INTRODUCTION

Institutional Change, Nineteenth-Century Growth, and the Early Modern Legacy

WHEN THE ENGLISH STATISTICIAN Gregory King drew up the first comparative statement of per capita income within England, France, and the Dutch Republic at the end of the seventeenth century, the economic achievements and derived political leverage of the United Provinces had already been distinctive for several decades.[1] Since the 1580s, their technical prowess, financial strength, and commercial preponderance had baffled and worried foreign observers from Thomas Mun to Jean-Baptiste Colbert. Productivity, per capita income, and investment had experienced a structural increase—a process which, as King acknowledged, had made Holland by far the most prosperous region within Europe by the end of the seventeenth century. Rooted in a long history of agricultural development related to early urbanization and in ecological changes that made arable agriculture on increasingly marginal (peat) lands difficult to practice, farming in the provinces of the western and northern part of the country over the course of the fifteenth, sixteenth, and early seventeenth centuries became geared to specific parts of market demand, with an emphasis on raising livestock and dairy produce. Even more famously spectacular were changes at the other end of the reallocation process, that is, in services. Substitution of imported grain for homegrown cereals linked agrarian change to an original expansion in commerce and shipping. Yet it was only with the exploitation of the wider complementarity of especially Baltic and southern European supply and demand patterns, and the organization of "rich trades" based on colonial expansion, that Dutch overseas commerce evolved into the active entrepôt system that would serve as the hub of world trade and finance for over a century and a half. Based on a mixture of geographic advantage, shipbuilding innovations, financial instruments that lowered transaction costs, naval power, and an unrivaled stock of low-cost merchant shipping, Dutch merchants were able to extend their traditional dominance in Baltic bulk cargoes to include items such as spices, sugar, and textiles, all requiring close links with a wide range of processing industries.[2] Backward linkages between naval transport and ancillary industries, a human capital windfall from the skilled hands of immigrants fleeing the Habsburg provinces, reliable access to imported inputs, and a spate of technical change also helped foster the export-based growth of a labor-intensive industrial sector. By applying improved methods of using wind and peat energy and by modifying processing technologies in sectors such as textiles, paper-making, oil pressing, distilling, sawing, and ceramics, the productivity of labor and competitiveness in manufacturing soared. As a consequence, foreign and domestic labor was attracted to cities such as Leiden, Gouda, and Haarlem, where specialized branches of industry grew up.

From a wider perspective, Dutch primacy in international trade revolutionized the *économies mondes* inherited from the late sixteenth century. It transformed European colonial settlement in the Far East and the New World and established patterns of trade based on comparative efficiency by reducing risk and information asymmetry.[3] At the domestic level, it linked Dutch regional grain prices to the international market (thus dampening the variability of food prices), fostered an unparalleled division of labor, and established the role of formal factor and commodity markets.

The political and fiscal institutions underpinning these development characteristics were affected only to a limited extent by the economic changes after 1580. Rooted in resistance against the executive centralization, fiscal reforms, and religious strains of Habsburg rule, the Dutch Revolt that started in the 1570s served to consolidate "traditional" regional and urban privileges within a loose confederate alliance, rather than transforming the structure of politics. By limiting the leverage of central policy-making institutions and leaving sovereign power in the hands of the provincial states, the Dutch polity functioned on the basis of subsidiarity that acknowledged earlier prerogatives and the need for negotiated compromise over common interests. Because its decentralized structure was composed of a hierarchy of urban particularism and representation at the provincial level, the mechanics of the Republic's political system were defined only in part by its constitutional aspects. To a perhaps larger extent, they were forged by a changeable equilibrium in the allotment of powers, ruled over by the seemingly contradictory principles of provincial sovereignty and that of the union between the provinces, which was dominated by Holland. With the constitution of government specifying the sovereignty of the seven provinces, the provincial states were, in turn, mostly dominated by largely independent towns. But even in the more rural inland provinces, political opinion in the states typically balanced out. Moreover, while delegations of each of the "allies" held a single vote in the States General, and unanimity was prescribed in decisions of federal importance, that—contrary to the provincial states—it was in permanent session, dependent on the fiscal leverage of Holland, and physically close to the meeting place of the states of Holland and the quarters of its *stadtholder,* made monitoring costs over the inland delegates high, the distribution of power asymmetric, and the qualification of issues open to dispute.[4] With the effectively depoliticized Council of State left to preside over annual budget proposals and a reinterpreted position of what (except for the two northern provinces) was typically a joint *stadtholder* wielding power over numerous local appointments and the armed forces, the Dutch early modern system of executive rule functioned by an elaborate complex of largely informal checks and balances. Yet in defiance of forces pushing toward centralization, notably debt accumulation that placed pressure on the existing fiscal fragmentation and the recurrently changing political prominence of successive *stadtholders,* the Republic would continue to abide by this form of government for the duration of its existence. Indeed, as especially J. L. Price has propounded, it was only through such a limited set of central institutions that the context could be provided for formulating joint policy objectives while at the same time balancing the economic and political dominance of Holland against the political independence of the other sovereign provinces for more than two centuries.[5]

In contrast to its "anachronistic exceptionality" in political structure, the Habsburg Netherlands and the ensuing Dutch Republic, finally, are also held to have pioneered a revolution in public finance. Fueled initially by the wartime fiscal demands of Charles V, the regular imposition of province-wide excise and property taxes, formally earmarked as service annuities transferable on the open market, underwrote a smoothing of tax returns, the creation of long-term public debt, and the emergence of a market in negotiable securities.[6] After 1572 the rebellious provinces were increasingly able to command large sums with a high risk profile for relatively low rates of interest. The reverse implication was, of course, a comparatively unparalleled incidence of taxation and the introduction of fiscal redistribution as a principal bone of distributive contention between the various provinces. Given the commercial and financial preponderance of Holland, this "capital-intensive path of state formation" (in the terminology of Charles Tilly) provided an efficient way of raising funds beyond taxation by implying the strongest possible nonreneging commitment to bondholders, but at the same time was rooted in the fact that the underlying reform of public finance did not inaugurate the emergence of a nation-state.[7]

Despite being built upon a longer history of political and economic change, the Dutch economic and political ascendancy of the late sixteenth and early seventeenth centuries was nevertheless swift, hegemonic, and threatening to vested commercial interests. The Republic not only achieved dominance in trade, transport, and finance but also acquired the international leverage to promote and protect its adjoining policy objectives. But, at the time when its macroeconomic performance was assessed as part of King's exercise in political arithmetic, a change in its advanced path of development occurred, and the essential phenomenon of the period subsequent to King's inquiries was to be one of relative decline. While there has been largely unresolved debate over the precise pace and chronology, it is widely agreed that between the last quarter of the seventeenth century and the commercial disruptions of the Napoleonic era, the economy of Holland—and, by force of numbers, that of the Republic—

experienced a long-term standstill in productivity, a loss of international market share in commodity trade, and a decline in manufacturing output.[8] In parallel fashion, by the end of the eighteenth century Holland's international political stature had been reduced to little more than that set down in John Adams's famous metaphor of a squeaking frog caught between the legs of the two bulls engaged in the Anglo-French conflict.[9] Starting with the commercial disruption, aggravated fiscal imbalance, and rekindled political turbulence engendered by the Fourth Anglo-Dutch War of 1780–84, the years prior to the 1814–15 Treaty of Vienna saw not only overseas blockades and international monetary policies distorting commodity and capital flows but also Prussian and attempted British and French military invasions, fiscal exigencies, and finally the default of the state. Accordingly, it is a basic yet only rarely emphasized fact that the history of the early modern Dutch state is delimited not only by the events that occasioned its independence from Habsburg rule and, at the other end of the spectrum, a subordination to Napoleonic policy objectives after 1795, but simultaneously also by the rise and decline of its economic viability.

Such a conclusion is further enhanced by the evolution of scholarly exchange in the debate on the chronology and sectoral aspects of nineteenth-century industrialization. Few hypotheses in Dutch economic history have attracted as much scholarly discussion as that about the nation's late, or "retarded," transition to industrialized modernity, reflected in a piecemeal process of mechanization until the 1890s. From the first works addressing the issue—most famous is I. J. Brugmans's 1925 dissertation—to the authoritative 1968 work by De Jonge on industrial growth after 1850, the tendency is to associate this apparent lack of industrial dynamism with macroeconomic stagnation.[10] Yet in more recent years the historiography of nineteenth-century development has moved away from conflating a paucity of changes in mechanization and firm size with a lack of income growth. Starting with a range of books and papers by Griffiths, Bos, and De Meere published between 1979 and 1982, the notion of backwardness became questioned, and the focus of debate on industrial performance shifted from alleged entrepreneurial inertia and capital market failings to combined cost penalties resulting from transport and input costs related to natural resource endowments and from high wage levels, the result of early modern wage developments.[11] Moreover, modest growth in sectoral output and productivity was identified for the years after 1830. Instead of "backward" or "late," as Griffiths's 1980 inaugural lecture termed the issue, the Dutch development transition had been "different," its sectoral pattern having been marked by "balanced growth."[12] Finally, a recent succession of quantitative analyses of economic performance during this period have posited a drawn-out transition in the structure and causes of productivity change coming to full fruition after 1850. This new range of sectoral studies measuring changes in value added and factor-input combinations have argued for a modified chronology and broadened interpretational framework of Dutch economic development.[13]

In consequence, evaluated from either side of the turbulent 1795 to 1813 revolutionary period and within the context of disjointed historiographical debates, the present general consensus may be said to identify a chronological concurrence between a transition in the structure of economic performance and a realignment of executive government and fiscal accountability. Straddling the political turbulence and commercial disruption triggered by the Fourth Anglo-Dutch War and the institutional changes of the years after 1840, this phase saw the mechanisms of Dutch politics altered in a way seemingly at odds with all that had gone before, while simultaneously witnessing a transition in the structure of economic performance. A central message of this book is that this concurrence was not just chronological. Rather, it was deterministic. Far from being part of the separate realms of enlightened intellectualism and economic change that have been featured in the literature so far, both processes—the reorganization of the state and the observed pattern of economic development—were strongly interrelated. We will argue that a specific constellation of political power adapted from the early modern legacy and the post-Napoleonic settlement, shortsighted fiscal policy, tax distortions, and institutionalized failings in product markets together shaped the features of Dutch development in the early nineteenth century. The 1840 political crisis over public finance that ushered in debt conversion and constitutional reform was in the long run linked to another restructuring of the process of growth. As a result, after 1860 we witness the emergence of sectoral and distributive characteristics that fitted the typology formulated by Kuznets in the 1960s: that is, shifting sectoral output and employment shares, urban labor absorption, increasing real wages, an enhanced integration of markets through deregulation, and infrastructural change.[14]

These interrelationships were not limited to the phase between 1780 and 1848. Liberal democracy and emerging industrialization (after 1860) caused the emergence of new problems, such as the "social question," which required solution. This induced, after 1870, a series of developments into the direction of a new institutional structure that would have a great effect on the state (i.e., the emergence of the welfare state in the course of the twentieth century) and would shape the direction of economic change in the twentieth century. In this complex way, we establish indirect links between the dramatic changes that began after 1780, which demolished the old structure of the Republic, and the new sociopolitical and economic structures that would arise in the Netherlands in the twentieth century.

The theoretical basis for our assertion that reforms in the political sphere and in the institutional framework of economic life in general affected the development of the economy can be found in the extensive literature on institutional economics in the broadest sense. In this context, institutions are defined as the rules, laws, and customs that facilitate transactions. These vary from unwritten customs on a specific market (e.g., is bargaining permitted? how is the sales price determined?) to the laws of a country that regulate the property rights of market participants. One of the concerns of institutional economists is where these institutions come from and how specific institutions determine the structure of incentives that affect the behavior of the state, of entrepreneurs, and of workers. For example, Douglass North, perhaps the most influential theoretician in this area, defines the economic problem as the question of how cooperation between individuals can come about: How do market transactions develop that lead to division of labor and specialization? Which formal institutions—in the sense of laws implemented by the state and enforced by a judicial apparatus—and, at least as important, informal rules and customs guarantee the property rights of agents? And how do these institutions, these rules of the game of the market economy, change over time?[15] It is clear that the state—the organization that creates the statutory framework for market transactions—plays a fundamental role in this process of change. From this point of view, politics can be interpreted as the game to continuously modify these rules. The rules of this "meta-game" are, ultimately, determined by the constitution of the state. This document establishes the formal rules that determine how political relationships are defined and how changes can be made in these relationships.

Economics and politics, the economy and the state, are from this point of view closely linked to each other. The development of an economy is ultimately self-determined by the constitution of a country, which, after all, defines how the political game will be played. For example, it defines how the monarch and the parliament can affect the outcome of the political process and, consequently, how changes in institutions can come about.[16] Our book will investigate how close these relationships were. One central theme is the influence of the various constitutions of the Netherlands on economic development. This concerns the following stages of constitutional development:

- the decentralized state structure of the Republic, based on the Treaty of Utrecht of 1579;
- the establishment of a unified state in 1798;
- the formation of the Kingdom of the Netherlands between 1813 and 1815;
- the breakthrough of liberal democracy in 1840–48;
- fundamental reforms aimed at the extension of the franchise of 1887 and 1917

We will attempt to show that these sequential constitutions had a major influence on economic development during these periods in order to test and refine part of the program of the institutional economics. Moreover, this approach links up with another closely related school of economic thought: political economy. Economists from the generation of Tinbergen and Kuznets viewed the state as an independent umpire striving for the maximization of welfare, "the formulator of rules under which economic activity was to be carried out; as a referee . . . and as provider of infrastructure."[17] The essence of the new political economy (public choice) that has unraveled such myths is that the behavior of political actors is analyzed in an identical fashion to that of the participants in markets, assuming that they strive for the maximization of a specific public utility function, for power, prestige, budgets, or votes. During this process, they are also confronted with constraints, with scarcity. In the view of economists such as Downs, political entrepreneurs strive to be elected or reelected; to achieve this aim, they attempt to accommodate the preferences of the average voter (and in this way acquire the support of 50 percent of the electorate plus one). A change in the voting system, such as an extension of the franchise, can therefore have major consequences for the behavior of political entrepreneurs and, consequently, for the result of the political process. As a larger part of the population gains the right to vote, politicians who promote the interests of less prosperous population groups can count on greater support.[18] This mechanism will turn out to be very important for understanding political dynamics after 1870.

The state can be seen as the first layer of the institutional framework of an economy. The second institutional layer is the arena of collective action, of groups that have organized themselves with the aim of promoting their specific interests. In their rent-seeking they often require the support of the state; exerting influence on the political process is therefore one of the most important aims of these interest groups. In a stable society, Olson (in his classic work on political economy) expected a continuing increase in the number of interest groups that were able to organize themselves. This ultimately results in a process of institutional sclerosis, where the economic surplus will no longer be invested in growth and development but is completely consumed by the distributive coalitions that control the state apparatus.[19] This thought plays a role in our analysis of the decentralized state structure of the Republic, which is rooted in a relatively closely knit corporatist structure in which many interest groups had entered coalitions with the urban oligarchy (or parts thereof). The destruction of this corporatist society was one of the most important goals of the Batavian revolutionaries. Under the slogan "Freedom, Equality, and Brotherhood," they attempted to eliminate these corporatist structures; the abolishment of the guilds is an example of this process. As we will see, these reforms were only partly successful. The liberal reformers after 1840 still had to complete the process. The acceleration of economic development that began in the second half of the nineteenth century is, in our view, related to the liberalization of economic life that began after 1798 and was finally completed in the 1840s and 1850s. However, it is striking that this process was barely completed when the construction of new corporatist institutions—trade unions, farmers' organizations, employers' organizations—began. A phase of spontaneous, bottom-up, institutional renewal, which began after 1870, formed the basis for the corporatist structures that would characterize economic development in the twentieth century. While in the eighteenth century institutional sclerosis and economic inertia went hand in hand—which is in accordance with Olson's expectations—the growing corporatism of the first quarter of the twentieth century was in fact linked to an acceleration in economic growth, which does not agree with Olson's predictions.[20] Also at odds with his model is the fact that the emergence of new interest groups did not appear to be a continuous process—inherent to a stable society—but was concentrated in a relatively brief period (between 1890 and 1920). This, too, requires an explanation.

The third layer of analysis in the present book concerns the issue of how economic change was steered by these institutional changes and how it was in turn the cause of new institutional experiments. This analysis concentrates on the transition from a "stationary state" (characteristic of the eighteenth century) to the process of "modern economic growth" (beginning in the 1860s and 1870s). The first term, which refers to a stationary economy, was coined by the founder of economics, Adam Smith, who in his famous *Wealth of Nations* (1776) typified the economic development of Holland in this way. This raises the question of how it was possible for this relatively modern market economy to achieve a virtually constant level of production and income during a period of approximately 150 years (between 1670 and 1820). Why was there no growth, based on technological and organizational progress, during this extended period? The second term, "modern economic growth," originates from the founder of long-term economic growth analysis, Simon Kuznets.[21] He showed how long-term growth in per capita income, the most important characteristic of modern economic growth, is closely related to processes of structural transformation of the economy, especially those characterized by the relative decline of agriculture and the expansion of industry and the services sector. These changes were also linked to the process of urbanization. The economic development after 1860 will be analyzed within this framework.

Focusing on these two concepts—a stationary state until 1820 and modern economic growth after 1860—introduces a risk of disregarding the intervening period. It is therefore important to pay a great deal of attention to explaining the deviating development of the Netherlands during the first half of the nineteenth century. The explanation, as one could expect on the basis of the preceding, can primarily be sought in the specific institutional development of the Netherlands during this period.

Although this book concentrates on the endogenous forces that gave shape to the processes of economic and institutional change, we certainly cannot ignore the external influences that affected this small country. The decline of the Republic after 1780 was initially the result of the dramatic end to the naval war with the British (1780–84), the Prussian intervention (1787), and the French occupation (1794–95). In other words, it was the result of the incapacity of the

Republic to sustain itself within the European state system, which, as Tilly has pointed out, was characterized by warfare and preparation for war.[22] This relative decline undermined the legitimacy of its form of government and led to attempts to implement drastic reforms, first by the Patriots and later by the Batavian revolutionaries. Between 1814 and 1815, the major European powers intervened in another way by expanding the state to include the southern provinces of the Low Countries. The relatively independent position that the Republic was still able to occupy as a "great power" was lost after 1815, and the kingdom realized at important moments that it was especially dependent on its "most natural ally," Great Britain (which, for example, returned some of the colonies after 1815 and also continued to supervise how the Netherlands exercised this colonial authority).[23] To a certain extent, the Netherlands became a "client" of the powerful Albion and had to explicitly adapt important aspects of its international policy to the demands of this power on the other side of the North Sea. But like every client, the Netherlands attempted to optimally utilize the latitude it was given by this complex relationship.

Of a somewhat different order were the economic forces of the world economy that acted on a small, open economy. These included not only changes in relative prices—the result of industrialization elsewhere—or the growing demand for agricultural products in these newly industrialized regions but also the waves of cyclically increasing and decreasing protectionism. One of the causes of the relative decline of the Republic after 1670 was the emergence of mercantilism, especially in the England of Cromwell and the Stuarts and in the France of Colbert and Louis XIV. This protectionism, in varying disguises, would thrive until the mid–nineteenth century, only to make way for free trade after 1846, when the Corn Laws were abolished. Free trade would again come under pressure due to the agricultural depression after 1873. Here as well, the question arises of how the institutions called into life by the government—in the form of import and export duties and other measures focusing on promoting domestic industry—affected economic development in this small, open economy.

Despite these important exogenous influences, institutional developments in the Netherlands during the period 1780–1914 displayed a high degree of "path dependency," which brings us to another fundamental aim of the analysis that follows.[24] The generations of politicians who shaped the development of this state, from the Patriots of the 1780s to the radical liberals of the 1890s, responded to the specific economic, political, and institutional problems with which they were confronted. The solutions they found for their problems often determined constraints and problems that then confronted the next generation of politicians. With some exaggeration, one could even state that parts of the Republic's economic inheritance, such as its capital wealth, its very productive agricultural sector, or its rich colonial possessions, would continue to dominate the evolution of the economy until deep into the twentieth century. Similarly, it took three generations of reformers—from the 1780s to the 1840s—to free the economy of the institutional sclerosis that was the sociopolitical inheritance of the Republic. The fact that the Dutch economy took its own path between 1780 and 1914 was to a large extent due to this specific inheritance. In this book, we will attempt to reconstruct this path in its depth and breadth.

An important aim of this book is to show the extent to which the economic history of the Netherlands can be rewritten based on the new insights offered by the new institutional economics. We are convinced that the most important characteristics of the specific path taken by the Dutch economy between 1780 and 1914—a path that has been debated by historians for generations—cannot be understood without these new insights. In addition, we provide a great deal of new information about the growth of incomes, production, employment, prices, wages, and other economic indicators. This information is essential to analyze the long-term development of the economy. We can do this because the present book is the final result of a major study into the national accounts of the period 1807–1913. This study, in the tradition of scholars such as Gregory King and Simon Kuznets, has been conducted during the past ten years at the universities of Amsterdam (Vrije Universiteit), Utrecht, and Groningen. It has resulted in a unique and consistent database concerning the national income and various aspects thereof, and is the quantitative basis for this book.[25] In this regard, we have not aimed at making an exhaustive quantitative analysis of this database; other publications are being prepared with this aim. An important objective of our book is to make the information about the economic developments during the nineteenth century accessible to a relatively broad readership, since this historical-quantitative research has led to many new insights about the exact course of economic modernization. During the process of researching and reconstructing the national accounts, however, we gradually realized that the ultimate determinants of economic development cannot be found in the growth accounts themselves but must be sought in the complex interaction between markets and institutions.