a producer will substitute one factor of production for another whenever, he thinks it pays. For example in production, capital, in the form of machinery, is apt to replace labor

if the former can perform the work more cheaply. This tendency is apparent in marketing for there are always new methods being tried out, in order to find ways of doing the distribution work more efficiently(1); and the middleman who clings to the old wasteful methods will lose out under free competition. Of course what is, is not necessarily right, yet there are undeniable forces at work tending to make it more profitable to use the best combination of factors. If advertising is wasteful it will tend to destroy itself, although the process may be a very slow one.

When actual business practice is examined in order to see how advertising does affect the use of personal salesmen, it is hard to get helpful data. Doubtless advertising has reduced the number of salesmen needed.(2) If Table XI is referred to again it will be found that advertising expenses range from .2% to 4.2% of net sales with an average figure around 1.8%.(3) This would mean that the average

(1) "It(advertising) tends to displace these other agencies in whole or in part, whenever it is a less expensive or more direct means of communicating ideas to the consumer. It cannot be dismissed as mere "puffing", because its substantial usefulness in our present scheme of distribution has been demonstrated". Shaw, A.W., "An Approach to Business Problems", Harvard University Press, 1920, page 202.

(2) "Advertising vs Salesmanship" L.D.H.Weld, Advertising and Selling, October, 1927, page 19-20.

(3) 2% of net sales is a common advertising appropriation for many business houses. For 1925 the total advertising figure amounted to more than a billion dollars, which was only one and one-half per cent of the entire production of manufactured goods. J. Walter Thompson News Bulletin, June, 1927, page 4.

sales per dollar of advertising would be roughly \$55. Sales per dollar of salesman's wages are much smaller than this. A study prepared by the Domestic Distribution Department, Chamber of Commerce of the United States, of the retail and wholesale trade of eleven cities reported that the average sales per dollar of wages in retail establishments selling some 47 different kinds of merchandise ranged from \$7.44 to \$9.53 (1) These figures are more or less comparable because advertising and salesmanship were used together in both cases. When advertising and personal salesmen are used together what effect do they have upon each other's costs? The data given in Tables XI and XII do not show very much relationship existing between advertising and total salaries and wages. In only four cases out of the sixteen businesses for which statistics are given was the highest advertising expense correlated with low selling force expense; in fact in most cases, eleven of the group, high advertising was accompanied with the highest total salaries and wage items. It would take more data than we have and a very careful analysis to measure definitely the correlation existing between high advertising and low wages, but the material that is available seems to point to the fact that increased advertising expenditures do not reduce salesmanship cost in every case.

(1) "Retail and Wholesale Trade of Eleven Cities", Domestic Distribution Department, Chamber of Commerce of the United States, May, 1928.

As we bring this discussion of the effect of advertising upon marketing costs to a close there seems one conclusion possible, namely that advertising must have very limited opportunities to lower prices to the consumers because the principles of large-scale methods of production do not apply to any great extent to marketing. It might be argued that this is an analysis of a given situation and that over a period of time decreasing costs might be obtained due to improved methods of marketing. That is, at any given time, if a business man decides to build up a national market for his goods and succeeds in establishing a tremendous distribution organization, costs will probably increase for the time being. If in the end, however, better marketing methods are evolved because the work is done on a larger scale, it is possible that marketing may involve falling costs, and hence that advertising could help to lower distribution expenses. Also at any given time it seems more than likely that advertising checks the increase in marketing costs and thereby lowers them relatively.

A final summary of this material should be made in connection with the discussion of the last section regarding the effect of advertising upon production costs. In the last section we found that if attempts were made to increase the output of such goods as farm products increasing production costs were probable. Likewise, insofar as the marketing costs

of such commodities act like the typical marketing expenses we have examined, we should expect them to increase.(1) It would appear therefore that advertising could have little tendency here to lower such prices. However in a dynamic situation taking into account the changes which will ordinarily come about, an increased output of farm products may be produced at falling cost due to better methods of production; to the extent that advertising tends to stimulate better technique in production and marketing it is one of the factors bringing about lower prices.

The same sort of analysis applies in the case of manufactured goods. In a given situation increased output would normally tend to be supplied at approximately constant production cost, and with increasing marketing costs. Hence advertising could do very little to lower the price to the consumer. But as was true with farm products, from a dynamic standpoint both production and marketing costs can be reduced. In actual fact new output is produced at lower unit costs for producing and distributing processes are continually being improved. These improvements are apt to come faster in manufacturing than in agriculture; hence the

(1) The marketing of farm products are apt to involve increasing costs more certainly and quickly than manufactured goods. For a discussion of the factors affecting the cost of marketing farm products see, "The Marketing of Farm Products" by L.D.H. Weld, p. 183.

conclusion must be that advertising as a part of the process inaugurating the new methods can be safely credited with helping to reduce prices.

As for decreasing cost goods such as public utilities there is even more opportunity for advertising to lower their prices. Even in a given state of the arts advertising can effect decreasing production costs by stimulating demand. Little is known about the marketing costs of public utilities, but if they are like other distribution costs they tend to rise after a very short stage of decreasing costs; but this increase in marketing expenses would probably not be sufficient to offset the decreasing production costs. In the last analysis, therefore, it must be concluded that in actual practice advertising tends to be one of the forces lowering price. We will now turn to a more detailed discussion of the reasons why advertising should have these effects upon marketing and production costs.

PART IV

EFFECT OF ADVERTISING UPON DEMAND.

As was brought out in an earlier part of this paper, a study of the economic consequences of advertising should analyze the effect of advertising not only upon costs of production and marketing but also upon demand, since price, or economic value, is a result of demand as well as of supply forces. Our analysis of the effect of advertising upon demand, however, must of necessity be brief and much more limited in scope than the supply discussion because the subject matter lies for the most part without the field of economics.(1)

Demand has been defined as the amounts which buyers stand ready to take at each of a series of prices. These amounts depend upon two factors, the income of the buyers and the utility of commodities to them. Thus the only way in which advertising can influence demand is by changing either anticipated utility or income. There is reason to

(1) Ordinarily the student of economics takes utility as his starting point and does not attempt to look behind it, leaving such investigations to the psychologist or the sociologist. Here, however, as we shall see later, deeper examination than usual is needed since the utilities created by advertising cause different demand schedules than do some other utilities.

believe that advertising can influence the former because the utility of a good grows out of a multitude of physical and psychological elements which advertising can reach^{and}/modify. In the first place by stimulating a diversification of wants it encourages the spending of income over a wider range of goods. It is a well-known economic fact that the marginal utility of a goods decreases as the stock of the article increases. If then income is divided among a variety of purchases, the utility derived from each unit of income will tend to become greater; consequently the valuation placed upon each kind of good will tend to be higher. These tendencies will reflect themselves in increased demand schedules.

In the case of new products advertising can also change demand by "creating" entirely new utilities, for new wants may be developed by making various appeals to the buyer's reason and emotions until he feels that the article is necessary to his happiness and well-being. For example, when invention makes possible the manufacture and sale of a hitherto-unknown contrivance like the radio, advertising can, by educating the public to its use, cause the article to have utilities which of course never existed before. These new utilities will change the demand not only for that product but for other commodities as well, and hence will influence price all along the line. Another illustration in

point is the increased demand for banking services built up in the last few years. Financially advertising has caused people to look upon banks in an entirely new light and as a consequence they have come to make more use of the trust departments, the checking system, and the savings accounts of their banking houses. Moreover through their advertising the bankers have helped to teach the nation thrift. Not only has this been done by encouraging savings accounts, but perhaps just as much by widening the market for sound investment securities. It might be pointed out, however, that advertising has had a counter effect upon savings, in that it has tempted some to spend beyond their means. To a great extent, for instance, advertising has been the means of reaching the consumer with installment-buying propaganda and other enticing sales talk which has made for prodigal spending. Such spendthrift buying would presumably eat into savings, but it has evidently not taken all of them, for the fact remains that the total amount of savings has been increasing along with the growth of expenditures upon luxuries and other goods. (1)(2)

(1) "It appears that annual savings, in terms of dollars with a constant purchasing power, from 1900 through 1913, averaged considerably less than one billion dollars a year, while from 1922 to 1927, savings averaged nearly two billions, and for the three years ended with 1927 held steady at a level somewhat about two billions." O.M.W. Sprague and W.R. Burgess, "Money and Credit and their Effect on Business." Recent Economic Changes, page 674, National Bureau of Economic Research, 1929.

(2) Probably the amount of savings (Continued on pg.99)

Thus advertising has changed the buying habits of the people; it has educated them to use new products and services and has showed them how to get more utilities from old ones. The continual fire of sales publicity is bound to show its effect in altered demand schedules, which may in some ways raise the standards of living.(1) E.E.Calkins says on this point: "Advertising is one of the great educational forces. ---The phonograph, radio, camera, motor car, vacuum cleaner, kitchen cabinet, safety razor were quickly and easily made necessities." (2) Objection might be made here that the ease and speed with which the new habits have been acquired, so that living is an entirely different matter than it was twenty-five years ago, have been attributable to other factors than advertising, for example better merchandising. Advertising, however, as an integral part of the

(2) (Continued from page 98) has been furthered by the fact that people have enjoyed increased incomes, which in part have been caused by advertising. This phase of advertising's effect upon demand through increased income will be discussed presently and until then the analysis is incomplete.

(1) Some critics would say that advertising has lowered the standard of living because it has standardized tastes, bringing all down to a common low level. On the whole this is an objection based on aesthetic values, but there would also be some economic consequences in that demand is stabilized on fewer products, a subject matter which will be taken up in the next section.

(2) Calkins, E.E., "Reading with a Purpose" American Library Association, 1929, page 21.

marketing process should be mentioned as one of the most important of the causes in determining changing buying habits.

Not all the buying habits encouraged by advertising are of the nature just mentioned. While it is true that advertising of the so-called "pioneer type which helps to introduce new products and services, may be defensible, insofar as it gives truthful information, there are some results of advertising which are questionable. The persistent bombardment of clever advertisements appealing to the weaknesses of human nature, often hoodwinks men and women into foolish purchases. One has only to glance through one of the modern books on how to sell goods, to form some opinion as to the strength of this influence. These scheming, cunning methods of selling are well illustrated in one treatise which says, speaking of how to control the indecisive type of customer: "Decide for the customer by positive suggestion." And for the suspicious purchaser the advice is, "Get the customer to agree with you by agreeing with some of his doubts and fears." Exert yourself is this writer's admonition, because "it takes a tremendous amount of mental energy ----to control another man's mind." One has misgivings as to whether modern methods of selling are truly educative in the right directions when he considers that an army of salesmen equipped by such training and supported by a barrage of the same kind of advertising is constantly attacking the consumer.

One bad effect coming from advertising of this kind is said to be the accentuation of the buying of "style" merchandise. While advertising has undoubtedly been successful in establishing some buying habits, it appears that it does not have much effect upon purchases determined by the fads of the moment. Cherington says that "style trends usually cannot be controlled by advertising" (1) Forces too fundamental and powerful for advertising to reach set the cycles of fashions, evidently; and effective advertising must follow the first indications of changes in style rather than attempt to change them. As one writer says, "Apparently Mrs. Partington and her broom have a better chance of sweeping the rising tide back into the ocean than advertising has of turning about an adverse influence. Advertising men themselves concede their inability to fight a "fashion". (2) If bad results come from demand for this kind of merchandise, the blame should not be entirely laid at the door of advertising.

There is, however, another criticism of advertising which is more justified, namely that much of the demand

- (1) Cherington, P.T., "The Consumer looks at Advertising" Harpers, 1928, page 26. See also this author's article in the Harvard Business Review, July 1924, entitled "Some Commercial Aspects of Styles and Fashions in the Clothing and Textile Industries."
- (2) Goode, K.M. and Powel, H., "What About Advertising"? Harpers, 1927. pages 171-2.

creation work of advertising amounts to nothing more than causing demand to shift from one product to another; or what is worse, perhaps, causing one brand to be replaced by another which to all intents is practically identical. If the new good is not better than the old one there has been no total social gain in the process. The point to be determined here, however, is not whether there has been a profitable change or not, but rather whether there has been any change which will affect price. In a discussion of the economic consequences of advertising apparently there should be no occasion to comment upon the kind of utilities advertising creates. Utility is a neutral term, i.e., the want-satisfying power attaching to a commodity, implying neither that the want satisfied be good nor bad. If advertising increases the utility of an article, demand and price should be affected regardless of the nature of the want. This is not quite the whole matter, however, as we shall see, since price is affected by the elasticity of the demand, which depends in part upon the type of product involved. In the case of food products, for example, there are very real physiological limits to the total demand of any one individual. Advertising may have the effect of diversifying the diet but the possibility of greatly increasing the consumption of food is clearly checked by the inelasticity of the demand schedule.

Clearly here is no solution of the farm problem.(1)

Regardless of the direct effect advertising may exercise upon demand in changing the utility of goods, there are some general results of advertising which will react upon the buyer. I have in mind the effect of advertising upon the quality of goods and the resultant outcome upon demand and price. The protagonists of advertising maintain that it has raised the general quality of merchandise on the market, since it places the advertiser and his claims under the microscope of popular scrutiny. Once an article is packaged, branded and advertised, the manufacturer's name is identified with the product and his success depends upon what the buyers think of the goods. Since it is not the present sales alone which will give him profit, but rather the steady repeat orders of the future, it will repay him to keep up the quality of his goods. As one writer says, "Advertising is a quick and sure test of merit of a product. It brings the buyers, but does not bring them back if they are disappointed in the product. On the contrary it merely reminds them that they were disappointed." (2) Thus the public has come to associate

- (1) See Taylor, A.E., "Consumption, Merchandizing, and Advertising of Foods", Harvard Business Review, April 1924 for an elaboration of this point.
- (2) Praigg, N.T., "The Advertising Yearbook of 1922" Associated Advertising Club of the World. Doubleday, Page & Company, 1923.

the advantages of packaging and uniform quality with advertised goods, whether justly or not.(1) Even if non-advertised products are as good quality as the advertised ones, it might be true that advertising is still responsible, since the presence in the market of one high-quality advertised good might tend to bring up the standard of all the other competing brands, whether advertised or not.

Many experiences of producers can be instanced in which advertising has been instrumental in raising the quality of the goods in question. One case in point is an experience of a successful candy manufacturer who had regularly advertised the superior quality of his product. At one time, due to a mistake, an inferior grade of confection was turned out. Not wanting to sell it themselves the company disposed of it to a marketing concern, but forgot to specify that their name be taken off; and as a consequence it was distributed all over the country under their label. The public's reaction was

- (1) In the investigation carried on by the Federal Trade Commission in 1929 regarding resale price maintenance it was found that consumers placed quite a bit of dependence upon brands and trade-marks as indications of quality. Part of conclusion reads: "Thus about 81 per cent indicated that they (the 1,990 consumers replying to the questionnaire sent out) place some dependence upon brands or trade-marks, while only about 17-1/2 per cent answered the question with a definite "No", indicating that they do not place any reliance upon brands or trade-marks as guarantees of quality." "Resale Price Maintenance" Report by Federal Trade Commission, Part I, Government Printing Office, 1929.

pronounced; the sales dropped off immediately and the company went down to a very low place in the industry. They had been educating the consumer to expect high quality and when it was not forthcoming, the buyer was not slow to detect it and turn to other goods. Such experiences soon teach producers that they must maintain high standards.

Generally speaking, however, it is probably nearer the truth of the case to say that maintenance of quality is due more to the sellers' efforts than to anything done by the consumers. In the absence of any thorough governmental assistance the buyer must depend upon the seller for information regarding commodities, since ⁱⁿ the complex of modern living there is no hope that any one can become an expert buyer in all the lines in which it is necessary to make purchases. The best results will be obtained probably by depending upon the self-interest of the manufacturers, and the middlemen who are anxious to please their customers. It is foolish to believe that the only way to make a profit is to make and advertise a poor article. "Snatch success" might be built up by advertising an inferior product, but in the end the safest way is to develop the market for good merchandise. One outstanding manufacturer, who has advertised extensively, has said that the way to success is to "raise the quality of the product without raising the price." (1) But

(1) Simmens, S.G., Printer's Ink Monthly, September, 1925.

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(1) Simmons, S.G., Printer's Ink Monthly, September, 1925.

not only must the quality be present, the consumer needs to be informed of it. Speaking of the inability of the ordinary buyer to know very much about markets and their goods, Wesley C. Mitchell says that, "Under these conditions it is not surprising that what the world has learned in the art of consumption has been due less to the initiative of consumers, than to the initiative of producers striving to win a market for their wares." (1)

And many are the examples in which the sellers have had to take the initiative in order to teach consumers the use of better products. One minor instance might be mentioned in the case of a manufacturer who developed a venting radiator valve which was much superior to the ordinary type on the market. While sheer quality built up a moderately successful business, it was not until the company used consumer advertising that the public was willing to accept the improvement on a large scale. (2) Another more important illustration is that of the front-wheel drive for the automobile. One advertising man has said that it would take millions of dollars to educate the people to its acceptance, although it would undoubtedly be a real advance in motor transportation equipment. A company would not find it sufficient

(1) Mitchell, W.C., "Business Cycles" National Bureau of Economic Research, 1927.

(2) Success Bulletin, #50. Revised, August 2, 1926.

simply to make a good car of the new type and offer it for sale; they would have to sell the public with the most vigorous kind of advertising.

The work of educating the consumer is never done. In the first place there will always be a need for a large amount of educational advertising to keep buyers informed about the new goods and the new uses of the old ones. Even if there were no new products there could still be found reasons for advertising. One of them is that every year a certain percentage of the population reaches the age where they are for the first time susceptible to advertising's appeals. For some products this age would be much earlier than for others, but whatever it is, there are thousands of people every year reaching that period in their lives, and hence providing virgin soil for the seeds of advertising. Besides this there is some justification, perhaps, for advertising that keeps the public sold on the products of old established concerns. A car manufacturer, for example, must advertise not only to the new sales prospects, but also to his old customers to keep them sold. If society is equipped to furnish certain goods and services, advertising which is employed to keep people buying these commodities is rendering an economic service.(1) It is probably an economical bit of the

(1) Stabilization of demand, while perhaps wise, in view of our limited resources, has disadvantages in that demand may be maintained for an inferior product. This will be commented upon further in the next section.

marketing mechanism that follows a company through advertising to maintain a following of buyers year in and year out.

But giving advertising all the credit that is possible on these scores, there is surely a question whether the billion and a half which is estimated as being spent yearly in the United States on advertising, is doing as much for the education of the public as might be the case if it were used in other ways. From an absolute standpoint, advertising certainly has not attained particularly imposing results. Considering the matter on a relative basis, however what agency would be able to do the task even as well as it is being done now? Thomas Nixon Carver in speaking of turning over the advertising work to the control of the government says: "This, however, would be a somewhat dangerous experiment, because such public authority would have to be exercised by public officers. ----The man who has succeeded in getting elected to office by campaigning, which is a kind of advertising is not necessarily the best man to decide upon what is good and what is bad advertising."(1) While there is no question but that advertising is in many ways educative in the wrong direction, and is an extremely wasteful method of accomplishing certain ends from the social viewpoint, yet

(1) Carver, T.N., "Principles of Economics" page 183.

its faults are the drawbacks of a competitive order. The common answer to such criticism is that the gains are larger than the losses.(1)

It was pointed out at the beginning of this section that demand could be influenced by a change in utility or in income. So far we have analyzed the effect of advertising upon utility finding that advertising has affected demand in various ways. It will now be found that advertising can also change demand by altering income. The usual argument is that advertising creates in man a desire for more economic goods and as a result he will produce more in order to command the income to buy the things he has been made to want. In other words advertising does more than divert demand from one good to another; it actually increases the buying power of individuals so that they can purchase the old products as well as the new. Of course advertising has been only one of the minor causes of increased income. Income is the result of man's struggle to earn a living, a battle which is fought with varying degrees of vigor depending upon how worthwhile he thinks it is. If advertising can stimulate man to work

(1) For a discussion of the advantages and disadvantages of a competitive order see "Plain Talks on Economics" F. Franklin, Putman, 1924, Chapter XXXIV and XXXV. Also Melvin T. Copeland in "Advertising and Selling" October 5, 1927. A discussion of whether or not socialism would be a remedy for the defects of advertising will be taken up in a following chapter.

harder in order to reach a higher standard of living, the outcome should be increased productivity on his part, and finally a larger flow of economic goods or income.(1) Advertising has kept man's desires beyond his grasp and has enticed him on and on in the attempt to have more. If people have not been over-stimulated and if they have not spent the added income altogether foolishly, there has probably been a net social gain.

But advertising not only may increase total money income, it may also add to the amount of satisfaction, the real income, derivable from a certain number of dollars. As we have noted in previous connections, prices may be reduced by the use of advertising. When this is the case, money income could stay the same or even decrease, and each individual might be able to enjoy more goods. Advertising, moreover can increase real income by increasing the amount of consumer's surplus resulting from buying advertised goods.(2) Consumer

- (1) It is an actual fact that the average income of the United States has been increasing, though, of course as it has been said, the cause of the increase is not solely advertising. "During this period (1913-1927) the per capita realized income has considerably exceeded all previous records, even when price changes are allowed for". Morris A. Copeland "The National Income and its Distribution" Recent Economic Changes, page 838.
- (2) There is a difference between the changes in money income and changes in real income, since the latter are the result of demand and price while the former are determinants, at least in part, of demand and prices.

surplus is the difference between what a buyer would be willing to pay for a good and what he has to pay for it in view of the market price which is ordinarily close to cost of production. If price hovers close to a figure based upon competitive costs, and the buyer is in the mood to pay a great deal more due to the fact that the good has been advertised, the purchaser is the recipient of more consumer's surplus. For example, if a line of women's coats were widely advertised and a huge sales volume built up, a lower cost of production and marketing might be effected. If as a consequence price were as low or lower than similar non-advertised coats, a woman buying one of these garments would be getting more satisfaction than she pays for.

So far we have found that advertising is liable to increase the estimation put upon goods by consumers, and furthermore that it may tend to increase total purchasing power. What will be the effect upon price? If there has been increased utility, the buyers are willing to pay more than they did before; this is increased demand. If income is made greater this too will tend to make demand greater. Increased demand in and of itself tends to raise prices. But in the analysis of costs of production and marketing we came to the conclusion that in many cases advertising is apt to lower prices. Apparently we have advertising setting up two

counteracting forces; one tending to lower price, the other serving to make individuals willing to pay more for goods. This, however, is an unreal paradox. It is the increased demand that allows the production costs to drop. Under competitive conditions, if advertising is able to lower the costs of production and marketing, there is every reason to think the prices will tend to be close to this cost. Even if buyers are willing and able to pay more they will find that they will not need to because, barring monopoly, sellers will bid price down to cost of production in order to get the market.

If competition is not maintained, however, the effect on price may be altogether different. Many believe that vast amounts spent upon advertising can create a quasi-monopolistic condition which allows the producer to put up the price.(1) In some cases advertising appears to affect both the supply and demand forces in such a way that an equilibrium condition is established at a price much higher than competitive cost. The high-pressure advertising and marketing is so costly that although costs of production are cut by large-scale economies, the total costs may be materially increased,(2) so that the producer would make no exorbitant rate

(1) The problem of advertising's effect upon competition will be analyzed in more detail in the next chapter.

(2) This is not contradicting the previous analysis which brought out the point that advertising may lower costs of production; rather it is an illustration of the point made that if advertising is applied beyond the point of maximum efficiency any industry is apt to encounter increasing costs.

of profits, even at the high price level. At the same time, advertising has put the consumers in such a state of mind that they are willing to pay the high price. Will not potential competition spoil this game? In order that a competitor might break the consumer's prejudice in favor of the one article, he must likewise advertise on a tremendous scale, and in the end he would have the same high costs, counting advertising, that the first manufacturer had. This seems, then to be a self-perpetuating monopolistic condition. Although there may be counteracting force at work as long as the condition lasts the goods command the market and prices are apt to be higher than they would be without advertising. A monopolistic condition is particularly bad for the consuming public when the demand for the good controlled is very inelastic, that is when the buyers are willing to buy about as much at a very high price as they would at lower prices. If the demand falls off very rapidly at higher prices, the monopolist is unable to boost his price very far above costs. Then the question is, does advertising make demand more inelastic? It probably does not. To a great extent elasticity of demand depends upon the nature of the product, which advertising may not be able to influence materially. Insofar, however, as advertising does create monopolistic conditions for inelastic purchases it is a dangerous outcome of advertising. To what degree advertising has such an effect it is difficult to

determine. Certainly the criticism is made often enough that advertised goods are higher-priced than non-advertised goods. The sales manager of a large grocery chain system in a recent conversation with me expressed the opinion that a study of prices in that system would reveal the fact that non-advertised goods had a price advantage over advertised articles of the same quality. To the extent that the chain tended to cut prices on advertised goods, the real margin in favor of the non-advertised goods would be still greater in independent stores.(1)

As we try to summarize the discussion regarding advertising's effect upon costs of production, marketing expenses, and upon demand, no conclusion can be reached as to the final outcome upon prices. All that can be said is that there are some forces at work to lower prices and some to raise, with the presumption being perhaps that the former will be a little more apt to outweigh the others if competitive conditions are maintained.

- (1) Question might be raised whether or not the chains cut prices on advertised goods; One study made by Professor R.S.Alexander of Columbia University came to the conclusion that, "On the whole this summary of our survey seems to indicate that for the products included and among the stores from which we obtained price quotations, neither chains nor independents have any material price advantage." "A Study in Retail Grocery Prices." page 7.

PART VI

EFFECT OF ADVERTISING UPON THE EXISTING
ECONOMIC ORDER.

In the foregoing chapters the analysis has dealt strictly with the problem of the effect of advertising upon prices. There are results of advertising, however, which although they do not bear directly upon prices, need to be commented upon since they tend to alter the economic system in which prices are determined, and hence influence value in the end. For example, advertising may in some ways stabilize demand; may bring about standardization; encourage market research; change competition; and perhaps influence the allocation of productive factors. It will be the purpose of the present section to discuss how advertising has probably modified the present order along these lines.

In the first place many believe that one of the most important functions of advertising is its power to stabilize demand. It should and could be used for this purpose, though there is a question whether it is. As one writer has pointed out, "Economically speaking, the function of all advertising and all solicitation of demand is to maintain suction during the lapses between periods of natural recurrence of demand. It induces demand at a pressure, which is more

or less even, instead of permitting it to come fitfully at moments when the organization of supply is ill prepared to meet it."(1) Thus advertising gives to a producer a weapon wherewith to control his market; whether it is used wisely to accomplish that end is another matter.

There are several ways in which advertising might be used to stabilize demand. It is a well-known fact that advertising has occasionally maintained demand for whole industries which for some reason or other were losing their markets. For example, in the case of the wooden spoke wheel for automobiles advertising was used to revive demand after there was every reason to think that the industry would go bankrupt. Likewise, demand for bicycles has been sustained and even enlarged from time to time. This is an example of a product which might have fallen into complete disuse, if it had not been for the selling activities of the manufacturers. This argument is also well illustrated by the experience of the Victor Talking Machine Company. With the introduction of radio, sales for this industry fell off, but through the use of advertising, featuring their new orthophonic instrument, the demand was maintained and even increased.(2)

(1) Dibblee, G.B., "The Laws of Supply and Demand", Houghton Mifflin Company, 1912. page 189.

(2) Success Bulletin #32, Periodical Publishers' Association Revised October 11, 1926. More recently the Victor Talking Machine Company has merged with Radio Corporation of America. In order to keep up sales of the phonograph however, the company will have to maintain its advertising.

Not only does advertising help to salvage whole industries from the scrap heap, which may be a social gain reflecting itself in lowered costs and prices (1), but it can also help out in the temporary difficulties of business houses which are ordinarily successful. As one business man put it advertising is a kind of insurance paid for in good years to support the business in slack periods. It is said that the Buick Motor Car Company found it much easier to preserve their organization during their unfortunate experience of 1928 because of the goodwill built up by years of advertising. Likewise it is reported that the American Walnut Lumber Manufacturers saved their industry from a post-war slump by working out a dealer-and-manufacturer advertising campaign which at the close of the war was extended into consumer advertising on a cooperative basis. Not only did they help themselves temporarily, but a new business was developed larger than before the war.(2)

Lack of advertising is held responsible for the bad state of affairs in some industries and for the prosperous condition of others. After making a comparison of advertising

- (1) As has been remarked before it is an open question whether demand in such cases has not been stimulated for undesirable industries, which should be allowed to disappear.
- (2) Agnew, Hugh E., "Cooperative Advertising by Competitors". Harpers, 1926, pages 179-80.

expenditures for particular commodities, one writer remarks that "These detailed figures for changes in the expenditures for magazine advertising by the producers of various commodities provide significant facts for the analysis of causes of the degree of prosperity and rate of growth of numerous industries." (1) The lack of prosperity in the textile industry and in the furniture trade may in part be attributable to the failure of these manufacturers to stimulate a sufficiently effective demand for their products.(2) One study that was made of the relation between business failures and lack of advertising found that the "Average percentage of failures made by non-advertisers for thirty-two cities in nineteen states was 83.6% of the total".(3) While this cannot be considered in any sense as an indication that lack of advertising is a cause of business failures it at least affords an interesting side light on the problem and furnishes food for consideration.

A great many industries have also found that advertising can be a decided help in smoothing up demands which take

- (1) Copeland, Melvin T., "Marketing", Recent Economic Changes, National Bureau of Economic Research, page 419.
- (2) However, I have learned from good authority that the Grand Rapids Furniture Manufacturers are planning an extensive cooperative advertising campaign in the near future.
- (3) Printers' Ink Monthly, May, 1927.

definite periodical swings. One writer goes so far as to say that "Advertising makes a seasonal product an all-the-year-round one."(1) While it is highly improbable that the demand for some kind of products like seeds, farm machinery, toys and the like could be made constant throughout the year it is true that other producers have been more fortunate in manipulating their sales curves to get a steadier demand. For instance, the growers of oranges, walnuts, almonds, raisins, lemons have been successful in changing the seasonal nature of their demands. The California Fruit Growers' Exchange, for example, through their advertising have materially changed the demand for citrus fruits. At the time their advertising started, the winter and spring shipments from California were approximately twice those of summer and fall. Now they are reported as being more nearly equal. Another outstanding example of successful attempt to steady demand is the history of the American Express Company with its travelers' cheques. Through advertising, new markets were developed in connection with domestic travel so that the sales were made nearly uniform throughout the year. December sales were made greater than were those of June before advertising.(2)

Although advertising may be a powerful factor in

- (1) Goode and Powel, "What about Advertising?", Harpers, 1927, page 29.
- (2) Success Bulletin, Periodical Publishers' Association, July 1, 1928.

equalizing demand in some instances, there is a strong tendency not to use it for this purpose. Business men, in actual practice are more likely to advertise in the months which are known to be good, and to slacken up when people are not buying. This manner of handling the advertising appropriations is illustrated in the following table. It is evident from these figures that the jewelers in this group "commonly adjusted their advertising expenditures to accord roughly with the expected seasonal variation in sales"(1). To a large extent department store advertising also closely follows the seasonal swings through the year. A study made by the Metropolitan Life Insurance Company, found that there was a close correlation between monthly sales and departmental advertising expenditures in 250 dry goods stores.(2) There probably is a tendency to fit the advertising to the sales curve ---and thereby to heighten the monthly sales differences.

(1) Harvard Business School Bulletin, #76 "Operating results of Retail Jewelry Stores for 1927".

(2) An analysis of the statistics gathered by the Controllers' Congress of the National Retail Dry Goods Association, by the Policyholders Service Bureau, Metropolitan Life Insurance Company, regarding the relation between monthly sales and advertising expenditures for the various selling departments of department stores. Domestic Commerce Bulletin, September 23, 1929.

TABLE XIV

Seasonal Variation in Advertising.
147 Jewelry Stores, 1927.(1)

	Advertising Expense	Net Merchandise Sales
January	95	70
February	65	55
March	80	60
April	80	70
May	90	80
June	105	105
July	70	60
August	70	70
September	90	80
October	110	80
November	145	100
December	200	370

While we may be able to point to certain instances in which advertising has been used to accentuate seasonal variations and other periodical ups and downs, it is probably wrong to conclude that advertising has been generally employed in this fashion. Perhaps just as many other cases can be cited in which advertising has tended to iron out these fluctuations. However, when we turn to the discussion of the business cycle, which is an entirely different phenomenon, we find that it is a question whether advertising has checked or stimulated this condition in business. Many students of the

(1) Harvard Business School Bulletin, #76, "Operating Results of Retail Jewelry Stores for 1927."

problem feel however, that advertising has been a potent factor in the control of the business cycle. Even the critics of advertising who like to attribute some of the bad effects of cyclical movements to advertising are usually willing to admit that there is a possibility that publicity could be used for this purpose(1). Before we turn to a discussion of certain cases in which individual firms have used advertising in such a way as to mitigate the effects of business ups and downs, let us consider very briefly the different advertising policies which would be feasible in the different phases of the business cycle. There are three different policies which may be followed in planning advertising in relation to the cyclical fluctuations; advertising can move with the various phases of the business cycle; or against them; or it can be used continuously regardless of business conditions. The first policy is the one usually followed, that of advertising heavily when business is good and very lightly in depressions, since there

- (1) One writer says, "At present its (advertising's) net influence is to intensify the variations from "normal" business. It might be used, however, as a tool to control partially the course and duration of cyclical movements". Vaile, R.S. "The Economics of Advertising", Ronald, 1927, page 127.

are ready funds in prosperity. There is, however, more than just a matter of funds to be considered. For some goods like textile machinery it would be obviously foolish to do anything else than follow the trend of business. On the other hand the advertising of such staple commodities as staple food products should probably be continuous since there is about as much demand for necessities in depressions as in better periods. Moreover, if it is the intention of a company to build up general good will, it is obvious that advertising should be practically steady, regardless of business conditions. Likewise, in the case of expensive items such as automobiles, where the buyer is apt to decide a long time in advance as to his purchases, perhaps it is best to do continuous advertising, with little relation to changing phases of the business cycle.

There are some business men, however who feel that they can master the periods of depressions which strike at their sales and they use the third alternative, advertising against the business cycle. The Dennison Manufacturing Company for instance, has consciously tried to control sales by withholding new designs until depressions. At that time the new features are brought out and advertising greatly increased; in good times advertising is allowed to drop off, the belief being that the company will get all the business it can handle anyway. Such timing of advertising has enabled the company to weather depressions and maintain sales. For

example, "During 1921 and 1922 the sales did not decline in the proportion common to other concerns." (1) This result came about not only because of advertising's effect upon the consumer, but also because it helped to keep up the morale of the salesforce.

Other concerns have also tried to improve their sales position during slack periods. The data though scanty are significant. For instance, the Hygienic Products Company found that by advertising heavily during the depression of 1921 they were able to increase the sales of Sani-Flush, one of their products, by 30%, over preceding years. A recent letter from them stated that, "Owing to the recent stock market depreciation and its quieting effect on sales, we have decided to increase our advertising appropriation for 1930 on both Sani-Flush and Mel'o. This is clearly an example of using advertising to counteract an adverse business period.

But perhaps these are outstanding examples and a better check on how advertising has been used, might be had by comparing what all advertisers have spent with some representative business index. One study of this nature covering the years 1919-1926, compared total magazine advertising lineage and total newspaper advertising lineage in the United States with bank debits outside of New York. (See Chart IX).

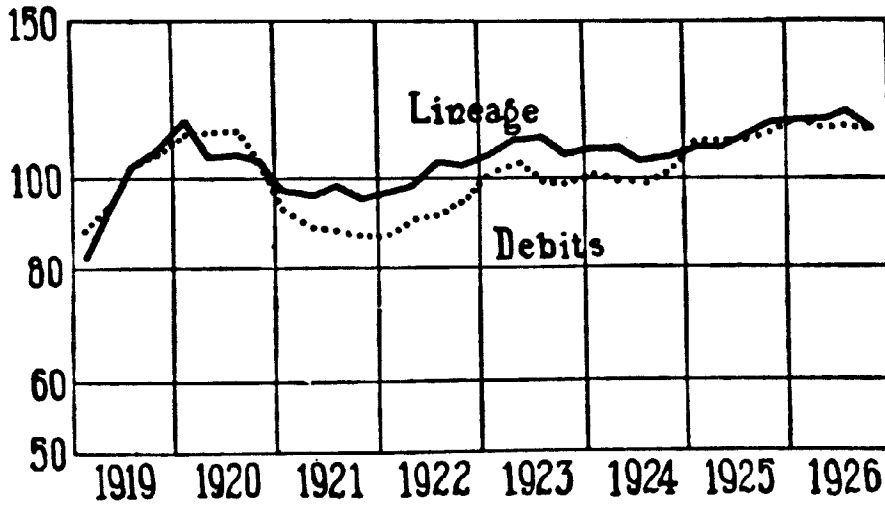
(1) The Harvard Business Review, Volume 1, October - July, 1922-23. The Hammett Manufacturing Company, page 380.

It was found that "Through most of the movements since 1919, there is a clearly noticeable tendency for the fluctuations in the advertising curves to precede slightly corresponding movements in the curve of general business activity. This anticipatory character of cyclical fluctuations in advertising is to be expected in view of the obvious relationship between advertising activity and the business which it serves to produce."(1) The author seems to imply here a causal relationship between advertising and the business cycle.

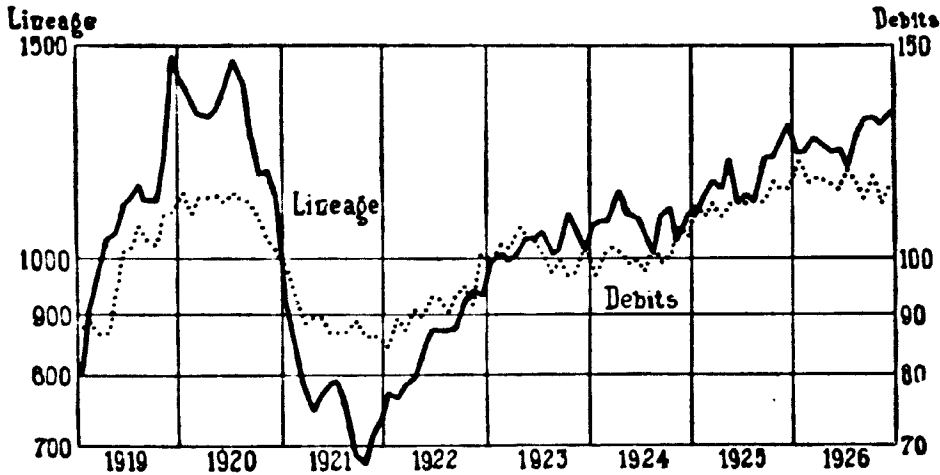
Another study made for a shorter period, 1919-1923, brought together money incomes of factory workers and magazine advertising. (Chart X) The comments were that: "As has long been known, newspaper and magazine advertising respond very definitely to the changing course of the business cycle. Magazine advertising varies much more nearly in harmony with our index than does newspaper advertising, though preceding it by a short interval. Whether advertising should be allowed to bear to the buying power of our large, variable-income group the relationship here disclosed, is a question which gives much food for thought. Certainly, the relation seems a plausible one; yet, further investigation may show that a

(1) Crum, Wm. L., "Advertising Fluctuations: Seasonal and Cyclical", A.W.Shaw Company, 1927.

CHART IX(1)



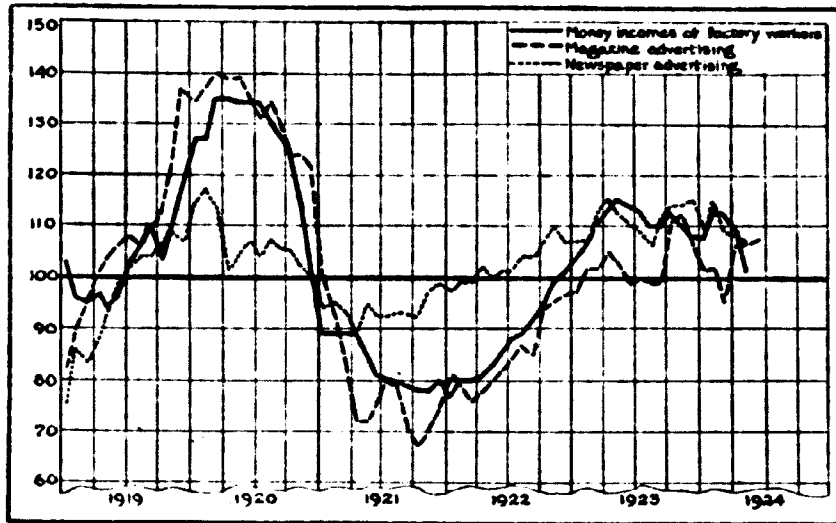
Comparison of total newspaper advertising lineage in the United States with bank debits outside New York.
(Unit: per cent. Both series corrected for seasonal variation.)



Comparison of total magazine advertising lineage in the United States with bank debits outside New York.
(Unit: for lineage, 1,000 lines; for debits, per cent of normal. Both series corrected for seasonal variation.)

(1) Ibid, pages 10 and 11.

CHART X (1)



Money incomes of factory workers compared with advertising
(Base: 1919-1922 average = 100. Unit = 1%)

- (1) Berridge, W.A. "Purchasing Power of the Consumer"
A.W.Shaw and Company, 1925, page 54.

different system of publicity planning might well be undertaken by advertisers bent upon tapping the market at the most favorable times."(1) This discussion also seems to imply that advertising might be used to control sales movements.

Whether or not advertising actually has any such power it is hard to say. A brief analysis of the causes of the business cycle might throw some light on the question. Professor A.C. Pigou of Cambridge University is of the opinion that "the movement of business confidence" is "the dominant cause of the rhythmic fluctuations that are experienced in industry," "optimistic error and pessimistic error" giving birth to one another in an endless chain.(2) Advertising based upon a firm foundation of economic data, might be used to counteract these periods of optimism and pessimism (3). Another current theory of business cycles is that they are caused by a "lack of equilibrium in the process of producing and consuming goods in general, that is, waves of overproduction result

- (1) J.Walter Thompson News Bulletin, March, 1924, page 14. Also, Berridge, Wm. A., "A Statistical Index", pages 53-56. A.W.Shaw Company, 1925. "Purchasing Power of the consumer".
- (2) Mitchell, W.C., "Business Cycles: The Problem and Its Setting". National Bureau of Economic Research 1927, pages 17-18.
- (3) That advertising is looked upon as a weapon to wage war against wrong psychological factors in business is evidenced by the recent billboard campaign sponsored by many local communities in an effort to develop a spirit of optimism to combat the present depression.

from "the well-nigh universal fact of industrial competition.

(1) If business ups and downs are caused by the maladjustment of production to demand, advertising might be a saving factor insofar as it could direct consumption along the right channels to absorb certain overproduced products. In dealing with the dangers of over-production it ought to be borne in mind, that the "solution of the problem consists not in limiting production to available consumer's money demand, but in sustaining consumer's demand on a level with available production." If this is true then clearly advertising can be said to play an important part in alleviating such distresses. As another writer says, "Advertising is essentially a device for overcoming the strains and stresses which rack an industrial society operating on a machine technology under a control system based on private property and the division of economic interests. The process of advertising and the organization of statistical services represent definite movements upon a considerable scale to correct, or to counteract the maladjustments flowing from the separation of producers and consumers" (2)

(1) Mitchell, W.C. "Business Cycles: The Problem and Its Setting" page 50-51.

(2) "Trade Associations: Their Economic Significance and Legal Status". National Industrial Conference Board, 1925. Page 236.

If it can be concluded from the above discussion that advertising has in any way stabilized demand it follows that it must also affect costs and prices. In steadying demand, causing it to ride a more even keel, advertising allows a company to plan ahead; to budget its business scientifically; to cut down on stocks and inventories; and to gain a more rapid turnover.(1) Thus advertising may influence prices by stabilizing demand. We will now turn to another possible channel, through which advertising may work to change economic value, marketing research.

Marketing research has had no inconsiderable development in recent years, a phenomenon which can be attributed very largely to two circumstances. In the first place the tremendous growth in our productive efficiency has made it possible to produce more goods than our distributive mechanism could dispose of easily. In attempting to solve their marketing problems, producers have utilized the same methods which they have found successful in production, namely invention,

- (1) If advertising makes the demand consistent and steady for an article there is sure to be some reaction on the costs of handling it. A study made by the Druggists' Research Bureau ascertained that toilet goods which were consistent sellers were about eight times as profitable as average stock. This reduction in selling expense will tend to lower the price of these profitable items under ordinary competitive conditions. Report in Domestic Commerce Bulletin. May 27, 1929, Page 4.

investigation, and business research in general. Marketing analysis, therefore, has largely been an outgrowth of business research in its broader aspects. Once attention was directed towards scientific analysis of marketing, however, there has been no dearth of supporters. The advertising agencies, the publishers, and others directly interested in the publicity business(1) were quick to seize upon this tool and to utilize it as an adjunct to their activities. Their own self-interest dictated a policy of studying the markets since an advertising campaign based on a careful examination of the marketing factors of demand and competition was much more likely to prove successful than one based upon guesswork. As one writer says, "There is no question but that market analysis prevents misdirected or inadequate advertising, and in many ways it is true that the results of the analysis are directly applicable to advertising."(2) Business men are coming to

- (1) In the 1928 edition of the "Market Research Agencies" published by the United States Department of Commerce, five advertising agencies are listed as having done original research in the field of marketing, while twenty-nine individual businesses are included, and over a hundred magazine and newspaper publishers. Of course much of the work done by advertising agencies and business firms would be of a confidential nature and would not be available for general use, and hence not included in this pamphlet.
- (2) White, Percival, "Market Analysis", McGraw Hill Book Company, 1925.

realize, therefore, that market analysis should be the "groundwork of advertising".(1) A producer ought to know his own product, its advantages or disadvantages, the best design and packaging as required by the market; he ought to know his competitors' products as well as his own; he should thoroughly understand his market, its location, its size, the retailer and consumer attitudes; the climatic and seasonal conditions which might affect his sales; the best media for carrying out his advertising policies.(2)

Though advertising has been a factor of no little importance in the development of marketing research, it should not be given all the credit for the benefits coming from such analysis, for there could be and has been much research without advertising. The two are separate processes; the fact remains, however, that they have been looked upon as almost inseparable. Furthermore, advertising departments and agencies, in their struggles to win a better understanding of market forces have been pioneers in some phases of the work.

- (1) "Advertising: Its Problems and Methods", J.H.Cover. D.Appleton and Company, 1926, page 17.
- (2) For a discussion of the value of scientific study and planning, see "Business Statistics", M.T.Copeland, Harvard Business Press, 1917. Pages 272 and 178; and A.W.Shaw, "An approach to Business Problems" Harvard University Press, 1920, Chapters XIII and XIV. Also artical in Printers' Ink Monthly, September, 1924, page 71; and one in the Harvard Business Review, January, 1929, entitled "Analyzing Advertising Results" by A.F.Falk.

To the extent that advertising has encouraged and facilitated market analysis it should be credited with a share of the accruing benefits. Thus in some measure it would be responsible for the increase in productive efficiency which follows the reduction of guess work in distribution. The cost of performing the marketing functions of risk-taking and financing, as well as the expense of demand creation might well be affected, and marketing cost have a tendency to drop.

In the preceding discussion we have shown that advertising may influence costs of production by stabilizing demand, and by stimulating the use of market analysis. Advertising may also change business conditions and hence economic values, by furthering standardization and simplification. Standardization has been defined as "the art of process of conforming to any measure or extent, quantity, quality, or value established by law or general usage or consent", while simplification is "the art of rendering simple or making less complex." (1) It is difficult to determine what part advertising has played in these movements. In some ways it has been responsible for a great deal of standardization and simplification and in others it has caused diversification. Within individual businesses there seems no question but that advertising has brought about much standardization. As one

(1) "A Primer of Simplified Practice", Bureau of Standards, Washington, D.C., 1926, page 9.

writer says, "It is well recognized that the spread of advertising, extensive, intensive, national, producer advertising, mainly accounts for the phenomenal development in modern times of the practice of standardizing commodities and marketing them under distinctive trademarks".(1) In order for a manufacturer to make use of mass selling methods he must first produce a highly standardized product on a large scale. Advertising would be far too costly if it were used to market small outputs which varied from time to time, since it is the cumulative effect of advertising which makes it possible to use such an expensive tool in demand creation. Repeat sales, however, can only be built up if the goods are practically uniform. This being the case advertising has been one of the causes of increased standardisation.

Advertising has also caused some manufacturers to simplify their lines. Only a limited amount of detail can be effectively advertised, and from the standpoint of demand creation alone producers often find it more profitable to push a highly simplified, standardized line than a more varied one.(2) It has been estimated that "in most lines of business

- (1) "Public Regulation of Competitive Practices" National Industrial Conference Board, 1925, page 82.
- (2) For a discussion of this point see paper given before the Washington Advertising Club, Washington, D.C. October 20, 1928, on "Standardization, Simplification and Advertising", by Ray N. Hudson, Assistant Director, National Bureau of Standards, United States Department of Commerce.

80% of the business comes from 20% of the line", (1) and any agency which encourages or forces the manufacturers to drop the non-paying sizes and types of products is a factor in lowering costs. In many cases advertising has performed such a function. An example in point is the experience of one middle western manufacturer who says, "After I had been advertising quite a while I found my business was bunched largely in a few items. ---- The result is that today I have standardized (simplified) my production. It was advertising that showed me what numbers were in best demand."(2)

Within individual companies, therefore, there seems to be some evidence that advertising has tended to simplify and standardize the product which it helps to market. On the other hand it is sometimes pointed out that advertising tends to diversify commodities as between manufacturers. In their desire to find something unique to advertise producers have consciously made their products appear different from those of competitors, and as result there tends to be at least as many varieties of any one good as there are manufacturers in the field. In a great many instances, however, this sort of diversification is not harmful--in fact it is probably desirable from the standpoint of the consumer in that he has

(1) Ibid.

(2) Printers' Ink Monthly, May 1927, page 42. W.A.Strong.

a wider selection of goods to choose from. The purpose of standardization is to effect economies in production and would apply mainly to work carried on within one business unit. In many cases, if the firms in a certain industry are each producing their own standardized line on a large-scale there is little to be gained by a complete standardization and simplification of the whole industry. This however, would not apply to some products: In the cases of industrial purchases such as construction materials, mill supplies, shop equipment, it is advantageous in having the products of one firm interchangeable with those of others. Here there is need for standardization and simplified practice between industries. If simplification and standardization are to be effected between companies however, the initiative must come from some outside source.(1) Advertising will be a hindrance rather than a help.

- (1) The government through the Federal Trade Commission, The Bureau of Standards, The Federal Pure Food and Drug Act, the Bureau of Markets of the Department of Agriculture; and the Division of Simplified Practice of the Department of Commerce, has been largely instrumental in this work of simplification and standardization. The trade associations and other private agencies have also helped. In a later discussion of the future of advertising the work of the government along this line will be taken up.

Sometimes the argument is made that advertising and standardization are irreconcilable, because all the features of the product which are standardized are no longer selling points.(1) Standardization carried to extreme lengths would doubtless tend to decrease the amounts spent upon publicity, and to that extent advertisers may fight this trend in production. But even with a great deal of standardization present there is much left to advertise. For example many drug preparations are identical as to formula, yet individual manufacturers make use of advertising with profit. Likewise the railroads, though they have been subjected to a great deal of standardization, find much to tell the consumer. In fact as long as competition itself is not eliminated at all points, and production is carried on by free, private initiative, there will be a place for publicity. It has been pointed out that, "There are such individual factors as company reliability; assurance of progressive product improvement through intelligent engineering or painstaking research ; ability to assist buyers by prompt deliveries; competence of representatives to advise on use and application of the product and on the conditions of the market. There are a hundred respects in which firms differ from each other. All these affect the willingness of the buyer to take one manufacturer's

(1) See Stuart Chase and F.J.Schlink , "Your Money's Worth", MacMillan, 1929.

product rather than another's even though the products appear to be similar." (1)

The net influence of advertising upon simplification and standardization is hard to measure. I would be inclined to think however that it has furthered these movements more than hindered them. If this is the case, advertising has been a factor in lowering cost. Professor F.E. Clark of Northwestern University has said that "The economies of large-scale standardized production would be impossible were not large market created by the sales force and advertising".(2) The government has estimated that simplification and standardization saves the business men of the country some \$300,000,000 annually. In pointing out some of the specific advantages which follow the adoption of simplification, for example, one government bulletin states that less capital is tied up in slow-moving stocks; less special machinery is needed; increased turnover is effected; less storage space required; overhead expense is cut; handling charges, and clerical work are decreased.(3)

One counter charge to the above is that standardization and simplification cut down productive efficiency in that

- (1) "Advertising and the Maintenance of Prosperity", James H. McGraw, 1928. (Booklet)
- (2) "Principles of Marketing" page 403.
- (3) "Simplified Practice: What it is and What it Offers". Bureau of Standards, Washington, D.C. 1928. pages 2-4.

they hinder the development of improved methods. It is argued that when a qualitative standard for a product is set, it tends to become the maximum as well as the minimum level of excellence. The Bureau of Standards, however, in referring to its work on simplified practice is of the opinion that "It in no way restricts improvements in method or the progress of invention." (1). Of course the results of the simplification and standardization which come through a cooperative body either sponsored by the government or by some trade association would depend upon the manner in which the work is kept up-to-date. There would need to be continual revision of the recommendations, in order to further progress.(2) On the whole, it is commonly believed that standardization and simplification are apt to be more advantageous than otherwise. Insofar as advertising has been a factor in stimulating such movements, it has, therefore, reacted favorably upon costs.

So far in this chapter we have examined the effect of advertising upon the stabilization of demand, upon business research and upon standardization and simplification. We must now consider two problems of a somewhat different nature, the effect of advertising upon competition and upon the alle-

(1) "Elimination of Waste; A Primer of Simplified Practice". United States Department of Commerce, 1926 pages 1-2.

(2) One other criticism is sometimes heard, namely that standardization of products makes for standardization of tastes, of art, and even of the thinking of the people. This phase of the problem was discussed in the chapter on the consumer.

cation of the economic resources of the country.

Competition is the striving of buyers and sellers to gain their own ends; buyers competing with buyers to purchase in the lowest market; sellers with each other to win sales. Perfect competition assumes a perfect market, one in which each buyer and seller knows the bids or offers of every other buyer and seller, and is motivated by the purest self-interest in using that knowledge. While such conditions could scarcely be realized in real life, yet it is important that the actual market conditions approximate as closely as possible this hypothetical "perfect market" since it is in the market that the prices emerge which regulate production and consumption. The very foundations of our present economic order seem to rest upon competition, and any unnecessary, extraneous force interfering with its functioning is to be condemned. If it is true as some believe that advertising has hindered the normal action of competition, the entire market mechanism has been meddled with and the resulting prices are not apt to be the "right" ones, economically speaking. As one writer put it, "In practice, of course, there is no such thing as perfect competition, and, even where advertisement is absent, these assumptions are never completely fulfilled. But in a world where advertisement is largely used, they cease to correspond, even remotely, to the facts."(1) On the

(1) Braithwaite, Dorothea, "The Economic Effects of Advertisement", The Economic Journal, March, 1928.

other hand there are the advocates of advertising who declare that competition has not been destroyed, in fact it is claimed that improved market conditions have been brought about by the presence of advertising, since it tends to make the consumer a better-informed buyer.

There are two ways in which advertising may change competition. It may alter the competition between sellers, or it may effect the buyers' side of the market. First, as was pointed out in a previous connection, in some instances advertising has a tendency to bring about a certain combination of circumstances which gives an advertiser almost undisputed command of his market (1). Not only is this the opinion of the critics of advertising but of many advertisers as well. Often the chief advantage of advertising in the eyes of business men is that it raises their products out of competition, a sort of "tonic for the price competition malady". The following excerpt from a current article gives one an idea of what advertising is expected to do. After describing the advertising policy of a certain producer the comment was that, "This manufacturer attained such a strong position in the western field that one of the big national manufacturers eventually had to buy the business at a high price so as to break into this territory. Advertising plus a quality product, a

(1) One has only to think of such products as the Gillette safety razors, W.igley chewing gum, Ivory soap to realize that advertising has been a major factor in bringing about such dominance of the market by one manufacturer. This, however, may not give the advertiser any "monopoly" power.

good organization and vision had built an impregnable barrier against the inroads of competition".(1) Clearly a strong argument that advertising excludes competition (2). This constitutes one of the most serious indictments of advertising, since to be in keeping with the present system advertising should encourage price and quality competition.

Another phase of the same subject is the effect of advertising upon concentration. The criticism is common enough that advertising has tended to stifle competition by driving out the small competitors. While the disappearance of the small businesses may not completely hinder the workings of competition, it will at least change its nature. The result may be that prices are affected either adversely or favorably. The first question to confront us is what evidence is there of growing concentration in industry? One study recently made of the increase in size of industries came to the conclusion that "The trend is clearly upward. The number of mergers is increasing steadily. The movement is not limited to

(1) Printers Ink Monthly, February, 1928.

(2) National advertising is said to be particularly guilty of affecting competition adversely. For a discussion on this point see "The Distribution Age", by Ralph Borsodi, Appleton, 1927. It might be argued however, that the same forces which are at work in retail or local markets are present when the market is wide-flung, --in fact, that the latter might be a closer approach to the economic "perfect market."

a small number of industries, but is general."(1) Many instances could be cited to corroborate this conclusion. In the food trade alone there has been a great trend toward concentration, as evidenced by the mergers of the manufacturers and also by the growing sales of a few retailing chains.(2)

To what extent can this concentration which has taken place in industry be attributable to advertising? One writer, after speaking of other motives which cause concentration, points out that "A further incentive, in certain industries has come from modern marketing methods, in which the concern which is large enough to undertake national advertising has definite advantage over its small rivals".(3) Truly there may be other more important factors than advertising lying behind the tendency towards mergers or the other forms of concentration, but advertising has at least played some small part.(4)

- (1) Thorp, Willard L., "The Changing Structure of Industry". Recent Economic Changes, National Bureau of Economic Research, page 217.
- (2) It has been said that "The sales of 27 grocery chains trebled in the period 1919 to 1926, while in the same period Kroger's sales multiplied five times." Professor W.C. Weidler, Ohio State University. Address at Associated Grocery Manufacturers of America Convention, November, 1929. It has also been estimated that the sales of the Great Atlantic and Pacific Tea Company in 1929 were equal to all other grocery chains put together.
- (3) Recent Economic Changes, page 217.
- (4) It probably should be pointed out here that some students of this problem believe that a merger of well-known advertised products could (Continued page 144)

What effect will such concentration have upon price?

In order for prices to approximate cost of production there must be freedom of competition. Any tendency for the sellers to gain a monopolistic control is apt to raise price above the competitive level. In order to approach a quasi-monopoly condition, however, there must be a very few sellers in the field, and the market for an otherwise homogeneous product must be divided into practically as many sub-markets as there are producers.(1) Now while it is true that advertising is a factor in strengthening the positions of the large producer, it must be remembered that it is a tool which the small producer can also use. Therefore, while advertising seems to allow the big producer to practically dominate the market, at the same time it sets up a counteracting influence in that it helps the small concerns to remain in business and perhaps furnish the needed competition. Especially is this the case

(4) not out down on its advertising expenditures. Hence advertising would hardly be an incentive in the creation of this type of combination. Further discussion of the effect of mergers upon advertising will be taken up in the next section. For information on these topics see article in Printers' Ink, Monthly, March, 1930, by Dean C.E. Griffin, University of Michigan.

(1) It ought to be pointed out here perhaps, that a "monopoly" of the production and sales of a trade-marked article is not what is usually meant by monopoly. In other words there is not apt to be any restraint of trade resulting from such a situation since other goods of the same character are available. Under true monopoly, the seller usually boosts price, but advertising is not apt to give the producer such power.

if the firms with limited sales band themselves together in trade associations and advertise jointly. The smallest competitors can sometimes break in and steal the strong man's grasp upon the market, by an intensive advertising campaign in one locality. For example a little bakery might find it possible to use advertising to get a foothold in his own community, at least, by advertising on a limited scale, even in the face of huge competitors. It is sometimes the little foxes that spoil the vines. Competition, therefore, may not be completely destroyed.

Although advertising may make the entrance of new competitors easier in some ways, it also erects barriers which may keep out competition for a time, since it not only takes a larger capital to advertise but it is also a more risky venture to start into a business which is already dominated by a huge concern. But the difficulties are not insurmountable and again and again new manufacturers come to the front who have the courage to enter the game.⁽¹⁾ In talking with an advertising man in Detroit recently, I learned that although there seemed to be a fairly good example of a quasi-monopolistic condition in the case of antiseptic mouth washes, he happened to know of a company making a similar product which was planning to step into the competitive area soon with

(1) A case in point is the success the Old Gold Company had in breaking into the cigarette business a few years ago.

a powerful advertising attack. His feeling was that although for the time being there might be a monopoly condition, in the long run competition would assert itself and advertising would be the open sesame to the market.

It might be contended that the small firms working singly or even through trade associations do not afford any effective competition for the giant producers. Even granting that, for the sake of argument, there is still reason to think that the big advertisers may not have undisputed sway over the market. Usually there is more than one giant in the field, if not in the same industry at least in some related line which might furnish some competition if prices got out of line. We have in such a case neither ordinary competitive conditions, nor yet a monopoly. What will be the effect upon prices? One argument is that with the fewer sellers, a closer approximation to the perfect market is attained. When the sellers are few there is a better chance to know the market conditions, and the prices which emerge are apt to be nearer the so-called right prices. The rejoinder might be that if advertising creates such concentration among producers, prices are apt to be higher because it is easier to effect at least a tacit

agreement to eliminate price competition.(1) It is difficult to measure just what the economic consequences of advertising may be in such cases; all that can be done is to point out what seem to be pertinent truths in the situation. In some industries like the automotive trade it is observable that although advertising has been accompanied with concentration, competition has not been eliminated nor have prices risen. On the other hand there are other industries, like the oil business, in which concentration seems to have interfered with competition.

Before leaving this discussion it would be well perhaps to point out that advertising has changed competition in another way -- it has raised the plane of competition. It has made business standards higher, for it has been impossible to do through the written page the kind of underhanded competitive practices which can be carried on by salesmen. Business men have been drawn together by their common interests

- (1) A recent article in the Quarterly Journal of Economics discussed this subject of price in the case of few sellers. The conclusions were as follows: "Unless the number of sellers is very large, it would seem that the consumer can rely for protection against monopoly prices only upon (a) the sellers' lack of intelligence, or (b) their having only a temporary stake in the market, or (c) their uncertainty as to what their rivals will do." The general thesis of the article seemed to be that these safeguards might not work, and that the price under "duopoly" is apt to be higher than the competitive price though lower than a monopoly price fixed to get the highest monopoly profit. "Duopoly: Value Where Sellers are Few" E.H. Chamberlin, The Quarterly Journal of Economics, November, 1929.

and "the old enmity of competition has withered up". (1) The disappearance of some of the predatory kind of competition, however will not affect prices adversely.

So far we have directed our attention to the problem of advertising's influence upon competition of the sellers. A word or two should now be added in regard to the effect of advertising upon the consumers' side of competition. (2) This phase of the subject is necessarily more limited than the discussion of supply, since the economist soon encounters in any analysis of demand, elements which are not susceptible of pecuniary measurements, and which consequently lie without his field. The alleged purpose of advertising is to furnish information about goods and services, hence ostensibly, at least, advertising might seem to be a help to the consumer. The argument would then be that competition was not hindered but aided by the selling activities of the producer. Such is not the case it seems, for advertising is said to be a disturbing element on the buyer's side of the market. Many are the criticisms that the kind of information that advertising supplies is a hindrance to consumers, causing an erratic type of buying

(1) Calkins, E.E., "Business the Civilizer", Little, Brown, and Company, 1928, page 281.

(2) The effect of advertising upon the consumer was discussed in the previous chapter, and needs only to be touched upon here.

which is far from that which is assumed in economic theory. Neither argument is capable of proof. The friends of advertising point out that any information even of a biased nature is better than ignorance; that the continual striving to reach the consumer with arguments designed to direct his buying tends to develop in him a better sense of values, --especially when the buyer arrives at the place where he discounts the overstatement made in the advertisements. However, as has been pointed out in a previous connection, this method of educating the consumer is very wasteful, absolutely speaking, and the criticisms directed against it seem more than justified.

In summary, therefore, there would seem no other conclusion possible than that advertising offers a dangerous interference with competition and hence may cause some unfavorable reactions upon price. It must be remembered, however, when this criticism is being made that advertising is in itself the result of competitive conditions. It is a tool of competition, a weapon evolved from a system of free initiative and *laissez-faire*, (1) and to criticize advertising is to criticize the present order. This fact suggests a different type of remedy than that sometimes offered, but the discussion

(1) As one writer points out, "Advertising is part of the mechanism of competition as well as of combination." Taussig, F.W., "Principles of Economics" Volume I, page 65.

of the future of advertising and sources of improvement we will postpone to the next chapter.

Thus far in this thesis we have made use of cost in the sense of entrepreneur's immediate money costs, or more simply the business man's cost of production as measured in money. There is, however, a more fundamental concept of cost, resource cost, which should be discussed since it determines the outward manifestation, money costs.(1) Resource cost is opportunity cost; it is that cost which society must bear in deciding to make certain uses of its limited factors of production. That is, the factors of production, land, labor, capital and business enterprise, are scarce, and decisions must be made as to their use, since it is impossible to satisfy all of our unlimited wants. Once a choice is made, however, we can say that there has been a sacrifice of some other possibility, the opportunity of having some other good or service. Advertising may have two influences upon this resource cost. First it tends to draw some of the factors of production into its own use, thus making it impossible to employ them in other ways; and second it tends to affect resource

(1) It is not my intention here to suggest any contrast between entrepreneur's cost and opportunity cost. This discussion of resource cost is designed to supplement our discussion of money cost, and to bring out certain aspects of the situation which are lost sight of in the analysis of the costs of entrepreneurs.

cost because it helps the consumer to decide what products he will purchase. These decisions determine what will be produced, in the main, and indirectly the allocation of the factors of production.

As far as the first point is concerned, there would seem to be no question that directing a billion and a half dollars into the work of publicity every year would limit the amount of other goods and services we can enjoy. Would we not have more economic goods to consume if the paper, lumber, paint, ink, the energy of the 600,000 men who work at this business, among which are some of the best brains of the country, were turned to other uses? Advocates of advertising maintain that using our resources for advertising does not cut down on the amount of goods and services mankind can make from its limited factors. That is, the amount of products derivable from a given amount of factors of production is a variable amount depending upon the productive efficiency with which they are used. Productive efficiency depends in turn upon certain conditions, the chief among which, as we have already pointed out, is the use of specialization. Advertising has made possible an increased use of large-scale production methods, for it widens the market which is the essential prerequisite of specialization in industry.(1) In fact, it

(1) The affect of advertising upon specialization or large-scale production methods was discussed in the section on production.

must not be forgotten that advertising itself is a form of specialization, a specialized way of performing one of the marketing functions.(1) Reasoning on this basis, therefore, the conclusion would be that advertising enhances the supply of economic goods in the world.

But not only has advertising used some of the limited factors of production for its own purposes and thus affected resource cost, but it has influenced their use in other directions as well. That the people of the United States spend \$117,000,000 a year on cosmetics for example, is the result of advertising at least in part.(2) The same thing could be said of a great many other commodities, namely that the demand has been largely stimulated by advertising; As a

- (1) The criticism is sometimes made that advertising has forced too high a degree of specialization into the marketing system. The retailer for example has become nothing more than a wrapper of packages. While there may be some drawbacks to such an outcome, they are probably not economic, since increased specialization tends to make for greater efficiency and lowered prices which in our present concern. A criticism much more to the point is that advertising is apt to bring about less specialization in some cases in that it encourages direct selling methods, eliminating some of the specialists of the market.
- (2) Chase, Stuart, and Schlink, F.J., "Your Money's Worth", MacMillian, 1927. page 21.

result of advertising, therefore, a different set of goods is being produced, and the resource or opportunity costs have been changed.(1) Whether the products which are produced are socially desirable ones is hardly a matter to be decided upon in a paper upon the incidence of advertising costs. All that can be done here is to point out that as a result of advertising a different set of goods has been produced, changing the resource or opportunity costs involved, and finally the prices of the goods which are brought and sold. A criticism of what advertising does to resource cost is really a criticism of the present economic system. If the outcome is unsatisfactory, the remedy should lie in a different guidance of production. We will now turn to a discussion of the advisability of some alternative scheme, and the possibilities of advertising exerting a better influence in the future.

- (1) A very good discussion of this point is to be found in an article referred to in a previous note. The following quotation is taken from this article:
"But, as it seems to me likely that the valuations arrived at by advertisement are less correct than those which would otherwise have obtained, I contend that the community loses in two ways. Firstly, by the production of a set of goods and services which are less adapted to its needs than those which would otherwise have been produced; and, secondly, by the diversion of resources to the production of reputation."
Braithwaite, Dorothea, "The Economic Effects of Advertisement", The Economic Journal, March, 1928, Volume 38, Number 149, page 26.

FUTURE OF ADVERTISING.

PART VI

An appraisal of advertising, based upon the analyses of the preceding chapters would probably lead to the conclusion that advertising in the main is an effective marketing mechanism, at least potentially. In many cases we have been able to show that advertising tends to lower the costs of production and marketing. Like other economic forces, however, it is handicapped by the waste and inefficiency which encumber all human activities. While some of the bad results coming from advertising may be due to unscientific, crude ways of using it; they may in part grow out of the inherent shortcomings of this selling agency. The first task of this chapter will be to investigate the factors at work in the present system which may improve the methods of using advertising. If such improvements do not promise to meet the difficulties, there is the further possibility of more governmental interference to be considered. That is, if the defects of advertising cannot be remedied by working along the lines we are now following, perhaps the state should step in. This interference might be of a minor sort, or might amount to complete control of advertising such as should be expected under socialism. The various

possibilities of governmental supervision will be briefly touched upon in an effort to determine the best solution of the advertising problem.

Before we enter the discussion of this chapter we ought first to define what is meant by "good" advertising. For example, before we can judge whether the different factors at work in the present system are improving advertising or not, we should have at least a general idea of what we expect advertising to accomplish. Advertising's main economic function is demand creation. From the standpoint of the advertiser this means increased sales, while from the social point of view it should mean a better-informed consumer and hence greater welfare. Assuming that there is a certain amount of selling work to be done, advertising in general is economically justifiable if it is able to do this work more efficiently than any other substitute agency. Moreover, one kind of advertising is better than another if it is able to accomplish this selling function with a relatively small use of our scarce productive factors. The various factors at work in the present system influencing advertising are good or bad, therefore, depending upon whether they increase or decrease the productive efficiency of advertising. Likewise governmental interference is justifiable to the degree it forces advertising to make better use of our resources. With this test in mind we will try to evaluate the influences affecting the future trend of

advertising.(1)

Our first task, then, will be to estimate the power of various forces at work in the present system tending to effect a better type of advertising. The stimulus for the improvement of advertising may come from within the advertising profession or from without it. That is, the users of advertising such as the merchants, producers and business men in general, as well as the sellers of advertising, the agencies and publishers, may strive to advance the standards of advertising. On the other hand some of the improvements may originate from without the fold -- may be due to the activities of the consumer; may develop from the work of the schools and universities of the country; or may be caused by the action of the government.

The truth-in-advertising movement is one indication of the attempt of the advertising men to improve their own industry.(2) This movement began to take definite shape just before the war period, although the struggle to make advertising more reliable and truthful probably dates back further than that time. In 1913 the advertisers' magazine, Printers' Ink formulated a Model Statute against misleading and dishonest

- (1) In this discussion we should keep in mind that any improvement effected in the use of advertising will tend to change the incidence of the cost of advertising
- (2) While the prime movers of such an activity have been the advertising men themselves, yet some stimulus has come from outside--for example from the Government as we shall point out later.

advertising, which marked the beginning of a crusade against the careless advertiser. In most of the states some such statute has been passed, under which any advertised statement which is untruthful, misleading or deceptive is illegal. These laws, however, have been more or less ineffectual in coping with this problem, and the success of the movement is due in the main to other measures. For example, during this same period the Associated Advertising Clubs of the World organized a National Vigilance Committee which in cooperation with what is known as "Better Business Bureaus" has been able to accomplish much more than the legislation. (1) The Better Business Bureaus are usually created by business men and represent an initiative on their part to clean their own doorsteps. These bureaus are now located in the principal cities of the country, their expressed purpose being "to make advertising accurate, to help newspapers and advertisers eliminate such

- (1) One writer has said on this point: "Only in extreme cases does the Better Business Bureau carry the matter to the courts. Quiet, steady pressure produces better results and gets the cooperation of the offenders themselves instead of their bitter antagonism. Court processes, moreover, are uncertain and tedious and costly; and in this connection the difficulty of securing real protection by legislation should be frankly stated." Moriarty, W.D, "Economics of Marketing and Advertising". Harpers, 1923, page 581.

practices which tend to destroy confidence."(1) While these bureaus are actively sponsoring sound business methods in general, some of their most important accomplishments come from their painstaking checking of all the advertising in their community. For example, each day the merchandising sections of the individual bureaus carefully check all newspaper advertisements. Suspected advertising items are referred to the shoppers of the bureau who make reports on each case, the advertiser being informed of the finding. In the cases where discrepancies between the description in the advertisements and the goods are found the merchants generally cooperate very willingly with the bureau in making corrections.

Business men have thus come to be their own taskmasters. Not only have they tried to eliminate outright untruths from advertising, but they have gone further in attempting to correct superlative statements, exaggerated, exuberant "puffery", which tends to do as much to alienate public confidence as absolute dishonesty. The following quotation is indicative of this trend towards better advertising: "We are not concerned with the kind of dishonesty that can be haled into court, or stopped by a fraud order. The cruder forms of dishonesty take care of themselves. I am suggesting honesty

(1) "Buying with Safety in a Complex Market", Pamphlet by the Chicago Better Business Bureau.

as an ingredient of advertising to make it more believable..... It is a peculiarity of this writing trade that a thing to sound true must be true. Honesty in advertising has a definite dollar and cents value in business." (1) It is true that advertising which is not strictly honest may for a while be successful in creating demand, because "some vague impression of superiority is produced by the incessant boasting". (2) A great many advertisers, however, have come to believe that truthful, straightforward publicity though perhaps slow to get demand started, will in the long run bring steadier sales. If there are only a few products to be sold the owner can probably make more profitable sales by chicanery; but if there are thousands of sales to be made every year and the bulk of them to old customers the advertising must be not only truthful---it must be 'believable'.

Let us now summarize the effects of the truth-in-advertising movement. In the first place there has been a distinct change, an improvement, in the kind of copy used.(3)

- (1) "Advertising and Selling" February 9, 1927. For another article in the same vein see Printers' Ink, December 17, 1925.
- (2) Taussig, F.W., Principles of Economics, Volume II, page 450.
- (3) Mr. R.S. Dustine in his book "Making Advertising and Making it Pay" says "With the disappearance of superlatives from copy has come a demand for quiet, convincing argument". Page 246.

Furthermore requiring the strict truth may tend to reduce the total amount spent upon advertising, since some kinds of advertising would be eliminated.(1) There is finally the social effect of this movement to consider. Has there been a resulting increase in the efficiency of advertising? Are we making a better use of our economics and social resources because of truth-in-advertising? Insofar as truthful advertising develops a better informed demand the presumption is that better guidance of production will follow. It is probably safe to conclude therefore that this movement does show some net social gain. It tends through education of the buyer to direct production away from fraudulent enterprise and into socially desirable channels.

A second reason why the advertising of the future may be better is that the men and women who are creating it are becoming more and more expert. The practice is growing among business houses either to place their advertising with an agency or to establish a department of their own. In either case the sales publicity of the business receives the attention of specialists and is apt to be more effective than under former conditions where the owner or some department head planned the campaigns in his spare time. It is estimated that there are about 1,500 agencies and that 500 of the

(1) On the other hand it might be argued that making advertising more truthful makes it more effective. Hence business men may make increased use of this selling agency.

leading organizations handle 75% of the business. A still smaller number, 133, which are members of the American Association of Advertising Agencies handle about 5,000 accounts and place around \$300,000,000 a year.(1) All told it is said that the agencies of the entire country are preparing and placing fully 90% of all advertising, except retail.(2) A great deal of the retail advertising, moreover, is produced in highly organized advertising departments.

How can we reason that such a trend will make for better advertising? In the first place the success of any work usually depends upon the workers. It is noticeable that the advertising profession is drawing into its different lines of work some of the best talent of the country. While it is important that the men who prepare the advertising should be skillful and intelligent, it is more important that they should use the right methods; that they should help business men to plan their advertising work with something more in mind than the success of the moment. Some factors in the situation make the professional advertising men and women especially capable

- (1) Crain, Jr. G.D. The Market Data Book, 1928, 537 S. Dearborn Street, Chicago. A survey by the Ad-craft Club in Detroit, Michigan showed that the agencies in that city handled accounts amounting to 50 to 60 millions.
- (2) Calkins, E.E., "Reading with a Purpose: Advertising", American Library Association, 1929, page 18.

of directing advertising policies, but in other ways they are handicapped. Of the former might be mentioned the fact that advertising agencies have turned to marketing research for help.(1) To the degree that they can get the facts about markets; to the extent they can measure the results of their advertising; and insofar as they are able to base their recommendations to business men upon the foundation of scientific knowledge, advertising may lose some of its present fancifulness and waste. Advertising which is based upon guess work not only loses in effectiveness by being poorly executed, but also because it is apt to create skepticism and distrust in the minds of the reader. Sometimes the cry is made that advertising is not and never can be a science; that advertising money can never be spent with assurance. Others, more hopeful, believe that there are decided possibilities of measuring and controlling the results of advertising. Even now there are some types of advertising, the results of which

- (1) It is true that the advertising agencies have in many cases discontinued their research departments which were so flourishing in the war boom. Perhaps the smaller amount that is being done is of a higher caliber; moreover they may be making more use of research carried on by the government and other agencies. There have also been attempts made by the advertising men of the country to carry on joint research. A recent prospectus issued by the Bureau of Research and Education of the International Advertising Association outlines several projects to be carried out in the next few years. It is felt that the uncertainties of advertising can be "removed by research". The task they set themselves is a large one and may never be accomplished, but the work ought to net the advertising profession some gain.

are considered measurable. Returns from mail order publicity, direct mail advertising, and "keyed" advertisements in general can be definitely checked. Using these types as a sort of testing ground for the effectiveness of certain appeals, for trying out new ideas, more may be learned of the so-called unscientific varieties of advertising. The following expresses the faith of some advertising men in their profession; "Adequate preliminary tests will so establish the value of a good advertisement that its owner may thereafter spend millions on it with perfect confidence."(1) While this is probably over-optimism in regard to the possibilities of measuring advertising results, yet we must not lose sight of the fact that any progress toward this goal is making advertising more dependable. The advertising specialists are interested in this development and we may look to them to correct some of the faults of present-day advertising which have been due to lack of knowledge and to poor workmanship.

There is one factor however, which may retard this advancement. The manner of paying the advertising agencies for their services has served as a stumbling block to improvement. An agency buys art work, engravings, white space, for its clients, and for the service rendered is paid a commission of fifteen per cent on the total amount spent by the

(1) Goode, K.M., and Powel, H., "What About Advertising", Harpers, 1927, page 90.

advertiser. Criticism has been made that such an arrangement tends to make the agency over-sell advertisers, urging them to spend more than they should. This might be improved by changing the payment to a flat rate basis. For example if an agency were paid \$10,000 to put on a certain campaign, rather than a 15% commission of an amount to be determined at least in part by the agency, there might be a more conservative use of advertising money and hence a better use of our productive resources.(1)

A third source of improvement from within may come from the publishers who, for their own self-interest, may attempt to raise the standards of advertising. They are not of course interested in cutting down the total advertising expenditures, but they are necessarily concerned with the general success of paid-for publicity as a marketing agency. Publishers as a whole are dependent upon the advertisers for financial support and if the public loses confidence in advertising they have a great deal to lose. Just what effect

- (1) The change from one basis of payment to another, although an improvement in the end, might in the meantime cause terrific out-throat competition, according to the opinion of some advertising agencies. Many feel, however, that the change will have to come. But the publishers have the whip hand and do not relish the idea of passing through a period of stress until they are forced to do so through pressure from the agencies or from the big advertisers, who come to feel there is not the correlation that there should be between what they spend and the results they get.

publishers have had in raising the standards of advertising is hard to determine. We do know that some publications have formulated definite policies about what kind of advertisements are acceptable for their columns. It is said that the New York Times, for example, rejects several million dollars' worth of business annually. Likewise some magazines exercise a very strict censorship, carefully scrutinizing all advertisements which come to them.(1) Some of them maintain laboratories in which they test the claims of the advertisers,

- (1) The following statement was received from the Curtis Publishing Company regarding their censorship. "Our censorship has four principal objectives:
 - (1) To meet the United States Postal Regulations and to make certain no advertisement violates their regulation concerning the use of the United States flag or in any other respect.
 - (2) To protect our readers against exploitation through the sale of products without merit or making claims for products that are unwarranted.
 - (3) To make our publications pleasing to read by omitting the advertising of any products which might be offensive to our readers, or use of any art or copy which might prove offensive, or use of type or layout which might spoil the harmonious appearance of our publications.
 - (4) To keep our publications a fair forum in which manufacturers may constructively promote their wares without unfair destructive copy from others. Doubtless this policy maintained for many years in Curtis Publications has lifted the standard of advertising in our publications and, I think it would be fair to say, has been a helpful factor in improving the general status of advertising."

and once accepted they guarantee the truth of the statements. The trade publications in particular have upheld the standards of advertising. One writer commenting upon the reliability of trade publicity says. "In other words their subscribers take it for granted that the publishers accept advertisements only from responsible concerns. Their readers look to them for information concerning new inventions and processes, new appliances and machinery that will reduce production costs, etc. The advertising columns are therefore, closely read because it is often the only way they can keep track of these things". (1)

Just as the advertising agencies have turned to market analysis to help them solve their problems, so we find the publishers making efforts in various directions to put their advertising work upon a firmer foundation. For instance, the Audit Bureau of Circulations established by the publishers in 1914 is an example of self-regulation -- an attempt to improve the effectiveness of advertising. Furthermore, some of the newspapers have established merchandising departments. The research work carried on by these departments is generally of an inferior nature designed chiefly to

(1) "Facts Worth Knowing about Advertising Mediums," National Advertising Committee of the Associated Advertising Clubs of the World, 1926.

show merchants and manufacturers why they should use their mediums, yet this is a start on the right methods and indicates some willingness to get at the facts.(1) Thus the press may through its censorship policies, its testing laboratories, its attempts at market research help to eliminate some of advertising 's waste and inefficiency.(2)

Thus far the analysis has dealt with the improvements which result from the self-corrective forces in advertising. We must also comment upon the advancement which may come because of outside pressure or development. The first factor of this nature which we will consider will be the influence upon advertising standards resulting from the research activities and the educational work of the schools and universities. In the first place there is a large amount of research work being carried on by the various educational institutions throughout the country.(3) While much of this work applies to general

- (1) To be sure some of the research work of the publishers appears to be above reproach. For example, a pamphlet issued by the Meredith Publishing Company on "Standards of Research" outlines a very high set of standards for their market analyses.
- (2) A question of some social significance, but not bearing directly upon the economic aspects of advertising, is the problem of the poisoning of the news by the influence of the heavy advertisers. It has been argued that the selfish interests of such advertisers prevent serious results in this direction since they tend to offset each other.
- (3) The "Market Research Agencies" issued by the United States Department of Commerce lists some several hundred studies (either completed or in progress) of colleges and universities.

marketing problems, there is apt to be some reaction upon advertising methods. In addition to the research carried on by the schools, there is the training of the students along certain lines which may help to correct some of the faults of advertising. For instance there are technical courses which deal primarily with advertising such as the psychology of advertising, advertising typography, the writing of advertising copy.(1) While it is true that such special education may give students some knowledge of the technique of advertising, the more general subjects of business administration and economics, giving a wider understanding of the larger aspects of advertising and business may do more in the end to raise the standards of advertising. While there is no doubt that educational development may reach and influence advertising through the channels mentioned above, it is probably true that education's effect upon the consumer will be much more potent a measure in forcing development in the use of advertising.

The consumers attitude indeed may be considered a second source of external pressure upon advertising. Many students are of the opinion that the improvement of advertising

- (1) In some institutions a course in technology of commerce is becoming part of the curriculum. The syllabus used in such a course given at the University of Chicago, School of Commerce and Administration came to my hands recently. Part of the work outlined deals with the characteristics of goods in view of their selling possibilities, -- investigations which ought to be conducive to more effective advertising.

will come largely because of the demands of consumers.(1)

"When better advertising is made the people will make it," someone has paraphrased, adding that "When the people thru the force of changing pressure begin to resent what is false only then will manufacturer and distributor find it financially possible to adjust their policies to the levels thus established" (2) The buyer in a way is responsible for the production and marketing methods which are used. An intelligent buyer, one who is awake to his own self-interest should discriminate in favor of methods which further his own ends. If certain types of advertising are wasteful and tend to increase prices, the consumer by proper action on his part can soon put a stop to the wasteful practices. It is true that this is far from the role taken by the consumer at the present time.(3) He appears to be at the beck and call of the advertiser, so that instead of his exercising control over production, advertising included, the producer performs this function.

What are the signs of the time which might lead support to the hope that consumers will regulate advertising

- (1) For a discussion in this vein see Chase, Stuart, and Schlink, F.H., "Your Money's Worth", pages 229 ff, and 251 ff.
- (2) Printers' Ink Monthly, May, 1928.
- (3) Professor W.D.Moriarty in his book "Economics of Marketing and Advertising" says that, "The weakest point in the system of regulation by competition is the lack of intelligent cooperation on the part of the consumer." page 582.

in the future to their own ends? An article in a recent issue of a weekly survey of food merchandising brought out the point that the buyers are beginning to control the distribution process because "the consumer today is doing an unreasonable measure of shopping." While the manufacturers and merchants may not like this "control from above" it is a healthy condition from the standpoint of society. As a result there has been price and quality competition in the field of food marketing, as is clearly evidence by the retail grocery advertising. From an entirely different source we get the following comment regarding the consumer's influence upon advertising: "Successful advertisers are becoming increasingly aware that the use of bombastic propaganda, bluff and psychologically enticing, will no longer suffice. On the contrary, it is apparent that the consumers are coming to demand scientific marketing of goods. They will demand, before buying, to be told exactly, and, if possible, quantitatively, all the valuable components of a commodity." (1) This may be an over-statement of the position and power the consumer has in the market. As he becomes more intelligent and well-informed, however, we may expect better cooperation from him in the performance of his economic function. While we might depend upon the native ability of the consumer and his general education to teach him

(1) A quotation from the syllabus referred to above for the course in "Technology of Commerce", 1927-28. University of Chicago, School of Commerce and Administration, by Joseph Schneider.

the intricacies of spending his money properly, yet many people feel that he should be supplied with definite unbiased information to guide his buying. The government might be considered the logical agency to furnish such data, (1) but so far it has not seen fit to do very much along this line. What has been done is of interest, however, and will be examined presently. But before we turn to this discussion, a brief mention of some of the recent developments in advertising might serve to round out our analysis of the future of advertising.

Among these newer trends may be mentioned radio advertising, testimonial advertising, institutional publicity, cooperative advertising, and finally the effect of resale price maintenance upon the future of advertising. The first among these, the advertising over the radio, represents in some ways a tendency towards a better type of publicity. This grows out of the fact that radio advertising may be largely of a cooperative nature in the future. In the first place, if there is to be an increasing use of this medium, advertisers may have to cooperate because of the time and station limitations. Furthermore, this type of publicity is often

- (1) An attempt by private initiative to meet this need is instanced by the so-called "Consumers" Club" which was formed a few years ago by Stuart Chase and F. J. Schlink. The purpose of the organization is, "to supply for its members on request expert opinion about some of the articles of everyday life." The name was changed to Consumers' Research Corporation ^{Inc.} in 1930. Address: 47 Charles Street, New York City, New York.

considered more successful and effective when done jointly.(1) As a result companies within a given industry may join forces to make the best use of this selling tool. "Competitive" advertising would give way to commodity advertising -- undue boasting and pushing of particular brands, unfair references to competitors, would be replaced with a more informative, educational, truthful type of advertising.(2) Such changes it would appear, would be in line with progress. One of the chief criticisms of advertising is that it utilizes resources in a way that brings no net social gain. One concern's advertising is neutralized by his competitor's, each maintaining the same relative position in the field with no increased market; and lowered marketing or production cost to justify the added cost of advertising. If less energy is spent on this type of advertising, and more on the kind in which manufacturers are cooperating, we might have a better use of

- (1) One writer makes the following comment upon this point: "For example fairs and exhibitions to which the public is invited are invariably more popular in their appeal, the wider the representation of the various factors in the trade. Motion pictures and the radio stand in a similar position" "TRADE Associations: Their Economic Significance and Legal Status" National Industrial Conference Board, 1925. page 241.
- (2) Insofar as we have higher standards in radio advertising, it may be partly attributable to the censorship exercised by the broadcasting stations. It is said, for example, that some of the stations refused to accept the Lucky Strike hour.

our productive factors.

Moreover, it might appear that joint radio advertising could be justified on economic grounds because it serves to educate the consumer, thereby making him a better informed buyer. There is, however, some reason to think that radio advertising is not a very effective educational medium. The fact that the radio listener can so easily cut off any objectionable advertising has tended to reduce the advertiser's sales appeal to little more than a mere mention of his product antecedent or subsequent to a program of entertainment.(1) Such advertisements while truthful and harmless perhaps, may yet fall short of meeting the test of good advertising. It is true that one mark of good advertising is to be able to accomplish a relatively large amount of selling work with a small use of productive factors. It is probable that radio advertising has accomplished that for some producers, although it would be a difficult matter to prove at the present time. Insofar as radio advertising proves to be a highly efficient medium for building up sales, and to the degree that it tends

- (1) In making a comparison of the effectiveness of radio advertising and magazine and newspaper publicity one writer points out that the "publisher often sandwiches in the advertisements with the news matter or articles" and although the reader attempts to disregard them, "they are still on the sidelines, beckoning to his subconscious mind." The radio advertisement has no such opportunity when it is tuned out. Jome, H.L, "Economics of the Radio Industry," A.W.Shaw Company, 1925, page 284.

to displace other less effective methods it should be said that the change is socially desirable. However, from another standpoint radio advertising may not be commendable. Since a great deal of it is mere iteration of slogans and names of products, it may not meet our criterion of increasing consumer information. May it not be argued that a type of advertising suffering such a handicap is socially undesirable? The answer of course must be qualified by the nature of the product and by other factors which it is impossible to measure at the present time. The whole subject of radio advertising is too novel to permit of any very definite conclusions as yet.

A second of the newer types of advertising worthy of mention in passing because of its contemporary interest, is paid testimonial advertising. This method of appeal to the public has been severely criticized of late; even the advertising fraternity itself has frowned upon its development. (1) It is maintained that such publicity when carried too far tends to destroy public confidence, and, although it may be

- (1) One reputable advertising agency in Detroit informed me that most of the agencies of the country were fighting this fad in advertisements, and that only four of the larger organizations were holding out for it. A recent article in "Fortune" on "Good Taste in Advertising" criticizes "stunt advertising", testimonials included. March, 1930.

temporarily successful in developing new increments of demand, in the end the effectiveness of advertising as a selling medium is impaired. This does not mean that testimonials have no legitimate place in advertising copy. They have been used in the past with good results and with some modifications will probably continue to be employed.(1) Just recently the Federal Trade Commission issued a cease and desist order regarding the paid testimonials appearing in the advertisements of a tobacco corporation. The company has agreed not to use testimonials and endorsements unless they represent and are the genuine, authorized, and unbiased opinions of their author or authors. If the testimonials have been paid for, this fact should appear in a conspicuous place in the advertisement. Such regulations ought to eliminate some of the worst manifestations of this type of advertising.

A third kind of publicity, about which relatively little criticism is heard, is institutional advertising. When attempted by trade associations on a cooperative basis this type is generally of a very high standard. Even when carried

- (1) A defense of testimonial advertising can be found in the April, 1929 issue of the J. Walter Thompson Company's Bulletin in an article by Stanley Resor, entitled "Personalities and the Public". The author feels that "sincere testimonial advertisements will not lessen the reader's belief in all advertising.

on by individual companies it has been unusually free from the defects of other kinds of advertising. Ordinarily it is more truthful and informative,⁽¹⁾ with less boasting and pushing of individual brands. This may be good advertising from the standpoint of consumer information, but on the other hand some question might arise as to its value in selling goods. For example such advertising as that done by Metropolitan Life Insurance Company, while perhaps of some educational value to the community, may be wasteful. The main function of advertising should be to sell goods, and incidentally to give correct information to the consumers to guide their buying. It is a question whether money spent for institutional advertising is as effective as more direct expenditures to build up sales. The returns seem even more immeasurable than those of ordinary advertising, and it is easy to see that some firms might be induced to spend altogether too much in this direction with the vague hope that some undefinable benefit may accrue to their

(1) References to the education^{al} effect of institutional campaigns are often made by writers. For example one author points out that the advertising of General Electric Company and the American Telephone and Telegraph Company has spread the use of mechanical power and labor-saving devices in United States. Vaile, R.S., "Economics of Advertising", Ronald Press, 1927, page 64.

business.(1) From the standpoint of the individual business man and for society it might be better if resources were spent otherwise.

There are certain conditions, however, in which it appears justifiable to use institutional advertising. For example in the case of public utilities there is often need to employ advertising as a defense against adverse public opinion.

(2) If such advertising does not degenerate into pernicious propaganda, it can be defended on economic grounds even if it does not sell merchandise directly. Institutional advertising may also be employed in lines in which there has been a great deal of standardization and simplification. This probably accounts for the type of advertising utilized by the General Electric and Western Electric Company. Furthermore, the

(1) Mr. R.S. Dustine in his book "Making Advertisements and Making them Pay", says "An institution advertiser has no - - immediate evidence of his advertising's power. He must have faith sometimes for years until some day a test comes and he finds that his investment has rolled up for him a mass of goodwill behind his trade mark which can be destroyed neither by disaster or competition." Such "Faith" might lead to an over-investment in this type of advertising.

(2) A case in point is the institutional advertising of the Canadian Pacific Railroad. In describing the advertising policies of the company, a writer makes the following comment regarding institutional advertising: "It has been especially successful in combating violent prejudices against "big business" and in rehabilitating in public favor organizations which have found themselves pilloried for no other crime than that of being successful". "When Can a Company Stop Advertising" Printers' Ink Monthly, January, 1925.

large business units which have been formed as the result of the recent mergers may find it advisable to use institutional advertising. Combinations in industry may lead to an increased use of this type of publicity when the products brought together are of such a nature that separate advertising must be continued for each of them. Over and above this individual product advertising, general publicity for the whole group may be necessary. The effect of mergers upon advertising has been discussed in a recent article appearing in Printers' Ink Monthly in which the writer comes to the following conclusions which are of interest to us at this point: "It appears, then, that the answer to our question of the probable effect upon advertising of the recent mergers in the food industry is that advertising of the specific brands will or should continue without any abatement and that in addition, an opportunity is offered for institutional advertising to present the mergers to the public in a favorable light and to gain the reciprocal effect of the support which the several products can give to one another and to any new products which may be offered by the new companies. The mergers may effect economies in advertising, but if so the economies will probably take the form of more effective advertising rather than less of it". (1) The conclusion of this discussion must be that

(1) Griffin, C.E., Dean, "What Will the Mergers Do With Advertising" Printers' Ink Monthly, March 1930.

institutional advertising fulfills a definite need in business. Although it is practically impossible to measure its results in terms of sales it probably is defensible on economic grounds. At least, its truthfulness, its educational attempts, its freedom from "brand" competition, are points in its favor.

A fourth development in advertising which may help to set the standards of the future, is cooperative advertising. This movement among business men to join forces in their sales efforts is nothing novel, however, for many of the successful cooperative campaigns started years ago.(1) However, there has been a very rapid growth in the last few years which may make this type of advertising increasingly important.(2) This is significant because an examination of association advertising shows that it is free from many of the faults of other kinds of advertising.

In the first place it seems to be economical, -- to be able to accomplish a great deal with relatively little cost.

- (1) A great many of the cooperative accounts appeared for the first time in the period between 1918-1922, although a few of them, such as the Southern Cypress Manufacturers' Association and the California Fruit Growers Exchange date from 1913 or 1914. Agnew, Hugh E., "Cooperative Advertising by Competitors" Harpers, 1926, page 24.
- (2) It has been estimated that "In 1928 there were over 150 associations doing national advertising on a fairly large scale -- spending nearly twice as much in magazines as during the previous year!" "Association Advertising" by Henry Legler, The J. Walter Thompson News Bulletin, April, 1929.

The cost of a great deal of cooperative advertising, averages well under one percent of total sales. In the "Save the Surface and You Save All" campaign, for example, carried on by the paint and varnish manufacturers since 1919 the cost has been around 1/8 to 1% of gross sales. It is reported that this expenditure has been accompanied by a one hundred percent increase in the consumption of paint and varnishes. Some cooperative campaigns, however, have cost the producers a great deal more, but the increase is usually due to the fact that they have attempted other joint activities.(1)

But even aside from the low cost involved, cooperative advertising has many advantages. Association advertising has been very successful as a medium for joint educational campaigns. Some of these projects would not be feasible nor effective as individual attempts. For example it has been suggested that "shoe manufacturers could enlighten consumers about the cost of following fashion and the economies of using staples, so that there would no longer be any confusion in the public mind

- (1) For example it has been said that "Over a period of several years, the advertising and sales expense of the California Fruit Growers' Exchange has been 2.82%. That includes a very efficient corps of salesmen, extensive telegraphic reports, a large amount of developmental work with the dealers and all the advertising". Success Bulletin, January 15, 1925. For the size of expenditures of representative Associations see the material in "Cooperative Advertising by Competitors" by H.E. Agnew, Harpers, 1926, pages 23, 25.

about the necessity of paying for their style whimsies."(1) This might be highly desirable from the standpoint of both the consumers and the producers, but it would be suicidal for any one firm to attempt such a program. Another reason why advertising done cooperatively tends to have greater merit is that it is based upon a better foundation of experience and investigation. A cooperative campaign being the product of the experience of a group of business men rather than one, superior results should not be surprising. At least there should be less exaggeration, and less "puffing" of individual wares. Furthermore, we might rightly expect better results from association advertising because the trade associations are exceptionally well-fitted to carry on effective market research. An individual business must be fairly large to do much with this work; but, grouped together, even the smallest firms who are willing to pool resources and information can support rather extensive projects of such a character.(2) The advantages of cooperative advertising are well brought out in the following quotation: "Joint advertising campaigns seek

)1) Cherington, T., "The Consumer Looks at Advertising", Harpers, 1928, page 26.

(2) One advantage of cooperative advertising, mentioned in a previous connection, is that it has enabled many small concerns to stay in business which otherwise might have been squeezed out. Competition may thus be maintained to the advantage of society.

to stimulate demand for the product of the group, in competition with alternative products by combating unfounded prejudices, by directing attention to new uses, by extending publicity to large market areas for the output of small and scattered producers. Such publicity is relatively free of the notorious wastes of usual competitive advertising; it aims to promote the common interests of common groups".(1)

While advertising of this nature has many praiseworthy aspects, there may be some drawbacks. In the first place it may tend to foster demand for products which are socially undesirable. By concentrating upon the sale of one type of product, the cooperators may be successful in excluding from the market another product which may be better in many respects. Again, a foolish use of our resources may very well be stimulated by powerful cooperative advertising; we may be induced, for instance, to demand a fancier grade of product than should be used in view of our scarce resources. The very strength of its educational possibilities which has been previously noted may be a danger from this point of view. It may offer too potent an influence upon the allocation of our productive factors, or too great an interference with the consumer's guidance of production.

(1) The American Economic Review, Supplement, March, 1926. "The Trade Association Movement" by I.L.Sharfman, University of Michigan. pages 206-7.

A further criticism of cooperative advertising calls into question its effectiveness as a selling agency. It must of necessity be more general in its appeal than many other types and consequently may fail to bring in the business that individual advertisements which concentrate on particular selling points of certain products might achieve. Experience of many associations, however, show that their joint efforts in advertising have been very successful in building up sales and that too, as we have already seen, at a very low cost. It nevertheless, might be thought that such advertising is wasteful since it duplicates the advertising done by individuals, thereby increasing the total spent on advertising without accomplishing more. It is true that oftentimes the leading companies in a trade have not joined the cooperative advertising schemes; hence they continue their individual advertising--perhaps with increased vigor if the new competition from the association is powerful. Moreover, even for the cooperating firms, the joint advertising rarely supplants the individual advertising efforts.(1) In fact, association advertising often stimulates the member firms to do more advertising than before. As a result of these general factors the total spent on advertising may be larger. Whether such an outcome is

(1) It is true that some associations, like the California Fruit Growers Association, handle all the publicity for the individual members.

desirable or not depends upon the results obtained by the increased expenditures. The mere fact that cooperative advertising has tended to increase the amount spent for advertising would not be prima facia evidence that this was a wasteful type of publicity. It all depends upon the social and individual economic consequences. These, however, are such as to justify the conclusion that, in spite of some drawbacks, cooperative advertising is one of the best types of publicity. If so, an increased expenditure in this direction cannot be condemned.

To the extent that business men become more alert to the nature of inter-industrial competition we may expect them to turn more and more to joint advertising efforts. That is, as producers in one industry begin to see that real competition is coming from producers in allied and even unrelated fields, they are apt to band together in trade associations and present a unified front through cooperative advertising.(1) Another factor which may cause more cooperative advertising is the recent tendency towards mergers in industry. The small Business

(1) Sometimes this is referred to as "commodity" competition in terms which would imply that there was a new force in the market. It is a mistake to think that there is anything new about such competition, for commodities always have competed with each other for a share of the consumer's income. All that has happened is that producers have become more awake to this condition.

houses may find it necessary to do joint advertising to meet this new competition.(1) While there are certain factors which seem to favor the growth of cooperative advertising, it must be remembered that there are some industries which will gain more from such publicity than others.(2) It follows, therefore, that while the present extent of joint advertising may be satisfactory it would probably be a mistake to use it to the complete exclusion of other types; but there is little danger of such an occurrence as long as we have the present type of competitive production. There is, however, every likelihood that there will be some increased expenditures in this direction.(3) Incidentally it might be pointed out that the government will probably offer no interference with such a

- (1) For a discussion of this point see an article entitled "Do Mergers Mean More Cooperative Advertising" in *Printers' Ink*, March 8, 1928. "That more mergers mean more cooperative advertising campaigns cannot be escaped in any thorough analysis of the trade association and the merger," is the conclusion reached in this analysis.
- (2) The "principal avenues for joint publicity undertakings" are analyzed in "Trade Association: Their Economic Significance and Legal Status" by the National Industrial Conference Board. page 237-241.
- (3) A student of cooperative advertising in a book already referred to, has pointed out that "On the whole, it seems that cooperative advertising will rapidly increase in the future both in the number of accounts and in the amount of educational work that the different industries will undertake." Agnew, Hugh E., "Cooperative Advertising by Competitors", Harpers, 1926, pages 231-2.

trend. In one of the decisions of the Supreme Court in a case involving a trade association it was stated that "The defendants have engaged in many activities to which no exception is taken by the Government and which are admittedly beneficial to the industry and to consumers; such as cooperative advertising and the standardization and improvement of its products." (1)

Thus far in this section we have been attempting to see if the problems of advertising can be solved by a laissez-faire policy. That is, whether the evils of advertising will be remedied by the natural forces at work -- for example through the self-interest of the consumers and the producers, through the activities of interested parties both within and without the advertising field. With this in mind we have investigated the different sources of improvement within the present situation, and have reviewed the various types of advertising which seem to be significant today. Although we have found many promising developments, it may be questioned whether better results might not be obtained by direct governmental interference. It will be the purpose of the following discussion to investigate the part the government may take in solving the problems of advertising.

The influence of government upon advertising depends upon the position the government may assume in the regulation

(1) Ibid, page viii.

of business in general. There are several alternative roles that may be considered but let us examine the existing situation as a point of departure. At present the government is carrying on certain activities which may be considered beneficial to the advertising industry. Some of these activities make for improvement through the influence they exert upon the advertising standards of the producer. Others tend to achieve the same results through the education of the consumer. Among the former may be mentioned first the statutes of the federal, state and municipal governments forbidding certain unsatisfactory practices. For example, the Federal Pure Food and Drug Act prohibits advertising of a deceptive character regarding the materials used in the manufacture of foods and drugs. Again, as has been mentioned before, certain state laws have made misleading and untruthful advertising illegal. Moreover, the Federal Trade Commission has exercised quite a degree of censorship over advertising,(1) and its investigations leading to an occasional cease and desist order have eliminated some misrepresentation and fraud. The Commission has been powerless, of course, to check exaggeration and "puffery". Other agencies than the government must be depended upon to purify advertising of such faults.

(1) A brief discussion of the work of the Federal Trade Commission and advertising is to be found in *Printers' Ink*, May 3, 1926.

Although much has been accomplished by the government through direct regulation, more has probably been done by a second group of activities, namely those which involve helping and encouraging business to discipline itself. One such activity has been that of the Trade Practice Conference. A trade practice conference has been described as a "means through which representatives of any industry voluntarily assemble under auspices of the commission (The Federal Trade Commission) for the purpose of considering unfair practices in their industry and collectively agreeing upon and providing for their abandonment."(1) Some sixty or seventy conferences have been held since the institution of the work in 1919. Most of these conferences have formulated and adopted resolutions which have eliminated many questionable practices pertaining to their industries. Some of the agreements have direct reference to advertising and in almost every submittal there were rules which would affect the standards of advertising somewhat. For example in one case part of the agreement stated; "Advertising should be at all times fair and honest. It is not discreditable to become enthusiastic in print about the goods you offer for sales, but to imply that your neighbor is not selling good productsshould not be permitted because we consider it an

(1) "Trade Practice Conferences" Federal Trade Commission pamphlet, July 1, 1929.

unfair method of competition.(1) Another trade practice conference held by the correspondence schools of the country adopted resolutions which dealt almost entirely with ways and means of advertising. Untruthful, misleading advertisements were scored and even the use of superlatives was condemned.(2)

In order to illustrate further the influence the government may exert upon advertising under the present system, it might be well here to digress a moment with a brief mention of the effect of the government's stand in the resale price maintenance controversy. All the manufacturers' attempts to legalize the fixing of retail prices have failed, at least in all the forms that have thus far been attempted. As a result it is probable that national advertising, will stress price less and less.(3) The argument is that if a manufacturer spends money on advertising a price, he plays into the hands of the cut-rate retailers who will use his product as a "leader". The consumer then may come to think that either the article

(1) Ibid, p. 22.

(2) Ibid, pages 64-70.

(3) The position of the government in the resale price maintenance problem has had little effect upon retail advertising. To some extent it might lead to the featuring of cut prices on nationally advertised goods, but the chief effect will be found in the national advertising of the producers. If they are no longer able to dictate the retail price, the manufacturers may feel dubious about stressing prices.

has been over-priced by the manufacturer or that its quality is inferior. The good-will of the advertisers is thus converted into ill-will. Consequently the advertiser is apt to avoid the mention of price. Does this make advertising less effective or less useful as a selling agency? In a past connection it has been remarked that advertising should, in order to be in keeping with the present order, further and develop quality and price competition. From such a basis, it might be reasoned that the government's action in the question of resale price standardization has had a bad effect upon advertising. Whether it tends to have this result or not depends upon how the price appeal has been used. It may be that advertising may not need to stress price to fulfill its economic functions.

From the standpoint of consumer information it is probably desirable for advertisements to emphasize price. Even if the goods are not sold on the market at the prices advertised, the buyers are given a better basis for judging the worth of the goods. It has been pointed out that, "So far as aids to proper consumer guidance are concerned, price cutting on standard nationally advertised goods does supply a condition more favorable to the consumer than price advertisements on other goods" (1) Yet when the price appeal is incorporated into advertisements there may be danger that the

(1) Moriarty, W.D., "Economics of Marketing and Advertising". Harpers, 1923, page 451.

advertisers will use the latent powers of advertising to support too high prices. So much publicity may be given to a certain price that the consumer comes to over-valuate the commodity. As we have mentioned before business men often look upon advertising as a medium for "lifting their products out of price competition". Likewise many consumers are of the opinion that advertising raises price. A study of resale price maintenance made by the Federal Trade Commission in 1929 collected some information relative to the consumer's attitude on the prices of advertised goods. Questionnaires were sent out to a number of consumers. One question asked was: "Do you regard branding or trade-marking and widespread advertising of goods as affording assurance of a reasonable price?" The answers were tabulated and the final conclusion reached was "that a majority of the consumers replying did not regard branding or trade-marking and widespread advertising as assuring reasonableness of prices." (1) But even if the consumer does feel that advertising fails to bring about the right prices, and while we may be able to point to the danger of inflated values, still it does not follow that there should be less price advertising. It is probably true that an advertisement which carries a price message to the consumer comes nearer to

(1) "Resale Price Maintenance", A Report by the Federal Trade Commission, January 30, 1929.

fulfilling its economic function than one which does not give the consumer any definite monetary basis for judgement,

From the standpoint of society perhaps national advertisements should consist of detailed, informational, truthful descriptions of products with a great deal of emphasis on price. This price should not necessarily be maintained in the market since there is no justification for the manufacturer's dictation of the retail price. The goods passing to the retailer should be sold for a price in keeping with the marketing costs involved, which may vary with differing marketing agencies. In many cases this is exactly how advertising is used. For instance, in automobile advertisements, as well as in those of other speciality products of high value, we find the price appeal greatly emphasized. But while prices are featured in the national advertisements, giving prospective customers an opportunity to make comparisons between various makes of cars, there is much price cutting in the retail market. There are many channels through which these price discriminations can be easily effected. The price allowed for turned-in cars, the shading of prices at the end of the season, the variable freight mark-up on the factory price, offer the retailers many opportunities to deviate from the price set in national advertisements. Thus it seems difficult to measure the effect of the government's action in the resale price maintenance problem, since many advertisers appear to be playing

up prices irrespective of the retail price cutting. However, we might conclude that if there has been any tendency for manufacturers to shift away from the use of price advertising, there has been a questionable influence upon advertising.

In another direction, however, the government has been of definite assistance in raising the standards of advertising. I refer to the government's activities in business research. Advertising, as well as other lines of endeavor, needs to be based upon facts. The government, of all agencies, ought to be fitted to supply such information from an impartial basis, and although it lies within its power to do so, thus far it has done very little along this line. One governmental official discussing this situation before a group of advertising men recently said in part, "Distribution and marketing and their handmaiden, advertising, are suffering because of the dearth of statistical information in this field of business activity." (1) He estimated that of the some 1800 series of current statistics published by the Bureau of the Census, more than 95% related directly or indirectly to production and not more than 5% to distribution. As the government corrects this defect -- as it has already taken steps to do -- it will help advertising to become more effective.

- (1) "What the Census of Distribution Means to advertising" Address before the International Associated Advertisers, Detroit, July 10, 1928, by Dr. Frank M. Surface, Assistant Director in charge of Domestic Commerce, Bureau of Foreign and Domestic Commerce.

Referring to the census of distribution to be taken this year (1930), the same speaker pointed out, "Such a national stock-taking of our distributive agencies is fundamental to further progress in the field of market research. It would provide advertising with the basic facts by which its work could be planned with a definiteness and direction not now possible".(1) Another example of the government's work in market research is to be found in the "Market Data Handbook of New England" published in 1929 by the Department of Commerce. This study is a very comprehensive survey of that territory giving such minute information as the distribution of income in each community, number of automobiles, number of telephones, retail and wholesale outlets, and so on. It is planned to subject other sections of the United States to the same kind of analysis. Such information should form the basis of ^amore intelligent use of advertising.

The government may likewise contribute to the productive efficiency of advertising in a fourth direction, namely by the simplified-practice work of the Bureau of Standards of the Department of Commerce. While a simplified-practice program for an industry must be started by the business men in that field, and while those concerned must determine all the details such as which items shall be eliminated and which retained, the government has played no small part. Its principal

(1) Ibid.

help has been advisory, however, although it has been instrumental in securing general adoption and sustained adherence to the new practices, a task impossible for the unaided efforts of the industry. Such work has been attended with outstanding success in the way of savings in production and marketing expenses for business as a whole. As for its effect upon advertising they are hard to determine. In the first place, as we have already pointed out in an earlier part of this dissertation, the amount of advertising may be reduced by the increasing standardization in business. On the other hand, the simplification of the line of products and a high degree of standardization may make mass selling methods more effective than formerly and thus lead to a wider use of advertising. Likewise the quality of advertising from the standpoint of productive efficiency might conceivably be improved by this activity of the government. If advertising has been spread over a great many sizes and types, or used spasmodically for a product which varies in quality from time to time, an increase in simplification and standardization may make possible a better type of advertising.

Finally, however, the government's work along these lines may have the greatest effect upon advertising through its influence upon the consumer, who may be helped to become a more intelligent buyer. Let us see what the government has accomplished in this direction. For years the government has made use of the testing laboratories of the Bureau of Stand-

ards to make its own buying more economical and safe. It is estimated that the Bureau saves the federal government in the neighborhood of \$100,000,000 a year on purchases of supplies and equipment.(1) But the ultimate consumer is getting little benefit from this research. It is true that the government releases some of the results of its investigation, but usually in a way that is of little value to the small purchaser. Even the material which is in such form as to be readily comprehensible to the layman, is rarely utilized by him.(2) Perhaps what is needed is a little advertising by the government of the fact that they do supply such information!

Besides publishing occasional reports of the results of its research activities, the government will furnish on request "lists of manufacturers who have expressed their desire to supply material in accordance with certain United States Government master specifications promulgated by the Federal

- (1) Schlink, F.J., "Your Money's Worth" , Chase, Stuart, Mcmillan, 1927, page 202.
- (2) This applies not only to the work of the Bureau of Standards. There is a great deal of information worked out in other departments which the government will supply on request, which is never used by the public to any large extent. For example, although very thorough, reliable studies have been made of the best ways to eliminate certain insect pests, clearly stating that some of the insecticides sold are ineffectual, individuals make little effort to avail themselves of such help. Instead they turn to the highly advertised remedies on the market. One has only to turn to a bibliography such as the one to be found in "The Education of the Consumer" by Henry Harap to see that much more consumer help is available, both from private sources as well as the government, than is put to use.

Specifications Board." While these lists contain hundreds and hundreds of companies who are willing to certify to purchasers that their goods meet the requirements of government standards, this service is of little value to the ordinary buyer. He cannot buy directly from the manufacturer very frequently, nor can he afford the time and expense of checking up on the results even if he could. If the government could release information stating by name that certain advertised brands tested higher than others, the research work of the government would have greater significance for the consumer. As matters now stand it seems that the following statement is a fair estimate of the present situation: "With full allowance for the efforts of the Federal Trade Commission and the Food and Drug Administration, the government affords practically no protection against fraudulent and misleading advertising and selling." (1) As long as we try to maintain the existing competitive ideals and methods of production, it seems improbable that the government will ever release definite information against the products of given producers. To do so would presume a wider departure from *laissez-faire* than we now tolerate. This raises the question ^{as} to whether more governmental interference in industry would not be an

(1) Quotation from a circular letter sent out by the Consumers' Research Corporation, March 1930.

improvement over the present regime. Let us now turn to a brief discussion of such a possibility.

Thus far in this section we have discussed the ways in which advertising may be improved under existing conditions. Some of these improvements promise to come from individual effort, others from the present activities of the government. If the results do not promise to be sufficient to warrant a continuation of the existing methods, there are at least two possible alternative policies. One is the regulation of advertising by the state; the other the socialization of all industry including advertising. The regulation of advertising by the government might involve nothing more than supervision on minor points, such as the limitation of the amount of concern might spend upon its publicity, (1) on the other hand it might mean complete control of the industry, such as we have in the case of the railroads at the present time. In either case it would seem to be in conflict with the policy of the present order. It has been said by a famous economist, "Laissez-faire, in short, should be the general practice; every departure from it, unless required by some great good, is a certain evil." (2) One wonders on what grounds the case for

(1) At the present time there are limits set to the amounts which can be spent in getting certain political offices. This is a sort of governmental control of advertising and conceivably could be extended to take in other types of publicity.

(2) Mill, J.S., "Principles of Political Economy", Book V. Chapter XI, 7.

the state's interfering with advertising could be pleaded. Perhaps for the reason that advertising is one form of educating the consumer. Mill says on this point "In the matter of education, the intervention of the government is justifiable".(1) However, advertising is primarily a business device and only incidentally, educational. Consequently it would be hard to justify governmental interference on that score. In fact it would probably be very difficult, if not impossible to make out a case for complete governmental control of advertising on purely economic grounds. However, it may be worth our while to examine advertising under a socialistic regime, as a basis for a better understanding of the limitations of governmental control in this field. With this end in view let us turn to an examination of our final alternative, the complete socialization of advertising as well as of all other productive and marketing methods.

There is no definite way to determine what part advertising would play under socialism. All we shall attempt therefore will be a brief answer to two questions. What indications are there that advertising would be needed if production were in the hands of the state, and second what happens to productive efficiency under socialism? Even though the first inquiry should bring out the fact that there might be great saving in the advertising expenses under socialism, there

(1) Ibid, Book V. Chapter XI, Section 9.

may be no net gain if the answer to the second question shows that productive efficiency is reduced.

If the state took over production there would still be need for some advertising. First because there might be some separation between production and consumption. In any system in which the consumer had any choice in his consumption the producer, the state in this case, might find it advisable to direct consumption along certain lines. Especially would this be true if the goods had already been produced but for one reason or another were not being bought. Then again when some new product was produced, there would be a necessity of telling the prospective consumers about it, in such a way as to awaken their interest in it. If the state were in complete control this would probably be accomplished with far less wasteful "puffing" and exaggeration, than is true under the present methods. A new product, however, would not sell itself any more quickly and easily under socialism than it does now -- there would need to be some selling effort behind it. Moreover, the selling work could not be done once, for all time to come. One reason would be that the new generations growing up would require a steady amount of advertising from the state to help them become well-informed, intelligent buyers. (1)

- (1) A certain amount of propaganda to keep the citizens sold on the political situation might be required. This would be excluded from our discussion, however, since in this dissertation we have been analyzing only the publicity which is (Continued on page 201)

The total amount required to do this work, however, would no doubt, fall far short of the amount that is now being expended upon advertising. Whether the lesser amount would be more efficient is a matter of conjecture; perhaps however it does indicate an expenditure which would be nearer what is right even under present conditions. If we assume a system in which consumption as well as production is completely regulated there might be still less need for advertising.(1) It is possible, however, that a wise government in such a situation would make some use of advertising in order to make the people like the products that were doled out to them from the state store houses.(2) This expense, however, would probably amount to very little as compared with the billion and a quarter now spent in the United States for advertising every year. It would seem, therefore, that the socialization of industry would

- (1) (Continued from page 200) used for selling goods. It is said, however, that the Soviet Government of Russia at the present time is making a tremendous use of poster advertising for this purpose.
- (1) Such a system is sometimes designated Communism, as contrasted with Socialism. In the latter there is a less completely organized system of cooperation, in that the individuals are allowed to buy and own consumption goods. For a comparison of these two orders see "Principles of Economics" by F.M.Taylor, Ronald, 1925, Chapter II, page 17.
- (2) Our government's use of poster advertising during the war is an example in point. In some cases there was no question about which goods were to be consumed-- rather it was a matter of keeping up the morale of the people and making them more or less satisfied with conditions.

be advantageous for society as a whole.

But, before we can determine whether the lesser amount spent for advertising under state control is a gain or not, we must first answer our second question. What happens to productive efficiency under socialism? This is no place to take up the matter of the relative advantages and disadvantages of socialism and the present order, but some brief mention will be made of the main arguments for and against each. If it can be shown that socialism, though more saving with the use of resources in demand creation, is after all deficient in the general use of factors in production, then the conclusion may well be that the remedy for the defects of advertising does not lie in that direction.

The usual indictment of the present order is that production is not being carried on for the best interest of society when left to individual guidance. It is pointed out that the business man, motivated by profits, does not act in accordance with what is best from the standpoint of society. It is contended that the remedy is production controlled by the state in the interests of the consumers. There seems no question but that in some ways socialism would effect a better use of the productive resources than the present order. One student of the problem has pointed out that although "The business economy provides for effective coordination of effort within each business enterprise", it is not so successful in

the "effective coordination of effort among independent enterprises." (1) Socialism would remedy this defect to a large extent, since production would be controlled from some central planning bureau. Whether it would be as efficient as existing methods in the use of the factors "within each business enterprise" or not is a moot question. Many students feel that it would not be. Economists argue that the present order is superior because it links economic efficiency with individual rewards, thus stimulating greater activity on the part of the producers. Workers under socialism, on the other hand, lack this incentive and no adequate substitute seems to have been suggested thus far. In this connection it may not be amiss to call attention to the possibility of advertising as a stimulus to productive efficiency. That is, a socialistic state might divert part of its economic energies to a persistent hammering upon the direct individual advantages to be gained by a fuller cooperation in the joint venture. It is not inconceivable that such a policy might well accomplish results in increased efficiency at least comparable with, if not superior to those obtained under *laissez-faire*. If the net result is a greater volume of output with less expenditure of energy the advantage would seem to lie with socialism. If, however, socialism does not fulfill this promise, and the system of

(1) Mitchell, W.C. "Business Cycles: The Problem and Its Setting". National Bureau of Economic Research, 1927, page 172.

free, private initiative is in actual practice more productive, then it would be a serious mistake to attempt to solve the problems of advertising by a socialization of industry; If such is the case the solution must be found under the present conditions and must be in keeping with laissez-faire.(1) Furthermore, even though the presumption should favor socialism, we must still look to laissez-faire for any very proximate improvement since it seems quite unlikely that there will be any very immediate shift to socialism. The remedy for the greatest defects of present-day advertising then probably lies in the consumer's hands. However the advertisers themselves and the government too should take an active part in this house cleaning. More should be done with governmental research, with simplification and standardization, more pressure can be brought to bear upon advertisers who resort to unfair or predatory practices. No doubt these activities will be helpful, but more can probably be accomplished in two other ways. The government ought to be instrumental in furthering the self-disciplinary activities of industry; and above all it ought to make the results of its investigations available in such a form that they will be of practical use to the consumer. Such activities of organized society coupled with

(1) By laissez-faire I do not mean absolute non-interference on the part of government but rather as fully liberal an interpretation of the policy as is commonly held today.

such internal improvements as competition tends slowly to achieve must be our chief sources of improvement. Much has already been accomplished and there is little reason to contemplate the future with other than a hopeful eye.

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