On Bilateral Monopoly: a fragment from the projected Volume Two of Marshall's *Principles*

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Introduction

The manuscripts of Alfred Marshall held in the Marshall Library, Cambridge, include the fragment whose text follows. The manuscript is headed with Marshall's note "From P[rinciples] XI iii. To be replaced 2.9.05". The fragment is of particular interest since it seems to be the only identifiable portion of a lengthy draft for the second volume of *Principles* that Marshall had composed in the decade or more following the publication in 1890 of its first volume. He recorded that by 1903 "a very rough draft for the continuation of my Principles extended to more than a thousand pages: and it was becoming obvious that I could not hope to finish the work on the scale to which I was then working" [1] . The fate of the remainder of this lengthy manuscript is unknown, although it seems likely that substantial portions were incorporated without notice into Marshall's *Industry and Trade* of 1919. In addition to serving as a brief example of the style of the lost volume, the fragment has intrinsic interest because of its clear exposition and integration of ideas that remain somewhat separated elsewhere in Marshall's writings. Marshall's incomplete and inaccurate attempts to provide references suggest that the fragment was composed when he was away from his books, but the intention seems to have been to use the fourth edition of his first volume as the primary source, suggesting a composition date no earlier than 1898.

Text [2]

This brings us to consider the relation of two or more businesses that supplement one another; each having something of a monopoly, which is however of little or no avail without the aid of the others. Thus the owners of neighbouring mines of coal, and of iron ore, if far from any good market except that which each offers to the others have no easy means of deciding on what terms they shall do business. A railway line that connects them may be able to plunder them both, at the risk of ultimate catastrophe if a special line is made on their behalf.

Such cases present two evils. Any increased outlay of capital or effort by either of the two monopolists will accrue to the benefit of the combined product. But there is no direct method of determining the share of this benefit that will be allotted to him to whom it is due. All that can be confidently surmised is that he is unlikely to receive the whole of it. He has therefore less motive for energy and enterprise than if the two monopolies were held in one hand, and the whole benefit of any outlay that improved the combined product went to him that made the outlay. This is the first evil. The second evil lies in the uncertainty and the waste of time and energy that are given to higgling and bargaining as to the division of the proceeds of the two monopolies.

One form of this problem is seen in the relations between old employees of a firm whose special experience would lose most of its value, if they left it: so that while they could not get equally good salaries elsewhere, the firm could not get as valuable service from others even at higher salaries [3] . Another form is seen in the relation of landlord and shopkeeper tenant, where the tenant could not move without breaking with his custom and thus losing perhaps more than he would by the doubling of his rent, though that is perhaps already higher than a new tenant would consent to pay [4] . Similar again is the case of composite rents such as that of a watermill when the water power and the only site convenient for turning it to account belong to different owners [5] .

But perhaps the most instructive form is that given by Metayer Tenure. According to the commonly received account the tenant is provided with land, buildings, cattle etc., on a definite scale rigidly governed by custom; and has fixity of tenure subject to the sole condition of handing over half (or some other fixed part) of the produce to the landlord. Hence it was inferred that the tenant would undertake nothing that was not enforceable under recognized customary rule, unless he expected from it an additional produce twice as large as was needed to compensate him for the trouble. And it was inferred that, if an alteration in the general plan of cultivation were required by changes in the markets for such part of the produce as was sold, the relations between landlord and tenant would be reduced to chaos. But in fact competition and bargaining were only lethargic they were not dead.

Custom had been fashioned slowly and imperceptibly by them; and it never ceased to be plastic. There would be ever and anon injustice, tyranny, unreason and obstinacy: but under the surface there was a drift towards perpetual give and take so that the landlord was generally induced to move slowly towards supplying any appliances or stock, and the tenant to move towards applying any labour, which were recognized by the common opinion of the place to be required by the conditions of the case: and common opinion moved, though slowly [6] .

Take for instance the case of passenger traffic between two large towns, the rate per mile being fixed by law. Suppose the accommodation at one of them to be inconvenient to passengers: and the question arises whether a new station should be built. If the whole line is owned by one company, the outlay will be weighed in the balance against the increased net receipts over the whole of the line. But if the line is shared between two companies then the outlay will be weighted against only that part of the net receipts which correspond to the traffic over its portion of the line. The one case will correspond to the English system of tenure, where the man who makes the outlay retains the whole fruit (excepting of course with regard to durable improvements): the other will correspond to the Metayer system where he retains only half.

But in fact nearly all monopolies are *conditional*: that is the exclusive privilege which they confer can be maintained approximately intact only so long as it is used with moderation. And even where a monopoly is apparently absolute, and the retribution that would follow on abuse is not clearly in sight, common sense and good feeling generally suggest some moderation; some compromise in its relations to other monopolies, and some understandings which are generally faithfully observed even when not explicit: and not infrequently they are explicit. Such considerations often tend to keep up to their work each of two monopolistic industries, which largely depend on one another's trade: whereas if they were fused, the fear of competition would be removed one stage further; and that would be adverse to public interests throughout, and not improbably to their own in the long run.

The relations of small producers in sleepy times are separated widely from those of vast business aggregations of today. But the fundamental strain of human nature is the same. As indirect competition and implicit bargaining worked under the surface where custom appears to have made all still and stagnant, so they work under the surface where monopoly seems to save one or more of a group of correlated producers from the need of considering the interests of any others.

Thus the real issue in all problems of this class is not to be decided by abstract reasonings. Indeed there is some danger that abstract reasonings may suggest a false idea of proportion: it being in human nature to lay stress on different considerations partly in accordance with the clearness and vividness with which they are apprehended. Thus a consideration which is capable of presentation with clear cut outlines is apt to count for more than another which is really of more import, but does not appeal so effectively to the mind's eye. There are perhaps no economic problems, with regard to which this caution is more needed, at the present time than those relating to the several functions of economic organization and economic freedom [7] .

The abstract side of the problem of two monopolists neither of whom can dispense with the cooperation of the other was initiated in Cournot's monumental *Recherches sur les principes mathématiques de la théorie des richesses* Ch IX, with all his customary force and suggestiveness but with less than his usual precision. He supposes copper and zinc to be each in the hands of an absolute monopolist, and to be useless except when united to one another to make brass. And he then professes to determine mathematically how their values would be governed. But the problem as he states it is indeterminate: the premisses give no reason for supposing that either monopolist will or will not get the better of the other in the bargaining. He however introduces in [the analysis] an equation as to the indirect demand for each of the metals, for which no psychological reason appears, and which leads directly to the conclusion that the aggregate profits of the two are equal: a conclusion which his avowed premisses justify as much [as] they do any other; but not more. In the real world we do not meet with indeterminate problems of this kind. We may find a water power owned by one person, and the only good site for utilising it owned by another. But the strategical positions of the two are never absolutely equal and symmetrical, like the haystacks midway between which Buridan's ass perished of hunger. Each is sure to have some points of vantage, such as indirect competition or substitution or alternative uses; each will make the most of his power and willingness to wait till the other gives more favourable terms.

[1]. See Whitaker (1975, vol. 1, p. 93). Marshall added that “The order proposed for the continuation of my Principles changed many times: but I left it in 1903 fairly settled”. At that point the fragment would have belonged to the fifth broad topic in a list of nine, the one dealing with “Business Combinations and Monopolies, Transport Problems” (loc. cit.). This would have been Book XI on the assumption that the nine topics were designed to become in sequence Books VII to XV of the second volume. Evidently the coverage of the draft had deviated considerably by 1903 from the proposal for Volume Two initially made in 1887 (*ibid*., p. 89), but there is little or no information on its evolving structure before 1903. For a detailed account of Marshall’s struggles with literary composition after 1890 see Whitaker 1990.

[2]. Marshall Papers 5/31; formerly Box 2. The text is composed of 16 small sheets of paper, numbered 27-29, 32-44. The text has been slightly edited (for example, ampersands written out and apostrophes inserted). Editorial additions or doubtful readings in both text and footnotes are enclosed in square brackets.

[3]. See VI viii 10 (VI xi [8] in Ed. II, III [and] VII xi in Ed I). [The first reference is presumably to the fourth edition of 1898 (replaced by the fifth in 1907) where the pertinent passage occurs on pp. 706-7. The correct reference to the first edition is VII xii 8. See pp. 625-7 of the eighth edition for the final version of the cited passage].

[4]. See ... [The reference was not completed but it seems likely that the intention was to refer to a passage in Marshall’s *Memorandum on the Classification and Incidence of Imperial and Local Taxes* provided to the Royal Commission on Local Taxation of 1897. See pp. 327-64 of Keynes 1926 for the text and p. 351 for the pertinent passage. In the fifth edition of *Principles* much of the Memorandum was reproduced as Appendix G. The passage in question is on p. 799 of the eighth edition of *Principles*.

[5]. See V x 4. (In Ed...[not completed]. [The reference given appears to be to the fourth edition where the pertinent passage occurs on pp. 508-10. The corresponding reference to the eighth edition is to V xi 7. pp. 453-4].

[6]. Compare VI xi. [The appropriate reference to the fourth edition appears to be VI x 3,4 pp. 727-33. See pp. 640-5 of the eighth edition].

[7]. [The following paragraph was to be set off as a footnote. See Pigou 1925, pp. 535-6 for further remarks by Marshall on Cournot’s analysis of bilateral monopoly].

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