THE FREEMAN
IDEAS ON LIBERTY

John Jacob Astor and the Fur Trade: Testing the Role of Government

by Burton W. Folsom, Jr.

What was the first industry in U.S. history to receive a federal subsidy? That dubious honor seems to go to the fur trade. If we study the story of the fur trade, we can see why government-supported companies so often fail and why entrepreneurs tend to provide better products at lower costs.

The buying and selling of furs was a major industry in America throughout its early history. The key animal in the fur trade was the beaver, whose pelt made hats that were in style all over Europe in the 1700s. The fur trade was a worldwide enterprise. It linked fashionable women in Paris to New York exporters, to frontier traders, to Indian trappers. The pelts of beavers, muskrats, otters, and minks went one way and kettles, blankets, axes, and muskets went the other.

At first, fur trading in the United States followed established patterns. The French and British had traded with the Indians for more than a century and the Americans simply picked up where they left off. Trapping methods, river routes, and trading posts were all in place.

The man who confounded the normal development of private enterprise in furs was none other than President George Washington. Washington feared that the many British fur traders along the Canadian border might stir up the Indians, win their loyalties, and thwart U.S. expansion into its own territory.

Private American traders, Washington argued, were too small to compete with larger, more experienced British enterprises. The U.S. government itself was needed to build large trading posts, oust the British, "bring in a small profit, . . . and fix them [the Indians] strongly in our Interest." The Indians especially needed to see evidence of American strength, so Washington recommended that the government build and operate a series of fur factories throughout the American South and West. With Washington's support, Congress appropriated $50,000 for the new factories in 1795 and raised it steadily in later years to a total of $300,000. Such a subsidy was a large expense for a new nation, and one that tested government's ability to act as an entrepreneur.

Here is how the factory system worked. The government created a bureaucracy—the Office of Indian Affairs—to conduct the fur

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For readers interested in learning more about Astor and McKenney, the author recommends John Denis Haeger, John Jacob Astor: Business and Finance in the Early Republic *(Detroit: Wayne State University Press, 1991); and Herman J. Viola,* Thomas L. McKenney: Architect of America's Early Indian Policy, 1816–1830 *(Chicago: Swallow Press, 1974).*

trade. It used the $300,000 from Congress to set up trading posts (usually near military forts), stock them with goods, and pay agents to buy, store, and transfer furs from the trading post to Washington, D. C., where they would be sold at auction. Once the factories were funded, they were supposed to be self-supporting, and perhaps, as Washington said, "bring in a small profit." Agents in the factories would use the first batch of goods to buy furs; then when the furs were sold, the agents could buy more goods and repeat the cycle.

Thomas McKenney and the Office of Indian Affairs

Almost from the start, however, the factory system struggled. Well into the 1800s, the British companies were trading actively throughout the Great Lakes area. So were private American traders. The factories were so poorly run that many Indians held them in contempt and refused to trade there. In 1816, President Monroe appointed Thomas McKenney, a Washington merchant, to take charge of the Office of Indian Affairs and help the factories expand their business.

McKenney worked hard and took his job seriously. He wrote long letters to Indians, invited them to Washington, and tried to expand his staff so he could deal with them more directly. Indians needed to be assimilated into American life, McKenney argued. Schools and farms, not trapping and hunting, were McKenney's vision for future Indian life. Therefore, he stocked the factories with hoes, plows, and other farm equipment. An active government, McKenney believed, was the best means to "amend the heads and hearts of the Indian."

McKenney's ideas proved to be a disaster. Indians wanted rifles and kettles, not hoes and plows. But since McKenney was funded regularly each year by government, regardless of his volume of trade, he had no incentive to change his tactics. Private traders, however, had to please Indians or go broke. As private traders grew in numbers and wealth in the early 1800s, one of them, John Jacob Astor, grew so rich he surpassed the government factories in capital, influence, and volume of business.

John Jacob Astor: Risk-Taker and World Trader

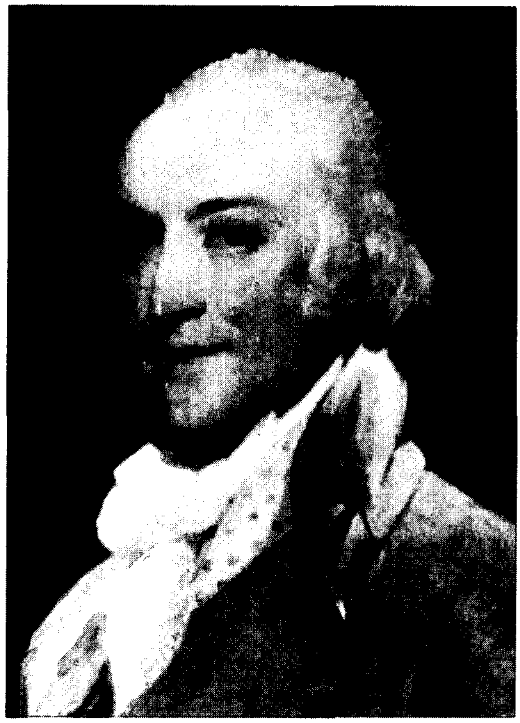
Astor, the son of a German butcher, came to the United States in 1784 at age 20 to join his brother in selling violins and flutes. Soon, however, he changed his tune. He became fascinated with the fur trade and studied it day and night. He learned prices, markets, and trade routes for all kinds of pelts. The fur territory—New York, Montreal, and the American Northwest—he traveled and mastered. Astor bought and sold cautiously at first, then with more confidence as the profits rolled in.

He was an odd man to be such a risk-taker. He was quiet, almost secretive, in his business dealings. Astor had a keen mind for enterprise, but he spent years at a time out of the United States, estranged from his wife and fighting bouts of depression. He was both decisive and patient. He had a vision of how America would grow, how the fur trade fit into that growth, and how to market furs around the world. With commanding vision and masterful detail he could profitably buy furs in Michigan, pack them on a boat to New York, ship them to China, and bring tea back home.

Astor separated himself from others through his foresight and perseverance. If the matrons of France wanted beaver hats and otter coats, and if these animals roamed the forests of New York, that was all most traders cared to know. Astor, however, thought more of world trade. Europeans liked to fight each other and wars disrupted markets; why not expand and sell furs to the Chinese—not for fashion, but for warmth in their unheated houses? Besides, he could bring the tea back from China and profit at both ends.

The large market of the Far East prompted Astor to turn his sights west to Michigan. New York and the Atlantic Coast were depleted of furs by the early 1800s. The Great Lakes area—especially the Michigan Territory—then became the heart of the fur trade, and yielding thousands of skins for coats and rugs all over the world. Astor founded the American Fur Company in 1808 and made his move to challenge the government factories.

Under Astor, the American Fur Company resembled a modern corporation with specialists, division of labor, and vertical integration. Astor ran the company from his headquarters in New York. Mackinac Island was the center of the actual trading, where most furs were bought, packed on boats, and sent to the East Coast. Astor's agents dotted the rivers throughout the Northwest and they had log cabins well-stocked with goods. They supplied the company's fur traders, who would live with the different Indian tribes and supply them with goods and credit as needed.



John Jacob Astor (1763–1848)

Astor's Advantage

In conducting business this way, Astor differed from McKenney and the government factories. McKenney and his predecessors just built trading posts, stocked them with goods, and expected the Indians to come there to trade. Many Indians, however, lived hundreds of miles from a factory and had no supplies to trap with. Even if McKenney had given credit easily, and had known whom to trust, the Indians would have been hampered by distances. Under Astor's system, the fur traders lived with the Indians, learned whom to trust, and bought and sold on the spot. If an Ottawa brave capsized his canoe and lost his musket and powder, he could get replacements from Astor's local trader and avoid the 90-mile walk through swirling snow to see if the government agent in Detroit would give him replacements on credit.

Astor built on this advantage by trading the best supplies he could find at reasonable rates of exchange. Indians wanted guns and blankets, for example, and Astor supplied them at low cost. The best blankets he could find were British-made blue-striped blankets, and Astor bought them at 15 percent less than McKenney paid for lower quality blankets made in America. Astor bought British Tower muskets, the best on the market, for about $10 apiece, but McKenney paid $12.50 apiece for Henry Deringer's muskets made in Philadelphia.

One reason Astor succeeded was that he accepted the Indians as they were, not as he wanted them to be. If they desired axes, kettles, and muskets, he tried to find the best available and sell to them at competitive prices. He respected Indians as shrewd traders and knew he had to have the best goods to get the most business. McKenney, as we have seen, squandered government resources on goods Indians didn't want.

McKenney refused to sell liquor in government factories and urged Indians to be sober, virtuous, and industrious. "The same devotion to the chase, and those irregular habits which have characterized the sons of our forests yet predominate," he lamented.

Liquor was also an item Astor preferred not to supply, even though he knew many Indians wanted it. Not that Astor was a moralist; he was a realist. Drunken trappers gathered no pelts, he discovered. If the factories had been his only competition he probably wouldn't have traded liquor at all. But the traders with Britain's Hudson's Bay Company carried so much liquor they could almost have created another Great Lake with it. Astor thus concluded that for him to be competitive he needed to have some liquor available for trade.

Motivation and Marketing

Trade was not the only area where Astor outmaneuvered the government factories. The motivating of men was another. Astor used a merit system and paid his chief managers good salaries plus a share of the profits. This guaranteed an attention to detail, which Astor needed to stay on top. McKenney and his staff, by contrast, received a standard salary from Congress with no bonuses given in profitable years or cuts given when trade fell.

One final area of Astor's genius was his marketing savvy. He sold his furs at auctions all over the world. If he didn't get the prices he wanted in New York he sent furs to auctions in Montreal, London, Hamburg, and Canton. McKenney, by contrast, had the furs collected in his factories sent to Washington. Then he sold them at auction in nearby Georgetown for whatever price they would bring. He didn't sell in different cities, nor did he withhold any from the market in bad years.

Sometime after 1808, John Jacob Astor surpassed the government factories and emerged as the leading exporter of furs in the United States. He widened his lead after the War of 1812. By the 1820s, the American Fur Company employed over 750 men, not counting the Indians, and collected annual fur harvests of about $500,000, which made it one of the largest companies in America.

McKenney nervously watched the government's share of the fur trade decline year by year. "Why do the factories lose money?" Congress asked when McKenney came before them each year to renew his subsidy. He was embarrassed by Astor's dominance and perplexed at what to do about it. At one point, he urged his agents, or "factors" as they were called, to stir up Indians against private traders. "[A]ll correct means that may be taken to expel those traders," McKenney wrote, would be "of service to humanity and justice."

By 1818, McKenney had reached a dramatic conclusion: the best way to beat Astor was to influence Congress to ban all private fur traders. If this could be done, McKenney could monopolize the fur trade, sell the Indians what he wanted them to have, and pursue his dream of amending their heads and hearts. "Armies themselves," McKenney argued, "would not be so effectual in regulating the native Inhabitants as would a state of dependence on the Government for their *commercial intercourse*." Sure, McKenney admitted, a monopoly "embraces the idea of compulsion." But "the power over the Indians is covetted [sic] only for their good—and also to prevent them from doing harm."

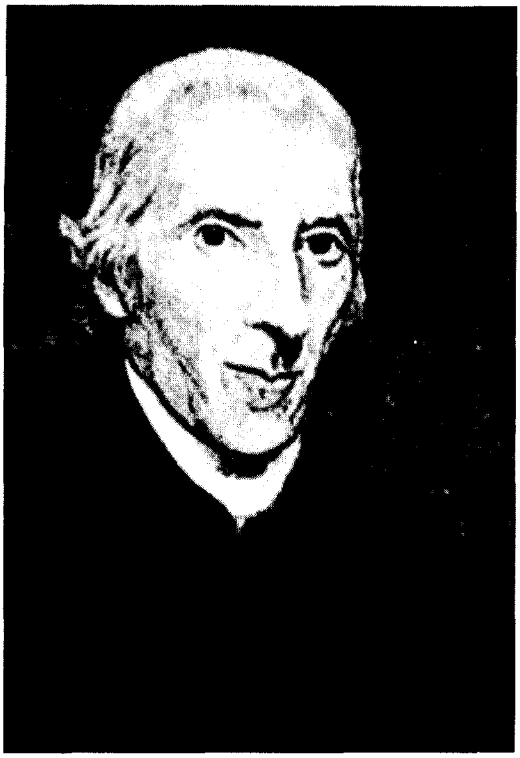
John C. Calhoun, Secretary of War and later vice president, was swayed by McKenney's ideas. "The trade should," Calhoun wrote, "as far as practicable, be put effectually under the control of the Government, in order that . . . [the Indians] may be protected against the fraud and the violence to which their ignorance and weakness would, without such protection, expose them."

Even with friends in high places, however, McKenney couldn't muster the support in Congress to ban private fur trading. He therefore presented two backup plans. First, the government should increase his subsidy from $300,000 to $500,000. Second, McKenney wanted to increase the license fees for his competitors. If he couldn't ban private fur traders by law, perhaps he could raise their costs of doing business, and thereby improve the competitive position of his factories.

Astor hated to play politics, but he believed he had to be politically shrewd to survive. He wrote President Monroe and explained how the American Fur Company helped the U.S. economy. Other politicians came to Astor's aid. Governor Ninian Edwards of the Illinois Territory challenged Calhoun: "For my part, I have never been able to discover, and I defy any man to specify, a solitary public advantage that has resulted from it [the factory system] in this country."

From 1816 to 1822, Congress heard from both sides and had frequent debates on the fur trade. For both sides, it was a fight to the death. When McKenney's factories showed a drop in fur sales from $73,305 in 1816 to $28,482 in 1819, his case began to weaken.

Astor then took the offensive and urged Congress to abolish the whole factory system. His first step was to get Congress to see how unpopular the factories were with Indi-



Jedidiah Morse (1761–1826)

ans. Calhoun, McKenney's ally, unwittingly cooperated when, as Secretary of War, he helped authorize Jedidiah Morse, a neutral observer and Congregational minister, to go into Indian country and report on the Indian trade.

Morse visited most of the government factories and interviewed the men who worked in them as well as the private traders nearby. In his report he came down clearly against the factories. "In the first place," Morse wrote, "I have to observe that the Factory system . . . does not appear to me to be productive of any great advantage, either to the Indians themselves, or to the Government." This conclusion was devastating because it revealed that the factory system had failed to do what Washington set it up to do—impress the Indians, gain their respect, and challenge the British in the Northwest Territory. Morse further wrote that "the Indians, who are good judges of the quality of the articles they want, are of the opinion that the Factor's goods are not so cheap, taking into consideration their quality, as those of private traders."

Morse was not completely pleased with private traders. They traded too much whiskey, he wrote, and they gave Indians too much on credit, which weakened their work ethic. But he couldn't deny their success or the "want of confidence in the Government . . . expressed by the Indians in my interviews with them."

Armed with the Morse report, Astor's allies in Congress moved to abolish the factories in 1822. Thomas Hart Benton, the new senator from Missouri, had been a lawyer for Astor and knew the fur trade well. On the Senate floor he ridiculed McKenney's purchases, particularly the eight gross (1,152) jew's harps he had recently sent to the factories. What use, Benton asked, could Indians have for jew's harps? "I know!" he said sarcastically. "They are part of McKenney's schemes to amend the heads and hearts of the Indians, to improve their moral and intellectual faculties, and to draw them from the savage and hunter state, and induct them into the innocent pursuits of civilized life."

The End of the Factory System

Not surprisingly, Benton urged Congress to end the factory system. Most Congressmen agreed. The Senate voted 17 to 11 to end the factories, and the House soon followed. On May 6, 1822, President Monroe signed Benton's bill.

The closing of the factories was a story in itself. The merchandise inside them was to be collected and sold at auctions around the country. The money received would then be returned to the government to offset the $300,000 federal subsidy. The auctions themselves, which became the true test of the market value of the articles in the factories, brought grim news. The government, on its $300,000 investment, received a return of only $56,038.15. As Senator Benton had said, "The factory system grew out of a national calamity, and has been one itself."

Many Congressmen were astounded at the waste of government funds revealed by the auctions. If Astor could make millions of dollars trading furs, how could the government lose hundreds of thousands? Critics demanded answers and Congress formed a committee to investigate the unprofitability of the factories. They sifted through mountains of records and interviewed lines of witnesses. McKenney was on the spot and had to testify, but the committee found no corruption, just "inexplicable" losses. The factory system just failed, the committee concluded, but it needed to be studied "not only as a matter of curious history, but for the lesson it teaches to succeeding legislators."

Astor, meanwhile, continued to expand and prosper. New companies entered the fur trade during the 1820s and existing ones continued to challenge Astor. The competition was keen and Astor's volume of business varied from place to place. The American Fur Company, however, remained the largest firm in the field after the factories were closed. Astor, better than any American before him, had mastered the complex accounting and organization needed to conduct a worldwide business.

Astor and McKenney: An Epilogue

By the late 1820s and into the 1830s, the fur trade began to decline. Astor always knew the trade couldn't flourish forever—furs were being collected faster than new animals were growing them. Changing tastes slowed down business even more than the scarcity of animals. As Astor noted from Paris in 1832, "they make hats of silk in place of Beaver." Also, the Industrial Revolution and the popularity of cheap, mass-produced clothing shut down markets for furs. "[M]any articles of manufacture which are now very low can be used in place of deer skins & furs," Astor observed in 1823. "[T]hey receive of course the preference." Evidently it didn't occur to Astor to try to get the government to handicap or eliminate his competition.

In 1834, three years before Michigan became a state, Astor quit the fur business and sold the American Fur Company. He was 71 years old and ready to do less strenuous work. The same skills that made him America's largest fur trader also made him profits in New York real estate. For many years, Astor had been buying lots in northern Manhattan, developing the property, and selling it at a profit. This he continued to do. He also invested in the Park Theatre, the Mohawk and Hudson Railroad Company, and the Astor House Hotel. By the time of his death in 1848, he had accumulated America's largest fortune, about $10 million.

The last years of McKenney's life were not so pleasant. Outside of government, he struggled as a businessman, writer, and lecturer. His wife died, and his son became a wastrel. McKenney lived out of his suitcase, borrowing money and moving from city to city. In 1859 he died, at age 73, destitute, in a Brooklyn boarding house. □

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Three Fallacies of Rent Control

by Robert Batemarco

From New York to Boston to Toronto, rent control is under attack. Not surprisingly, beneficiaries of this legislated plunder of providers rental housing are sparing no effort to maintain their unmerited privileges. In so doing, they resort to a wide variety of fallacious arguments. Three in particular stand out and will be discussed here.

1. "Rent control may not be needed everywhere, but my city is a special case."

Whole schools of "economic" thought have formed around the idea that all economic principles are special cases with no universal validity. This notion is actually an attack on the very status of economics as a science. As Ludwig von Mises noted, an attack on economics itself is the only way to undermine the irrefutable case that economic analysis makes against all kinds of interferences with the market. "If one tries to refute the devastating criticism leveled by economics against all these interventionist schemes, one is forced to deny the very existence . . . of a science of economics. . . ."[1]

The "special case" argument has been used by partisans of rent control. New York City's rent control regulations are actually codified in legislative enactments of New York State. Recent attempts to weaken, if not eliminate, rent control regulations have been spearheaded by upstate lawmakers. This led New York State Assembly Speaker Sheldon Silver, who represents a Manhattan district, to quip in reference to its housing situation: "I would suggest that New York City is a lot different from Troy."[2] The implication is that while rent control may not be necessary and effective in Troy, it works wonders for New York City. Yet one of the hallmarks of economic law is its universal validity. In this case, whenever government prevents the charging of prices high enough to clear the market, shortages will occur. This is true in New York, in Troy, or in Timbuktu, regardless of whether the market is for rental housing, gasoline, or medical care.

2. "A free market would make housing unaffordable for most people."

The longevity of rent controls has worked to the advantage of its supporters. Most New Yorkers have lived with rent regulation for so long that they have no conception of how the market sets rents in the absence of controls. For the lack of both experience with a free housing market as well as theoretical understanding, they are willing to believe the most ludicrous "horror stories." For instance, Speaker Silver suggests that repeal of rent stabilization laws would drive the middle class out of the city, asserting that "If the rents were tripled it would drive tenants out of the city."[3] My impression is that the period of rent controls has itself been characterized by a massive outflow of middle-class people from the city, which, as theory tells us, is no accident. The very logic of rent control is to make it possible for lower-income people to compete more successfully with the middle class for the limited stock of rental housing.

Furthermore, how can anyone know that rents would triple? There was no tripling of oil

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