

# How did states further the rise of the Great Divergence?

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The debate on the Great Divergence is bound to continue; not even the publication of *Escaping Poverty* by Peer Vries, an inspiring interpretation of the dominant strands in the debate, will change this.<sup>1</sup> The metaphor for the growing global contrasts that emerged in per capita economic growth and prosperity in the nineteenth century is simply too appealing. Yet the content of the debate will surely change. *Escaping Poverty* shows how the debate on the Great Divergence has undergone a gradual shift from being about ‘coal and colonies’ to being about ‘institutions and the state’; something that is especially visible in Chapters 20 and 25, which are entitled *Ultimate causes: institutions* and *The institution of institutions: The role of the state, in particular that of Britain*, respectively. So far, however, clear answers are lacking on the crucial questions of how the British state might have stimulated the Industrial Revolution, and how state institutions might further modern economic growth in general, above all before the development of powerful state establishments in the nineteenth century. This article analyzes the difficulties encountered in the search for more convincing answers, and addresses the question of how and to what degree central states might have influenced the rise of the Great Divergence.

## 1 The problem of obscure definitions

The historical overview of the debate given in *Escaping Poverty* by Peer Vries employs a number of concepts in relation to the Great Divergence –

<sup>1</sup> Peer Vries, *Escaping poverty. The origins of modern economic growth* (Vienna and Göttingen 2013).

'inclusive institutions', 'fiscal-military state', 'mercantilism' – all of which seem to work to the advantage of Britain and to the disadvantage of China. Upon closer inspection, however, the comparison is rather distorted, based upon weakly defined concepts that reveal a certain degree of Anglo-centrism. This has a detrimental effect on the debate (Britain stands for the 'West' and China for the 'Rest'), all the more so since several distinguishing features seem to be typical of Britain (and not of 'Europe') and of the time period between 1750 and 1850.

Let me start with 'inclusive institutions'. For several decades, a number of prominent scholars of the New Institutional Economics have been addressing the role played by the state and institutions in economic growth. Their work has yielded rich insights, in particular with regard to the regulation of transaction costs that tend to hamper trade.<sup>2</sup> Their instruments do not always allow for straightforward long-term comparisons across the globe, however. Take, for example, the work of Daron Acemoglu and James Robinson, *Why Nations Fail*. They regard 'inclusive economic institutions' as conducive to economic growth, since they 'enforce property rights, create a level playing field, and encourage technologies and skills'. Extractive institutions, by contrast, are rent-seeking, through resource extraction from the many by the few. A proper, solid definition of these terms is lacking, however.<sup>3</sup> Since property rights are not defined either, this results in circular reasoning: inclusive institutions further economic growth in the longer term, and because there is economic growth in the longer term, the institutions are inclusive.<sup>4</sup>

Thus according to Acemoglu and Robinson, Chinese institutions were extractive in the eighteenth century and were unable to promote economic growth in the longer term.<sup>5</sup> Yet can one really describe a state that has the benevolent aim of keeping taxes low for the masses of the peasantry as truly 'extractive', whilst closing one's eyes to the rent-seeking aspects of the British state at this time (see further below)? Moreover, there was nothing wrong with the enforcement of property rights for the peasantry under the Qing, who protected smallholders in general and used incentives to stimulate the colonization of less populated areas.<sup>6</sup> By contrast, the peasantry in

2 Douglass North, *Structure and change in economic history* (New York 1981).

3 Daron Acemoglu and James A. Robinson, *Why nations fail: the origins of power, prosperity, and poverty* (London 2012) 429. On the notion of the 'level playing field', see below.

4 See a similar criticism by Vries, *Escaping Poverty*, 126.

5 Acemoglu and Robinson, *Why nations fail*, 231 and 439.

6 Kenneth Pomeranz, 'The land market in late imperial and republican China', *Continuity and Change* 22 (2008) 1-50.

Britain, which according to Acemoglu and Robinson were under the rule of the most advanced ‘inclusive institutions’ of the time, suffered from a lack of cadastral surveys and from poor (customary) property rights on their lands. Enclosure (a typical *rent-seeking* phenomenon) and the high costs of lawsuits furthered the accumulation of land and wealth by the propertied classes at the expense of those with a limited amount of property.<sup>7</sup> *Some* property rights were enforced, whilst others seem to have been disregarded; *some* people gained inclusive rights whereas others were deliberately excluded. Without taking such class-related aspects into account, the terms used by Acemoglu and Robinson obscure more than they reveal.

A similar problem afflicts the ‘fiscal-military state’, a concept that is also seriously under-defined. John Brewer, who coined this concept in his groundbreaking *Sinews of power*, did not provide a clear definition, but referred to the *English* version of the fiscal-military state.<sup>8</sup> The provenance of his term ‘fiscal’ is quite obvious, being derived from the Schumpeterian notion of the ‘tax state’ that is characterized by the extraction of resources for the state through taxes, in contrast to revenues from the ‘crown domains’, which had been the dominant mode of extraction for the medieval ‘domain states’.<sup>9</sup> The term ‘military’ refers to the debate on the Military Revolution, with the concomitant rise of larger and more permanent armies and navies.<sup>10</sup>

After the publication of *The sinews of power*, other historians applied the concept of the fiscal-military state to Spain, the Dutch Republic, Russia, Austria, Ethiopia and Savoy, among others, all obviously less efficient than Britain. Savoy could only survive thanks to subsidies from other states, for example, and several of these ‘fiscal-military states’ did not even develop a

7 Eric L. Jones, ‘Economics without history: objections to the rights hypothesis’, *Continuity and Change* 28:3 (2013) 323–346; Andy Wood, *The memory of the people: custom and popular senses of the past in early modern England* (Cambridge 2014). Enclosure did not contribute to economic progress overall; see Allen, *The British Industrial Revolution*, 126. Intellectual property rights and patents were a mixed blessing at most, since not all patentees were the best suited to developing a device, and secrecy considerably undermined the spread of innovations; see Joel Mokyr, *The enlightened economy: Britain and the Industrial Revolution, 1700–1850* (New Haven 2011) 403–405.

8 John Brewer, *The sinews of power: War, money, and the English state, 1688–1783* (New York 1989) 27, 250; Julian Hoppit, ‘The nation, the state, and the first industrial revolution’, *Journal of British Studies* 50 (2011) 325.

9 Joseph Schumpeter, *Die Krise des Steuerstaats* (Graz 1918).

10 Richard Bonney, ‘Introduction’, in: Idem (ed.), *The rise of the fiscal state c.1200–1815* (Oxford 1999) 13.

proper system of public debt.<sup>11</sup> In *Escaping Poverty*, Peer Vries typically uses the ‘English model’ of the fiscal-military state as the standard.<sup>12</sup> China is thus excluded from the concept by definition; yet it should be included, being the world’s first tax state, with its roots in the successful Qin state of the fourth century BCE and with capacities that were further improved during the eight-century Song dynasty.<sup>13</sup> Recent research shows that East Asia was involved in a military revolution, too, which resulted in the use of innovative arms and tactics with linkages to taxation and state-formation.<sup>14</sup> Furthermore, China’s taxes applied to almost every inhabitant of the country, with virtually no exemptions or privileges for specific classes or groups (in contrast to England and almost all European states), within a large territory that was kept firmly under control by a meritocratic bureaucracy (and not through patronage, as in England and most European states). When wars affected part of the territory, the revenues of the remainder of China continued to support the state thanks to economies of scale, which recurrently reinforced Chinese hegemonic claims in Eastern Eurasia. The British fiscal state, by contrast, was only firmly established during the 1750s. The imposition of novel, highly regressive taxes (above all, excises) was accompanied by widespread unrest, since these taxes laid a particular burden on the lower classes. The state budget ran almost continuously at a deficit, whereas Chinese state budgets operated at that

11 Jan Glete, *War and the state in early modern Europe. Spain, the Dutch Republic and Sweden as fiscal-military states, 1500-1660* (London 2002); Christopher Storrs (ed.), *The fiscal-military state in eighteenth century Europe. Essays in honour of P.G.M. Dickson* (Surrey and Burlington 2009); Rafael Torres Sánchez (ed.), *War, state, and development. Fiscal-military states in the eighteenth century* (Pamplona 2007), in particular the contributions of Agustín González Enciso, ‘Foreword’, 9 and Rafael Torres Sánchez, ‘The triumph of the fiscal-military state in the eighteenth century’, 16.

12 Vries, *Escaping poverty*, 375.

13 Kent G. Deng, ‘The continuation and efficiency of the Chinese fiscal state’, in: Bartolomé Yun-Casalilla, Patrick K. O’Brien and Francisco Comín Comín (eds.), *The rise of fiscal states: A global history, 1500-1914* (Cambridge 2012) 335-352, 338; Victoria Tin-Bor Hui, *War and state formation in ancient China and early modern Europe* (Cambridge 2005) 81.

14 Peter C. Perdue, *China marches West. The Qing conquest of Central Eurasia* (Cambridge MA, 2005) 539; Joanna Waley-Cohen, *The culture of war in China. Empire and the military under the Qing Dynasty* (London and New York 2006); Peter Allan Lorge, *The Asian military revolution. From gunpowder to the bomb* (Cambridge 2008); Tonio Andrade, Hyeok Hkweon Kang and Kirsten Cooper, ‘A Korean military revolution? Parallel military innovations in East Asia and Europe’, *Journal of World History* 25 (2014) 51-84.

time with massive, regular surpluses, at least up until the late 1790s.<sup>15</sup> The imposition of taxes was by no means as uniform throughout Britain as has been assumed, since Scotland and Ireland paid far below their capacity as compared to England, due to the threat of secessionist movements.<sup>16</sup> Like numerous other European states, Britain was still a 'composite state', not a unified whole.<sup>17</sup> With regard to the British Empire as a whole, the state obviously exerted little control over the more peripheral territories overseas. The attempt to tax the American colonies had even resulted in a glaring defeat for Britain in the 1780s, leading to the independence of the United States and the loss of a massive potential economy-of-scale revenue machine. In addition, British power was entrenched in the European state system and always needed allies to defeat its arch-enemy, France, whereas China could maintain a centuries-long hegemony in East Asia on its own.<sup>18</sup>

Another obscure term is mercantilism, a true zombie-term in view of its repeated burials and revivals by historians. In *Escaping Poverty*, the term seems to be on the rise again. Peer Vries suggests the following definition: 'a broader set of measures that basically had in common that they were meant to support the national economy'.<sup>19</sup> Viewed in this way, however, China obviously belongs to this category, too. Its rulers furthered the colonization of less populated districts, maintained canals and rivers through impressive campaigns, preserved a nationwide granary system to prevent famines, and strictly regulated foreign trade, all with the aim of strengthening the national economy.<sup>20</sup>

Even then, I wonder whether such a 'benevolent' interpretation of mer-

15 The British budget deficits caused the rise of public debt; see Brewer, *The sinews of power*, 67, 75; see also Lawrence Stone, 'Introduction', in: Idem (ed.), *An imperial state at war. Britain from 1689 to 1815* (London and New York 1994) 10, on the tax burden and popular unrest. On China, see Deng, 'The continuation and efficiency', 345; Debin Ma, 'Rock, scissors, paper: the problem of incentives and information in the traditional Chinese state and the origin of the Great Divergence', *LSE Working Paper 152/11* (2011) 24.

16 Brewer, *The sinews of power*, 152; Nicholas Canny, 'Irish resistance to empire, 1641, 1690 and 1798', in: Lawrence Stone (ed.), *An imperial state at war. Britain from 1689 to 1815* (London and New York 1994) 314.

17 Hoppit, 'The nation', 308-310, 329; J.H. Elliott, 'A Europe of composite monarchies', *Past & Present* 137 (1992) 48-71. The major advantage of the 1707 Act of Union seems to have been that England was not hampered by hostile acts from Scotland; see Storrs, 'Introduction', in: Idem (ed.), *The fiscal-military state*, 5.

18 Brewer, *The sinews of power*, 177-178.

19 Vries, *Escaping poverty*, 371.

20 R. Bin Wong, *China transformed. Historical change and the limits of European experience* (Ithaca 1997) 113, 137; William T. Rowe, *China's last empire. The great Qing* (Cambridge and London 2009) 123.

cantilism is adequate for Britain. Institutions such as the East India Company and the Bank of England were founded with truly *rent-seeking* and *extractive* motives: their primary aim was to raise war funds for the state, not to develop the national economy.<sup>21</sup> The fact that in due course the Bank of England acted as a powerful buffer during monetary crises (see also below) was a typical unintended consequence of a typical rent-seeking action. The oft-mentioned assumption that foreign trade profited from imperialist expansion is dubious, too: trade with the United States did not drop at all after the War of Independence.<sup>22</sup>

The content of the debate must surely benefit from ‘purging’ the concepts of the most rabid Anglo centrism. Eighteenth-century China was a reasonably well developed fiscal-military state, with an efficient, nationwide tax system that yielded annual surpluses more often than not. It ensured proper property rights for the large masses of the peasantry and supported considerable economic development, albeit one that was Smithian in character. In many respects, China resembled European states. On the other hand, Britain was not the ideal fiscal-military state in all respects. Its fiscal system avoided taxing the wealthier groups in society and overburdened the lower classes; its budgets suffered from recurrent deficits; its mercantilist measures were strongly rent-seeking in character; the inclusive institutions of the peasantry were destroyed. Yet such insights still do not answer the crucial question: was there a connection between the policies of the central state and economic development?

## 2 Local dimensions of early-modern economic growth

In this respect, the debate suffers from the use of an anachronistic notion of the state.<sup>23</sup> The Industrial Revolution is frequently analyzed in its national context, but the ‘central state’ did not exert much impact on society at all.

21 Bruce C. Carruthers, *City of capital. Politics and markets in the English financial revolution* (Princeton 1996) 140; Isaac de Pinto, *An essay on circulation and credit in four parts and a letter on the jealousy of commerce* (London 1774) 20; Robert B. Ekelund and Robert D. Tollison, *Mercantilism as a rent-seeking society* (College Station 1981); Mancur Olson, *The rise and decline of nations* (New Haven 1982).

22 Moreover, the evidence points to the gradual weakening of mercantilist policies after the middle of the eighteenth century, which renders the concept less applicable after the 1780s. At the same time, corruption also seems to have been on the decline. Mokyr, *The enlightened economy*, 163, 393, 396, 424.

23 Vries, *Escaping poverty*, 358-376.

The eighteenth and the nineteenth centuries saw the *emergence* of the modern, territorial and eventually also the national state, but by the 1750s it was still *emerging*, with the waging of war and the extraction of taxes as its main tasks, with rare involvements in either agriculture or industry.<sup>24</sup>

The Industrial Revolution was a localized event, at least until the coming of the railway.<sup>25</sup> The British government deliberately refrained from influencing local economic arrangements and left most of the power for carrying out day-to-day procedures to local governments, which were still dependent upon the willing service of the local gentry. In fact, like most of continental Europe, the country consisted of a patchwork of numerous 'polities' and autonomous corporations that exercised some form of political independence. The interaction with the central state increased only gradually, above all during the political crisis of the 1780s caused by the disaster of the War of American Independence, when leading members of small-scale communities invigorated local governance, which then developed in tandem with the growing power of the central state.<sup>26</sup>

The context of the 'local state' provided the diverse political and societal framework that was needed for the spread of 'public science'; it was responsible for education and skills, and also furthered the diffusion of knowledge on all kinds of subjects. Public lectures by instrument-makers, local schoolmasters and others were given all over the country, on topics such as mechanics, mathematics and chemistry.<sup>27</sup> This was in fact the most important *level playing field*, to use Acemoglu and Robinson's term, with the difference that it had existed before the rise of Leviathan.

Such insights are helpful in the comparison with China, where the central state also deliberately left the arrangement of almost all local matters to the local authorities. The situation was different, however, with regard to the spread of knowledge. Most knowledge was accumulated within the state educational institutions, which tended to reinforce the dominance of

24 Lars Magnusson, *Nation, state and the Industrial Revolution: the visible hand* (London 2009) 10; E.P. Hennock, 'Central/local government relations in England: an outline 1800-1950', *Urban History Yearbook* (1982) 38-49; Hoppit, 'The nation', 317.

25 Robert C. Allen, *The British Industrial Revolution in global perspective* (Cambridge 2009) 141-149.

26 Joanna Innes, *Inferior politics. Social problems and social policies in eighteenth-century Britain* (Oxford 2009) 85-86, 96-127, 179-226.

27 R. Pearson and D. Richardson, 'Business networking in the Industrial Revolution', *The Economic History Review* 54 (2001) 657-679, 667; Joel Mokyr, 'Introduction', in Idem (ed.), *The economics of the Industrial Revolution* (Lanham, MD 1985) 12-15; Mokyr, *The enlightened economy*, 51.

existing cognitive traditions.<sup>28</sup> Another problem was the serious underfunding of Chinese local governments, which worsened considerably during the monetary crisis of the early nineteenth century. The worldwide drop in the supply of silver caused strong fluctuations in the value of the Chinese money of account, causing a massive plunge in tax yields. Corruption soared as extralegal taxation by local officials increased,<sup>29</sup> undermining the level playing field in communities even further and thus hampering the exchange and application of new notions and ideas.

A similar monetary crisis was averted in England thanks to the Bank of England and the ability to contract loans based upon the powerful excises. Indirect duties such as these, levied upon a large number of consumption goods, were much more flexible than direct taxes on land, such as those used in China, since harvests do not increase all of a sudden and the duties cannot be raised continually.<sup>30</sup> English public loans were raised even during wars, thanks to the increases on rather small excises whose proceeds ensured the payment of interest for the time being. Loans also tended to spread the burden of war over a longer period of time, resulting in a lower degree of war-induced disruption for society at large. The supposed 'crowding out' effects of such massive public debt were limited, since there was no increase in interest rates. The market for government securities even stimulated the rise of entrepreneurs' bonds.<sup>31</sup> The regular procurement of funds for the army and navy meant that private entrepreneurs working for the military were paid on time, which stimulated the tapping of 'additional resources of human, financial, and commercial capital which the state was unable to mobilize', also at the local level.<sup>32</sup> The *public debt-cum*

28 Karel Davids, 'River control and the evolution of knowledge: a comparison between regions in China and Europe, c. 1400-1850', *Journal of Global History* 1 (2006) 59-79.

29 Rowe, *China's last empire*, 52; Wenkai He, *Paths toward the modern fiscal state: England (1642-1752), Japan (1868-1895), and China (1850-1911)* (Cambridge, MA 2013) 18, 122 ff; Rowe, *China's last empire*, 158; Ma, 'Rock, scissors, paper', 26-28; see also Vries, *Escaping poverty*, 331 and 406.

30 Charles Tilly, *Coercion, capital and European states: AD 990 -1992* (Oxford 1990) 87-89.

31 Larry Neal, 'How it all began: the monetary and financial architecture of Europe during the first global capital markets, 1648-1815', *Financial History Review* 7 (2000) 117-140.

32 Aaron Graham, 'Public service and private profit: British fiscal-military entrepreneurship overseas', in Jeff Fynn-Paul (ed.), *War, entrepreneurs and the state in Europe and the Mediterranean* (Leiden 2014) 108; for similar developments in the Netherlands see Marjolein 't Hart, *The Dutch wars of independence. Warfare and commerce in the Netherlands, 1570-1680* (London 2014) 97, 165.

*excises* solution rendered the bonds between the propertied classes and the state even stronger.<sup>33</sup>

Yet the British trump card of using public loans based on excises worked only because of ongoing urbanization. Excises thrive only in commercialized, highly urbanized societies, and the fact that at this time urbanization continued at a rapid rate in Britain (in contrast to China, and even in contrast to continental Europe) explains the country's ability to continue to contract debts, also during the Napoleonic wars.<sup>34</sup> Thus even in relation to the fruitful excises policy, the role of local circumstances weighs much heavier than assumed.

### 3 The complicated relationship between states and the Great Divergence

Urbanization and local networks, or the lack thereof, have been underrepresented in the debate on the Great Divergence to date. No single book can be expected to deal with all aspects, of course, not even *Escaping Poverty*. I hope to have shown how future research might enrich the field by focusing more often on the role of local actors and their networks, the interaction between local and central authorities, and avoiding the use of loaded concepts such as inclusive institutions, fiscal-military states and mercantilism.

Overall, the early modern central state had a limited impact on the economy (quite the opposite is true in relation to the economy's impact on the state!<sup>35</sup>). Public debt and taxes had very little direct bearing on economic performance. Suppose China had won the Opium War; suppose the Chinese fiscal-military state had remained as powerful as it had been

33 P.J. Cain and A.G. Hopkins, *British imperialism. Innovation and expansion, 1688-1914* (London and New York 1993) 65; Carruthers, *City of capital*, 157-159. On the difficulties to tap the resources of the rich through taxation, see also Thomas Piketty, *Capital in the twenty-first century* (Cambridge, MA 2014).

34 E.A. Wrigley, 'Urban growth in early modern England: food, fuel and transport', *Past and Present* no. 225 (2014) 102; Patrick O'Brien, 'The triumph and denouement of the British fiscal state: taxation for the wars against revolutionary and Napoleonic France', in Storrs (ed.), *The fiscal-military state*, 192. On the lack of urbanization in China: G. William Skinner (ed.), *The city in late imperial China* (Stanford 1997) 226. A comparison with the Dutch Republic is revealing: in the seventeenth century, warfare had also been financed through public debt supported by an incremental increase in excises, enabled by growing urbanization. When urbanization slackened, the Dutch fiscal-military state lost its vigor; see Marjolein 't Hart, *The making of a bourgeois state. War, politics and finance in the Dutch Revolt* (Manchester 1993) 138-140.

35 See O'Brien, 'The triumph'.

during the eighteenth century: the Great Divergence would have continued nevertheless. The most important link is an indirect one: Britain managed to reduce the burden of war on the state and thus did not disrupt the growing bonds between local communities, local governments and the central state. Thanks to the flexibility of the fiscal system that became fully mature in the 1750s, supported by ongoing urbanization, the state did considerably *less* harm to society during wars than it had done in the seventeenth century.<sup>36</sup> China's financial problems had a nationwide impact due to its less flexible land taxes, and thus undermined potential local level playing fields, even destroying the famous policy to provide grain during famines.

The focus on the central state fails to acknowledge the true role of the level playing field within local communities in Britain, supported by local government and after 1780 also increasingly by the central state, and overlooks the contribution made by growing urbanization to the flexibility of the taxes at the central level. In his final chapter, Peer Vries mentions emulation as a possible solution to the problem of explaining the Great Divergence.<sup>37</sup> Unfortunately, he stresses only emulation between states. At least until the early decades of the nineteenth century, local political power, local emulation, and urbanization constituted crucial driving forces for economic development.<sup>38</sup>

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<sup>36</sup> See also Marjolein 't Hart, 'From the Eighty Years War to the Second World War: new perspectives on the economic effects of war', *Low Countries Journal of Social and Economic History* (TSEG) 11:2 (2014) 261-280.

<sup>37</sup> Vries, *Escaping poverty*, 434.

<sup>38</sup> On the substantial political power of European urban communities compared to the Chinese ones, see Wim Blockmans and Marjolein 't Hart, 'Power', in: Peter Clark (ed.), *Oxford Handbook of Cities in World History* (Oxford 2013) 421-437.

World War: new perspectives on the economic effects of war', *Low Countries Journal of Social and Economic History* (TSEG) 2014; and Karel Davids and Marjolein 't Hart (eds.), *De wereld en Nederland. Een sociale en economische geschiedenis van de laatste duizend jaar* (Amsterdam 2011). See: <https://www.huygens.knaw.nl/t-hart-marjolein>  
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