

# WARS AND LONG-RUN GROWTH IN EUROPEAN ECONOMIES

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*El profesor O'Brien participó en el ciclo "Guerras, catástrofes, crisis: lecciones de la Historia Económica", organizado conjuntamente con el Instituto Figuerola de Historia y Ciencias Sociales de la Universidad Carlos III de Madrid. El ciclo responde al convencimiento de que el análisis de cuestiones tan importantes y tan diferentes como el impacto de las guerras, las catástrofes, el colonialismo o las políticas económicas se enriquece cuando se tratan con la profundidad que da una perspectiva a largo plazo. El enfoque de la Historia Económica nos proporciona la reflexión suficiente para afrontar los problemas que puedan surgir en el futuro, y encontrar las soluciones adecuadas.*

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There is a famous phrase by Charles Tilly which reads that states make war and war makes states, but why is that war-like empires such as the Mughal Empire, the Ming-Qing Empire, and the Ottoman Empire did not create developmental states, and why was it that the British before the Spanish or the French or other European countries created developmental states?

Some countries have created and sustained the institutions which have made them currently amongst the richest in the world. But why they sustained and created these institutions is because they had a mega-institution, mainly the state. It is the state that ultimately creates and destroys or fails to create the institutions for growth. What we actually need is an efficient state that can be recognized retrospectively as one that provides an economy with public goods, namely external security. If you do not have external security, as per the Ukraine at the moment, you're not going to have economic growth.

Secondly, you need internal stability. Nobody expects large parts of the Middle East to develop at the present time because they do not have the most precious of public goods: a stable regime. Even a dictatorship, so long as it is stable, is very often good for growth. In fact, some dictatorships have been very good for growth. So, it is these states that are required for the maintenance of institutions, for our laws, and our cultures that promote economic growth. Lastly, the historical capacities to act in creating external security and internal stability are highly correlated to their

capacity for raising taxes, so taxation is a key element in the story of economic growth.

The concerns of pre-modern European states were not with economic development but with external security, internal stability and, above all, the Habsburg dynastic survival. In the particular case of Spain, they tried hard to centralize power in the context of political and geopolitical fights. In Europe we have warlords, we have aristocrats, we have urban oligarchies, we have the Church, and we have rebellious peasants and disaffected proletarians, and all these centrifugal forces which are now coming up again in Europe.

Until the 18<sup>th</sup> century, the economic gap between most of Europe and large parts of Asia/Eurasia, was rather minor. In these centuries the technologies available to states for the gathering of information and the acting on information and knowledge about the countries, the regions, the peoples, the ethnic groups, and the religious minorities over which they ruled, were really rather primitive.

Sometimes democracies co-relate highly with economic growth, but very often, they do not. Sometimes a period is needed of a very strong leadership. You need a Hobbesian monarch or a Hobbesian ruler to get you on the path of economic growth. What historians have decided to do in order to obtain some insights into this process is to compare states and how they developed in the West, within the West, and, lastly, between the Occident and the Orient. This, essentially, is the Marc Bloch's historical method. Marc Bloch advocated that

we did reciprocal comparative history, that we looked across Europe and we compared state formation in various parts of Europe. We've come up with the possibly Euro-centered hypothesis that the firms, farms, investors, entrepreneurs and innovators operating within this war-like Europe that we all know about in the early modern period, were operating with an ideology for state formation, for mercantilist order that was, in the end, conducive to more rapid growth compared with the great empires of Asia and other parts of the world.

### **But, how can we confront this hypothesis?**

But, how can we confront this hypothesis, which goes way back in historiography? It goes back, classically, to the writings of Max Weber, and which has already attracted a number of naïve answers from economists, including Acemoglu and Robinson. Following an approach developed by Schmoller and Schumpeter from the German Historical School, my approach has been to formulate hypotheses based on the vast bibliography of literature on state formation in the West, first of all, to explain why Britain can be represented as the paradigm case for successful warfare and mercantilism, and offer a negotiable explanation as to why Europe's delayed and Asia's retarded transitions to industrial capitalist market economies took the time that they did.

After 23 years of warfare against Revolutionary and Napoleonic France, the monarchy of Britain, along with its plutocratic and aristocratic elites was in charge of governing the, by then, United Kingdom of England, Wales, Scotland, and Ireland which, by the way, it is about to break up again. We are offered superior standards of external security, internal stability, protection of property rights, and



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support for a traditional authority of hierarchy, legal frameworks for the extension and integration of markets, encouragements for technical and business innovation, and, above all, more extensive and better protected access to the markets in all parts of the world. The question, first of all, is we need to understand why Britain got there first, and it is because we had a strong, comparative advantage in state formation and in violence, above all, in naval violence.

That was our strongest comparative advantage, and that was mainly derived because as a result of the Civil War, when we cut off the head of our king Charles I in the middle of the 17<sup>th</sup> century, for trying to raise taxes and centralize the state. But, it is not until we have a republic in the middle of the 17<sup>th</sup> century that we start to build a navy, that we start to build a real fiscal system, and we owe that not to our greatest sailor, but to our greatest soldier, Oliver Cromwell. Under the Republic, the British Navy and the British tax system started

to reform itself, and Britain started to become the greatest power in the rise of the West.

Along with taxation goes the capacity to borrow money. As many have discovered by being members of the European Union, it has much to do with our capacity to repay or not to repay money, as the case may be. People had extreme confidence in the state, created by the republicans and carried on by the monarchy and the aristocracy in the 18<sup>th</sup> century, that they could lend it money, and money flowed into London, not merely from all over Britain, but from all over Europe. Taxes were used to fight wars, but 60 to 70 percent of all the taxes that were raised, which were amongst the highest in Europe per capita, were going to service debt, so Britain was borrowing money, fighting a war, winning a war, and servicing its debt.

What were taxes also spent on? They were spent on the Royal Navy founded by Oliver Cromwell and we invested massive amounts of money in naval power, an obvious thing to

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do for an island, although we were already defended by the waters, as the Spanish Armada found out in 1588.

The British State and the British people thought their navy was very important, and the navy was extremely popular, and people were willing to support it. At the end of the Napoleonic Wars, we had the greatest tonnage of ships and we were in command of the

ocean, and we remained in command of the ocean right through the 19<sup>th</sup> century, so British hegemony is first and foremost a naval hegemony, derived from the creation of a fiscal state.

Some historians state that we had a successful fiscal state because we were invaded by the Normans and the Normans were great centralizers, so there is a medieval origin in the creation of the modern state. But the defining moment was to withdraw from imperial warfare on the mainland of Europe in 1453. Britain stopped trying to take over the whole of France and the whole of Europe after hundreds of years of warfare between British and French monarchs in that particular period.

Britain withdrew to the island, to internal colonization over the Celtic fringes of the kingdom, that were finally brought firmly into the kingdom. Compared with other powers on the mainland of Europe, particularly France, but also Spain, we did not play a really big part in the Reformation. If compared with France or Spain or Portugal, or particularly with the 30 years in Germany, it is really a rather minor sort of event. There is a change, the king becomes head of the Church and the Church becomes more secular. Over time, the Church of England has become steadily less and less religious.

Then, in the middle of the 17<sup>th</sup> century, we have our famous civil war, and that leads to a very sharp division. It is in that particular period, in which the navy is built up and Celtic threats to the stability of the kingdom from Ireland and from Scotland, are brutally suppressed by the Cromwell and the republic army, when the imposition of Protestantism is then firmly established. Then, it followed a period of further reforms to the structure and administration of the fiscal sys-

## Per Capita Tax Revenues Delivered to Governments

Expressed as Revenues Received by Central Governments  
(tons of silver -res of daily wages of unskilled construction workers employed in capital cities)

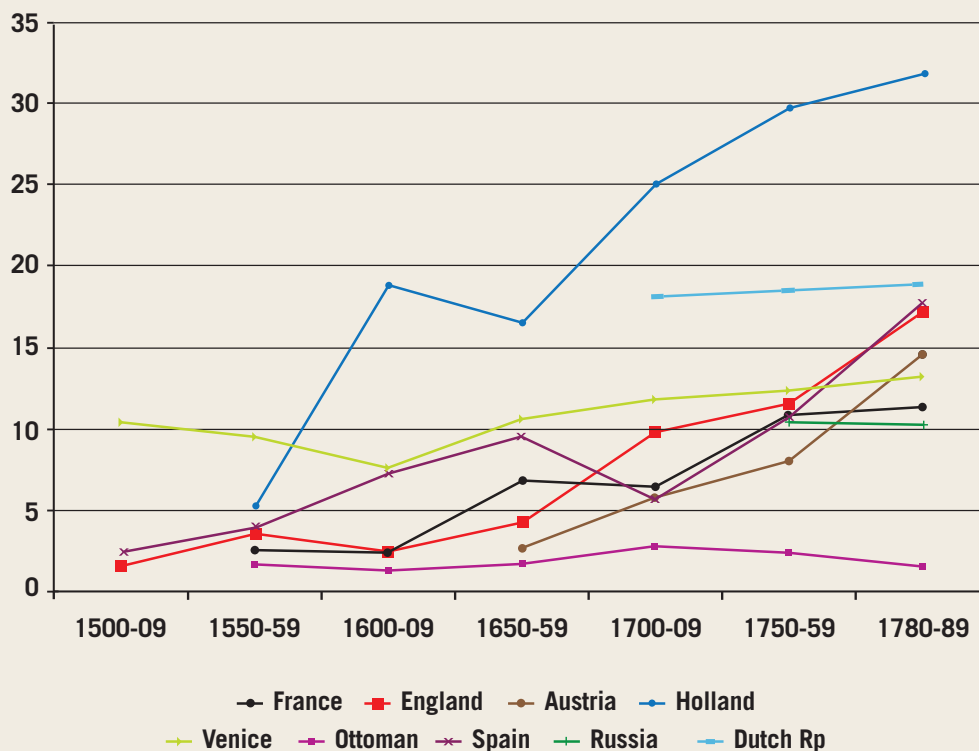


Figura 1

tem, and a period of continued aggression, particularly against the Dutch, since they controlled very large shares of world trade, they were clearly rich at doing so, they were colonizing large parts of the world; and they were seen as the prime threat to Britain's drive for hegemony and stability.

Britain fought three wars against The Netherlands, and then it fought a war against France with The Netherlands on its side. But in the famous battles when the British Navy is supposed to have showed up to help the Dutch beat the French, somehow or other the Bri-

tish Navy failed to show up. The Dutch got extremely annoyed about that because they were then beaten by the French and ended up signing the Treaty of Utrecht with a much smaller navy and a much weaker power. Britain is then ready to take their place in the world economy.

### Mercantilism based on naval power

Britain then has a financial revolution, creates a centralized national debt, and creates the Bank of England, what is a key element in its

success in mercantilism based on naval power. This mercantilism was pursued by all European powers for many centuries. They remained preoccupied with power compared with profit. They were focused upon the gains from a positive balance of trade, and committed to maximizing the direct benefits and externalities embodied in exports and strategic imports, particularly the kind of imports from Asia and from the Americas that you could actually make on the island: cottons from India, silks from China, all kinds of things that we were bringing in from the rest of the world. Raw materials were all refined at port, so the port becomes, in England, what Braudel called the *pôles de croissance*, the points of growth, which are brought in under naval protection from the rest of the world and copied by the English during their commercial revolution.

The mercantilists were right about bullion. They were often criticized with having a pre-occupation with gold, and Spain is often criticized for having a pre-occupation with precious metals. But, if you want to go to war, you need precious metals. You have to pay the troops so they do not mutiny, and you need to pay for your supplies, if you're abroad, with hard currency. This leads to an expansion and

*The British regime in the 19<sup>th</sup> century is ostensibly liberal but, socially and culturally, it is very hierarchical*

an agglomeration of economic activity in ports all around the coast, as described in Braudel's works on capitalism and material life in the early modern period, and it is modeled by economists latterly in their network technologies and gains for agglomeration. Organization is in many, many ways, as economists are beginning to understand, best for growth.

The best place to have skilled labor, to interact, to interconnect, to develop innovation, to develop science and technology is not in the countryside; it is in the cities. The bullion that you obtain will allow you to build up an efficient system of financial intermediation, a good banking system, a central bank that actually controls the money supply and helps to keep the money supply in line with the growth of the economy. Above all, it will give you raw materials and food stocks from overseas upon which programs of import substitution can actually be built. A lot of British industrialization, famously the cotton industry, but also many industries are actually created on the basis of imported raw materials and imported manufacturers, which were copied after having learned how to make them.

It was not a peaceful world though. Mercantilism promoted costly bouts of warfare, which led to pressures for fiscal centralization to fund ever more expensive wars, which became ever more expensive as the Europeans went over to gunpowder weapons and firearms of various kinds before the rest of the world. It facilitated a system in which the best and the brightest, if they had an alternative religion or they were persecuted in any way by the state, or they didn't feel at home, could actually move to a Protestant country or a Catholic country, or some other country, promoting what Alfred O. Hirschman called exit and voice. You had to hang on to these skilled people, you had to make concessions to them; otherwise, they

would leave. Skilled Europeans were mobile. They could always move about. It promoted proto-globalization, which was led by the Spanish and the Portuguese overseas, followed first as free riders and pirates by the English, but eventually led by the English.

It led, after 1815, once we had finally beaten

## Total Revenues Received by Central Governments

Expressed as share (%) of conjectures for GDP)

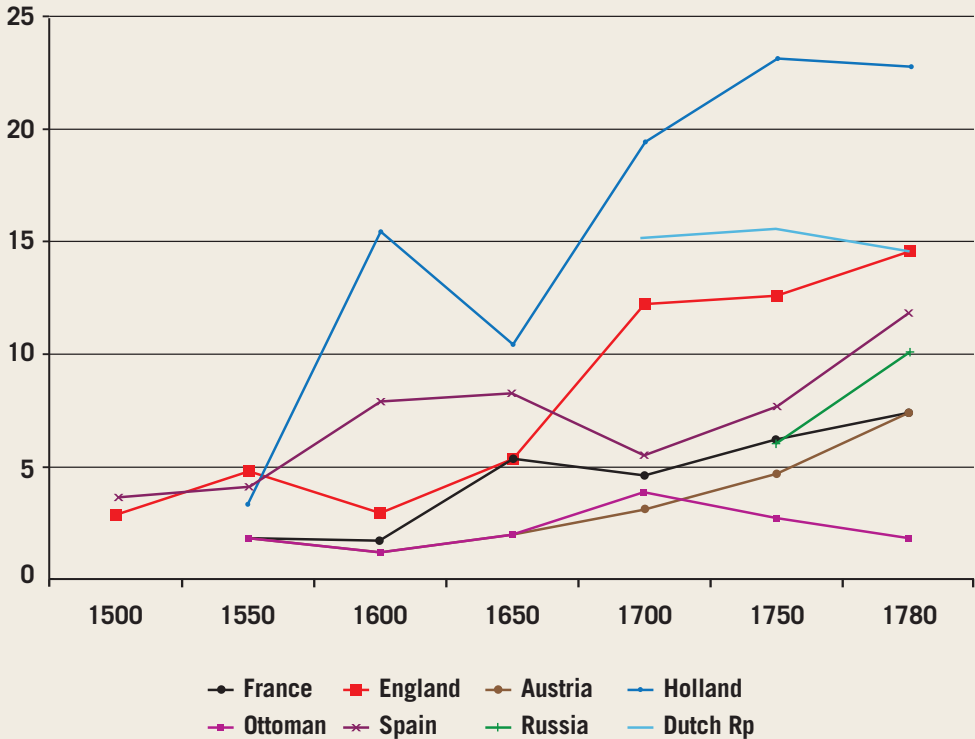


Figura 2

the French in the Second Hundred Years' War, to one hegemonic naval power. It is this hegemonic naval power, winning that battle at Trafalgar that really creates the conditions for the end of mercantilism and the beginnings of free trade, without one single navy commanding the oceans, preventing people re-colonizing the Americas, preventing the Spanish going back into North America, the French going there, carrying on with those colonial wars in the east. That helped keep the peace. The statistics for warfare in the 19<sup>th</sup> century drop dramatically, in terms of the number of countries involved, or the number

of days of conflict. The intensity of warfare, all the way to 1914, also dropped dramatically, and this is because supplying troops overseas became a monopoly of the British, because they alone have the naval power to actually expand colonially, and to prevent other people expanding colonially.

Why was it that the leading rivals of England between 1650, between the republic and 1914, were so slow to adopt the fiscal, military, and other policies pursued by this island? Why does not this example of an early and precocious transition to a modern, capitalist, indus-



trial market power take hold in Europe, or take hold at the pace that it does? Why does not it happen quicker in France, in Belgium, in Spain, or in Germany than it actually does? Britain had a number of advantages in relation to the rest of Europe. The rest of Europeans have always found it much more difficult, no matter how absolutist their monarchs pretended to be, to actually consolidate their gains from sovereignty. If you came to be absolute and sovereign you had to legislate for a tax or decree that there will be a tax and it will be universally applied across the territory that you claim to rule. There were very few countries in Europe that could do that before the middle of the 19<sup>th</sup> century, countries that could widely tap into whatever fiscal resources actually available to them. They found it much more difficult for all kinds of reasons –because they had lost so many wars and they were plagued by internal instabilities of various kinds– to maintain stability.

The British regime in the 19<sup>th</sup> century is ostensibly liberal but, socially and culturally, it is very hierarchical. The vote is not extended until very late in the period, and the English are extremely deferential to their monarch and to their aristocracy. We have this navy, so that before the buildup of the German Navy at the end of the 19<sup>th</sup> century, we do not have to worry at all about external security. Above all, we make most of the gains that are to be made from servicing the transnational economy. Who was it who funds transnational trade, international trade, which is the great center for banking, insurance, shipping, credit, commercial profiteering in the 19<sup>th</sup> century? Who are these gentlemen and the capitalists?

They come from all over Europe and they settled in London to make real money, some of which they invest in these industries in the north, and some of which they invest in the British service sector, which sells a very large

part of its output to the rest of the world. But the real money to be made is not in industry, it is not in making things; it is to be a successful middleman –a shipper, and, above all, in recent years, a banker. This is the way to make money, make real money. That's what is meant by English gentlemanly capitalism. We are ruled by aristocrats, ruled by gentlemen, and ruled by a plutocracy throughout the 19<sup>th</sup> century, although the 20<sup>th</sup> century would be different.

The rest of Europe is not able to create fiscal systems of the same power and the same extractive capacity as Britain. The British are somewhat more democratic, there is more compliance with demands for taxes but, if you keep winning wars, of course you're going to pay taxes to win the wars. If you get rather high rates and safe rates of interest from the government, you're going to lend money to governments who actually win wars.

On the mainland of Europe, there is continuous and persistent regional resistance, which is now re-emerging. Nobody likes the centralization and the universalization of taxes. It is bitterly resisted, so the central state is seen by large parts of Europe in much the same way as Britain sees Brussels at the present time: an extractor of revenues for no good reason. Secondly, the administration for taxes. If you look at the administrations on the mainland, a lot more taxes are collected than actually ever reach the capital city because it is siphoned off, it is corrupted away in various ways, or it deliberately has to be spent locally, as it happens in England regarding Scotland.

But that sort of thing, the Scottish issue, is absolutely commonplace throughout France for most of the 19<sup>th</sup> century. It is also commonplace in Italy, and commonplace in very large parts of Europe where fiscal autonomies actually survive in various forms, so that there



is not a centralized fiscal state but a federation of fiscal units that are called a state. This is not the most efficient way to run a state. What the republican regime showed was that Britain possessed the political, after they had executed their king, the fiscal, the natural, and the other advantages required, and fiscal centralization comes very gradually to Europe, so the 19<sup>th</sup> century story of Europe is the very slow construction in the wake of the Napoleonic Wars, which was a centralizing vent for most places in Europe, including Spain, of a fiscal system that is central and which provides the state with enough taxes so it can act positively to provide the public goods and the markets, the framework of markets that is required for growth.

But why is it that great Oriental empires are so retarded economically for such a long time? The answer is that they do not manage, ever, to obtain anything like the access that we Europeans have managed to obtain to taxation, so they do not ever have the same fiscal capacity as in Europe. Throughout most of the 18<sup>th</sup> century, with a population that is 20 times the size of Britain, the Chinese Ming-Qing regime collects less taxes than the British state.

On a per capita basis, the Chinese state, the Ottoman dominions, and, above all, the Mughal Empire collect pathetically small amounts of money. So, these vast empires look like states but they cannot provide neither social overhead capital nor defense. They do not have the resources. Even though they know what needs to be done to catch up, both geopolitically and economically, they simply never manage to construct a fiscal state.

Looking at these great empires, the amount of taxes that they are able to collect is really low by European standards, and particularly by British standards. One of the hypothesis is that Western states, led by Britain, succeeded

## Bio



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Estudió Economía en la London School of Economics (LSE) y se doctoró en la Universidad de Oxford. Fue profesor en Oxford durante dos décadas hasta su nombramiento como director del Institute of Historical Research, en Londres y a partir de 1998 fue nombrado *centennial professor* en la LSE, donde en la actualidad es profesor emérito de Historia Económica. Ha sido director de Historical Research y presidente de la Economic History Society. Es miembro de la British Academy y de la Royal Historical Society. Ha sido profesor visitante en numerosas universidades y es doctor *honoris causa* por las Universidades Carlos III y de Uppsala. Autor de numerosas publicaciones de Historia Económica Internacional de las cuales la más reciente es *The Rise of Fiscal States: A Global History, 1500-1914* (Cambridge University Press, 2012).

in centralizing command over their sovereign revenues much more effectively and much earlier than the bureaucracies in charge of the imperial systems of China, of India, of the Ottoman dominions. It seems that the German Historical School, who always had the state at the center of their explanations for economic growth, had a very big point to make, and that point is only now being realized even by the economics profession.