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Introduction

Power, Institutions, and Global Markets – Actors, Mechanisms, and Foundations of Worldwide Economic Integration, 1850–1930

Christof Dejung and Niels P. Petersson

The rapid expansion of world trade between 1850 and 1914, its difficult reconstruction during the 1920s and its subsequent decline during the Great Depression are key themes in the current historiography of economic globalisation.[1] Yet such scholarship has broadly focused on the changing volume of foreign trade between nation-states, on macroeconomic problems such as national tariff policies and on the history of the advancement of transport and communication technologies. There have been very few discussions of global trade development between the 1850s and the 1930s from the perspective of economic actors below the nation-state level, which is to say actors conducting trading operations in everyday business life. Likewise, economic and business historians have broadly neglected the institutional framework that both shapes and is shaped by the enterprises involved in such everyday trade.[2]

Through such a shift of focus, the contributions in the present volume strongly suggest that in the late nineteenth and early twentieth centuries,

[1] Among the numerous examples, it is perhaps helpful to refer to the work by the various contributors to Michael D. Bordo et al. (eds.), *Globalization in Historical Perspective* (Chicago, 2003) which in the 1990s began to complement older studies such as Albert G. Kenwood and Alan L. Lougheed, *The Growth of the International Economy 1820–2000: An Introductory Text* (4th edn. London, 1999).

[2] There are, of course, exceptions, which include, for example, Richard Tilly and Paul J. J. Welfens (eds.), *Economic Globalization, International Organizations and Crisis Management: Contemporary and Historical Perspectives on Growth, Impact and Evolutions of Major Organizations in an Interdependent World* (Berlin, 2000); Tilmann J. Röder, *Rechtsbildung im wirtschaftlichen 'Weltverkehr'. Das Erdbeben von San Francisco und die internationale Standardisierung von Vertragsbedingungen (1871–1914)* (Frankfurt a.M., 2006).

global economic integration was far more than the result of supply and demand and ever more efficient means of transport and communications. Rather, it was a fundamentally social process, one that would have been impossible without rules and institutions. Long-distance trade has always been an inherently risky business, requiring access to finance, reliable business partners in far-away countries, and protection of property rights under unfamiliar conditions and unforeseen circumstances. To these ends, market participants have developed conventions, sought standardisation and relied on mercantile law. Daniel W. Drezner has thus argued that the global economy's regulation 'is intrinsically important. Markets rely on rules, customs and institutions to work efficiently. Global Markets need global rules and institutions to work efficiently'.[3]

Recent writing in business history has underscored the importance of internationally operating firms for the establishment of global economic relations.[4] Yet for the most part such history has concentrated on entrepreneurial decision making and foreign investments without being very specific about either the social, cultural and political environments in which these enterprises operated or the norms and regulations underpinning their activities. In contrast, in other fields such as international history and legal history, there has been a growing interest in how institutions – rules, norms, regulations and organisations – evolve in settings beyond the nation-state.[5] Such research has also pointed to the important role played by nonstate actors in the development of institutions, these actors including merchants, banks, interest groups and internationally organised epistemic communities such as the community of international lawyers.[6]

[3] Daniel W. Drezner, *All Politics Is Global: Explaining International Regulatory Regimes* (Princeton, 2007), 6.

[4] See for instance John H. Dunning, *Multinational Enterprises and the Global Economy* (Wokingham, 1993); Geoffrey Jones, *Multinationals and Global Capitalism* (Oxford, 2005); Michael B. Miller, 'The Business Trip: Maritime Networks in the Twentieth Century', *Business History Review* 77 (2003), 1–32; Mira Wilkins, 'Multinational Enterprise to 1930. Discontinuities and Continuities', in Alfred D. Chandler and Bruce Mazlish (eds.), *Leviathans: Multinational Corporations and the New Global History* (Cambridge, 2005), 45–79.

[5] See, for example, Martin H. Geyer and Johannes Paulmann (eds.), *The Mechanics of Internationalism: Culture, Society and Politics from the 1840s to the First World War* (Oxford, 2001); Miloš Vec, *Recht und Normierung in der industriellen Revolution. Neue Strukturen der Normsetzung in Völkerrecht, staatlicher Gesetzgebung und gesellschaftlicher Selbstnormierung* (Frankfurt a.M., 2006).

[6] For a description of the role of nongovernmental organisations in shaping international relations in the twentieth century see Akira Iriye, *Global Community: The Role of International Organizations in the Making of the Contemporary World* (Berkeley, 2002).

The emergence of transnational institutions and organisations is complicated by the fact that they are in potential conflict with the control of states over national sovereignty and borders. In fact, international and intercontinental trade has always been a highly politicised activity. The processes of institutional development and economic integration thus need to be studied within their wider contexts. It is necessary to examine which actors have been involved and how they have contributed to the development of foreign commercial relations. Such a perspective has to take account of the interplay among state bureaucracies, internationally operating firms, stock and commodity exchanges, trade unions, peasants, and international and transnational organisations such as the League of Nations and the International Chamber of Commerce.

A focus on the creation of institutions by nongovernmental economic actors raises new questions about the periodisation of the history of economic globalisation. In particular, accounts of institutional continuity over time and the persistence of individual firms and internationally oriented institutional innovation in difficult periods of world trade may challenge the notion that we can clearly distinguish between eras of economic globalisation and deglobalisation. As a result, the First World War may appear as less of a watershed than in many historical accounts in which a period of Victorian and Edwardian globalisation is followed by deglobalisation in the interwar years.[7]

This volume addresses the question of how the rules and institutions that world markets needed to work efficiently came into being and evolved during the late nineteenth and early twentieth centuries, bringing together contributions from economic and business history, global and world history and legal history. It is informed by two sets of questions in particular. Firstly, which actors were most prominent in the creation of norms and institutions for global trade, and what were their interests, coalitions, conflicts and patterns of action? Second, how far should the First World War be seen as a turning point, dividing a period of rapid transnational

[7] For instance Hugo Ott, 'Kriegswirtschaft im 1. Weltkrieg – Ende der Weltwirtschaft?', in Jürgen Schneider et al. (eds.), *Wirtschaftskräfte und Wirtschaftswege. Festschrift für Herrmann Kellenbenz* (Bamberg, 1981), 505–24; Patrick Karl O'Brien, 'The Great War and the Dislocation of the International Economy 1914–1929', in Wilfried Feldenkirchen, Frauke Schönert-Röhlk and Günther Schulz (eds.), *Wirtschaft, Gesellschaft, Unternehmen. Festschrift für Hans Pohl zum 60. Geburtstag* (Stuttgart, 1995), 245–65; Eric Hobsbawm, *The Age of Extremes: The Short Twentieth Century, 1914–1991* (London, 1995); Ronald Findlay and Kevin H. O'Rourke, *Power and Plenty: Trade, War, and the World Economy in the Second Millennium* (Princeton, 2007), 429 ff.

integration from one of laborious, precarious and ultimately failed reconstruction, and to what extent or in what areas can a continuity of global integration be discerned between the two periods? In the remainder of this introduction, we take a closer look at the volume's three key concepts – institutions, power and global markets – and provide some reflections on the periodisation of economic globalisation between the 1850s and the 1930s.

The Importance of Institutions for Worldwide Economic Interaction

Intercontinental trade is an especially relevant topic for research on internationalism because it is associated with particularly high transaction and information costs; as institutional economics points out, these costs may be reduced by institutions or organisations that make interaction predictable and contracts enforceable. Indeed, already in the early twentieth century, the study of business organisation in international trade led scholars such as Austria's Josef Hellauer to analyse organisational phenomena with reference to factors such as principal-agent problems and information and transaction costs in much the same way as did later institutional economists.[8]

It may be useful to point out two 'structural facts' about economic transactions. The first of these is the fundamental problem of balancing security and efficiency. To maximise security, traders would have to deal only with known and trusted partners, directly and simultaneously exchanging goods or services against money. However, such a way of doing business would not be very efficient because it unduly restricts the choice of partners and limits the scope and speed of deals, thereby diminishing profits. In the real world, traders can subsist and thrive only if they deal with people they do not know, when for example they borrow money to finance deals, extend credit to their customers, sell goods they do net yet own and ship goods they have not yet sold. It is by doing just these things that intermediaries perform a useful service for which other people are willing to pay. Such practices increase both business volume and the turnover of funds, which means multiplying the profit to be made with a given amount of capital. The practices do, however, transform

[8] Josef Hellauer, *System der Welthandelslehre. Ein Lehr- und Handbuch des internationalen Handels. Erster Band: Allgemeine Welthandelslehre* (8th edn. Berlin, 1920, 1st edn. 1910). Hellauer's institutional focus did not prevent him from resorting to racist and 'culturalist' explanations for the actions of non-European businesspeople.

simple individual transactions into complex and interdependent networks of contractual relationships among a great number of highly specialised parties. When something goes wrong, disturbances can spread like a chain reaction through these networks, disrupting much more than individual transactions and possibly putting the existence of an entire business at risk. Increased efficiency often means increased risk. Awareness of these basic facts is evident from the anguished musings of a nineteenth-century 'mercantile Hamlet' recently unearthed by Hartmut Berghoff:

> To sell or not to sell?
> That is the question
> Whether it is better to send the goods
> And take the risk of doubtful payment,
> Or to make sure of what is in possession
> And, by declining, hold them.
> To sell; to ship; perchance to lose –
> Aye, there's the rub!
> For when the goods are gone,
> what charm can win them back
> From slippery debtors?
> Will bills be paid when due?
> Or, will the time stretch out till crack of doom?[9]

Many nineteenth-century innovations such as the credit rating agencies studied by Rowena Olegario in her contribution to this volume were designed to deal with such risks. Another solution was to substitute intra-firm transactions governed by hierarchy for market exchanges, as Ronald Coase has argued in a seminal paper.[10] In global trade, this could mean that merchant firms chose to open up company-owned agencies in far-off trading posts, thereby reducing transaction costs by bringing transactions under the control of their representatives. The contributions by Christof Dejung and Claude Markovits provide case studies of how traders on the Indian subcontinent tried to implement this strategy.

The second structural fact is the pronounced multilateral nature of trade and finance especially but by no means exclusively before 1914. It is well known that, from a macroeconomic perspective, multilateral clearing of balances of payment was an important contributor to growth

[9] Undated poem quoted in Peter R. Earling, *Whom to Trust: A Practical Treatise on Mercantile Credits* (Chicago, 1890), 200, here quoted from Hartmut Berghoff, 'Civilizing Capitalism? The Beginnings of Credit Rating in the United States and Germany', *GHI Bulletin*, 45 (2009), 9–28, 13.

[10] Ronald H. Coase, 'The Nature of the Firm', *Economica New Series* 4 (1937), 386–405.

and equilibrium in the prewar world economy.[11] From a microeconomic perspective, we see that, as a matter of unquestioned routine, *each individual commercial transaction* involved merchants, producers, brokers, transporters, insurers, banks and so forth from various countries or even continents, with contractual relationships thus usually stretching over several national jurisdictions. How did those involved in international business prevent things from going wrong or protect themselves if they did? Transactions on a global scale confront trading partners with particularly severe challenges. The huge distances they cover means that for a long time, goods will be in transit, entrusted to a third party, exposed to the considerable risks of long-distance transport, and under the control of neither the buyer nor the seller. Capital will be tied up in these goods and unavailable for other uses. There are likely to be cultural differences between the trading partners, as well as different understandings of key business practices and customs. Finally, buyers and sellers are likely to be situated in different nations with different legal systems. Similar risks are faced by those investing capital in ventures abroad or in railway, municipality and government bonds in far-off countries.

'New institutional economics' has addressed the question of how problems arising from such a situation – the enforcement of contracts, information asymmetries, principal-agent problems and so on – have been solved, bringing down transaction costs to an acceptable level. Following Douglass North, we may distinguish between formal and informal types of institution.[12] For a long time, international trade was marked by an absence of strong formal institutions. In an earlier age, traders had often relied on personal networks, kinship or religion to identify business partners they could trust.[13] As Timothy Guinanne has pointed out, trust is not an *explanans* but an *explanandum*. It results, for example, from knowledge about the trading partner or from a conviction that contracts can be enforced (a point supported by Claude Markovits's discussion in this volume of the credit networks of Indian firms).[14]

[11] Kenwood and Lougheed, *Growth of the International Economy*.

[12] Douglass C. North, *Institutions, Institutional Change and Economic Performance* (Cambridge, 1991). See also Mark Casson, 'Institutional Economics and Business History: A Way Forward', in Mark Casson and Mary B. Rose (eds.), *Institutions and the Evolution of Modern Business* (London, 1998), 151–71.

[13] A highly influential study has been Avner Greif, *Institutions and the Path to the Modern Economy: Lessons from Medieval Trade* (Cambridge, 2006).

[14] Timothy W. Guinnane, 'Trust: A Concept too Many', *Jahrbuch für Wirtschaftsgeschichte* (2005), 77–92.

However, as the cultural and geographical distance between trading partners increases, the foundations of such informal institutions become weaker or else even have to be created ex nihilo. This is precisely the situation created by the expanding late nineteenth-century world trade, which was taking place in a rapidly changing legal and institutional framework. Global markets were bringing together buyers, sellers and intermediaries with widely different cultural backgrounds, experiences, expectations and allegiances, as well as very heterogeneous ideas about the nature of the market in which they were participating. It thus became more important to create explicit sets of rules, either from scratch or based on precedents.

Both formal and informal institutions can be created by a variety of actors and in a variety of ways. Individual nation-states make laws for their national territory and for their colonial dependencies (see Chapter 7);[15] international conventions create laws valid in a number of states or that harmonise national legal rules (see Chapters 2, 3, 9, and 10); particular merchants' associations draw up standard contracts and codifications of mercantile custom (see Chapter 2); individual firms make agreements with agents in other parts of the world that are reinforced by personal ties and conceptions of honour (see Chapter 8); and business information is provided on a commercial basis (as examined in Chapter 4).

Our hypothesis is that institutions developed in complex negotiations between – in each case highly specific – sets of public and private, local, national and global actors. The rules and institutions that were discussed and sometimes implemented were of various types and status, among them national and international law, customary law, local customs, informal rules of the game and privately established orders. A tension was always manifest between the tendency of individual actors or networks to organise themselves, on the one hand,[16] and the claim of states and international organisations to create generally binding rules in their jurisdiction, on the other hand.

15 Wolfgang J. Mommsen and Jaap A. de Moor (eds.), *European Expansion and Law: The Encounter of European and Indigenous Law in 19th and 20th Century Africa and Asia* (Oxford, 1992); Lauren Benton, *Law and Colonial Cultures: Legal Regimes in World History, 1400–1900* (Cambridge, 2002); Helmut Janssen, *Die Übertragung von Rechtsvorstellungen auf fremde Kulturen am Beispiel des englischen Kolonialrechts. Ein Beitrag zur Rechtsvergleichung* (Tübingen, 2000).

16 This is a point stressed by scholars influenced by Niklas Luhmann's systems theory.

Power and Economic Exchange

Power, both economic and noneconomic, inscribes itself into markets by shaping institutions. Power is thus an aspect of every market, and the institutions governing international and global markets cannot be studied without reference to it. Four aspects of power stand out in the period studied here.

First, on a global scale, we need to take account of 'the rise of the West' and the 'great divergence' around 1800 that put an end to relative parity between Europe and other advanced regions, bringing ever larger parts of the world under European dominance.[17] In their classic paper, 'Imperialism of Free Trade', John Gallagher and Ronald Robinson have argued that Europeans preferred informal influence and economic integration to colonial rule where possible.[18] Countries unwilling to integrate into the Western-dominated global economy, however, were often forced to 'open up' and accept free trade with the help of gunboats, as was the case in China and Japan. Colonial territories were developed into areas for the production of raw materials, thus securing supplies for European industry. European law was introduced to provide legal security in the colonies, thereby reducing transaction costs, and to facilitate the operation of Western merchants and plantation owners in these areas.[19] This process often amounted to economic exploitation of the conquered regions, but the exploitation did not extinguish the agency of indigenous merchants, moneylenders and peasants. Often local social and economic conditions made the objectives of colonial bureaucrats much more difficult to attain than they had assumed, as Christof Dejung argues in an analysis of the problems faced by the British when they tried to improve cotton quality on the Indian subcontinent. Furthermore, as Claude Markovits demonstrates, indigenous economic elites

[17] William H. McNeill, *The Rise of the West: A History of the Human Community* (Chicago, 1963); Kenneth Pomeranz, *The Great Divergence: Europe, China, and the Making of the Modern World Economy* (Princeton 2000); John Darwin, *After Tamerlane: The Global History of Empire since 1450* (London, 2007). For a critical review of these approaches see Patrick Karl O'Brien, 'The Deconstruction of Myths and Reconstruction of Metanarratives in Global Histories of Material Progress', in Benedikt Stuchtey and Eckhardt Fuchs (eds.), *Writing World History, 1800–2000* (Oxford, 2003), 67–90; Peter Kramper, 'Warum Europa? Konturen einer globalgeschichtlichen Forschungskontroverse', *Neue Politische Literatur* 54 (2009), 9–46.

[18] John Gallagher and Ronald Robinson, 'The Imperialism of Free Trade', *Economic History Review New Series* 6 (1953), 1–15.

[19] Mommsen and de Moor (eds.), *European Expansion and Law* (Berg, 1992).

were sometimes able to create their own commercial networks, functioning in parallel to the globalised infrastructure of Western business.

Second, any discussion of power would be incomplete without reference to the often overwhelming importance of the nation-state – which often was also an imperial power.[20] The same period that witnessed the establishment of a truly globalised economy and of imperial expansion also witnessed a consolidation of national identities and a reinforcement of national borders. Several scholars have claimed that, at least in the nineteenth century, globalisation and territorialisation were not diametrically opposed developments but rather were closely interrelated or dialectally intertwined.[21] After the 1870s and then particularly in the interwar years, nations aimed to consolidate their economic influence on a global scale while at the same time trying to protect their domestic markets from foreign competition. International patent law is one example of the creativity of national governments in applying international conventions for the benefit of their domestic industries. For the sake of allowing their entrepreneurs to continue copying foreign products, small European countries like Switzerland and the Netherlands delayed the adoption of patent laws despite having signed the Paris Convention. As Pierre-Yves Donzé shows in Chapter 9, Japan also promoted technology transfer through a highly selective application of such international law: on the one hand, by protecting Western intellectual property, the Japanese government sustained the cooperation between major Japanese and Western firms necessary for breaking into technologically advanced sectors; on the other, it allowed Japanese firms to copy easily reproduced low-tech consumer goods by excluding them from that law.

Third, both individual companies and company networks enjoy a certain degree of power over the market. Obviously, they influence markets by simply participating in them – that is, by providing products and services at the highest price they can obtain and buying raw materials and services at the lowest available price. Large corporations may also seek to control markets by gaining monopoly position, forming cartels or creating formal institutions for a particular segment of the market. In addition, firms may try to influence decision makers outside the market, such as governments, political parties and regulatory authorities,

[20] On this, see Jürgen Osterhammel, 'Globalizations', in Jeremy H. Bentley (ed.), *The Oxford Handbook of World History* (Oxford, 2011).

[21] Ian Clark, *Globalization and Fragmentation: International Relations in the Twentieth Century* (Oxford, 1997); Sebastian Conrad, *Globalisierung und Nation im Deutschen Kaiserreich* (Munich, 2006).

thus shaping the economic rules. Economic power has often been influential in shaping political decision making – an argument developed by, for instance, Peter Cain and A. G. Hopkins, who have proposed that the 'gentlemanly capitalism' of the City of London was the main force shaping the evolution of British imperialism;[22] this issue is considered by Bernard Attard in Chapter 5, with reference to the City of London's 'structural power' in the global economy after 1850. Britain may have been a special case in this respect because maintaining institutions capable of supporting London's pivotal role in the world economy was a consistent priority of British economic policy, a fact explored in the contributions of Phillip Dehne, Christof Dejung and Bernd-Stefan Grewe. The United States and Germany appear to offer a contrast: in both countries, it has been argued that, in many areas crucial for international economic integration, policy has often been shaped by those societal groups least interested in its promotion.[23] In any event, political and corporate power interpenetrate and reinforce each other, and frequently, large – especially multinational – firms are able to resist political interference with their operations.[24]

Fourth and finally, power may of course have a much more direct impact on markets than that mediated through institutions. A prime example of such direct impact is warfare. As Ronald Findlay and Kevin H. O'Rourke have shown, international trade has rarely existed in splendid isolation from the sphere of international rivalry and war.[25] In the First World War, belligerent powers were aware that economic performance and the supply of raw materials were decisive for military success and thus closed or blacklisted firms suspected of 'trading with the enemy'.[26] Yet as Phillip Dehne's contribution makes clear, neutral countries provided

[22] Peter J. Cain and A. G. Hopkins, *British Imperialism, 1688–2000* (Harlow, 2001).
[23] See Drezner, *All Politics Is Global*, 5, on this point, which finds general support in Niels P. Petersson's contribution to this volume.
[24] For this reason, they were depicted as modern leviathans by Alfred Chandler and Bruce Mazlish in their *Leviathans: Multinational Corporations and the New Global History* (Cambridge, MA, 2005).
[25] Findlay and O'Rourke, *Power and Plenty*.
[26] For economic warfare during the First World War, see among others Avner Offer, *The First World War: An Agrarian Interpretation* (Oxford, 1989); John McDermott, 'Trading with the Enemy: British Business and the Law during the First World War', *Canadian Journal of History* 32 (1997), 201–20; Marc Frey, 'Trade, Ships, and the Neutrality of the Netherlands in the First World War', *International History Review* 19 (1997), 541–62; Niall Ferguson, *The Pity of War: Explaining World War I* (New York, 1999), 248–81; Stephan Broadberry and Mark Harrison (eds.), *The Economics of World War I* (Cambridge, 2005); Christof Dejung and Andreas Zangger, 'British Wartime Protectionism and Swiss Trading Companies in Asia during the First World War', *Past and Present* 207 (2010), 181–213.