

G.R.Hawke

# **Economics for historians**

---

---

# **Economics for historians**

---

**G. R. HAWKE**

Professor of Economic History  
Victoria University of Wellington  
New Zealand

**CAMBRIDGE UNIVERSITY PRESS**

Cambridge

London New York New Rochelle

Melbourne Sydney

Published by the Press Syndicate of the University of Cambridge  
The Pitt Building, Trumpington Street, Cambridge CB2 1RP  
32 East 57th Street, New York, NY 10022, USA  
296 Beaconsfield Parade, Middle Park, Melbourne 3206, Australia

© Cambridge University Press 1980

First published 1980

Printed in the United States of America  
Typeset by Vail-Ballou Press, Inc., Binghamton, NY  
Printed and bound by Vail-Ballou Press, Inc., Binghamton, NY

*Library of Congress Cataloging in Publication Data*

Hawke, Gary Richard.

Economics for historians.

Includes bibliographical references and index.

1. Economics. I. Title.

HB171.5.H3495 330 79-22127

ISBN 0 521 22734 8 hard covers

ISBN 0 521 29627 7 paperback

---

---

## Preface

---

This book is intended for students of history who realise that their subject demands some understanding of economics. I assume that the main interest of my readers is in some aspects of the past and that the fascination of abstract ideas, while real, is decidedly subordinate. I seek to build on an initial feeling that economics is relevant to understanding important aspects of the past by elucidating the ways in which economics can be important. Readers should eventually be confident that they can recognise when economics is important and what economics is important and that they can go on beyond this book when historical studies make more advanced economics relevant to them.

Within the large class of potential users so defined, I have in mind especially students reading economic history in British universities. They are now more likely than they were in the past to take a course in economics principles, but for most of their studies they will have little contact with economics. They will be taught (and usually well taught) by teachers who give little explicit attention to their reliance on economics. I think it is easy to underestimate the difficulties of relating the first-year economics principles course to the problems encountered in historical studies; practising economic historians forget how much they use the ideas of theoretical economics. So often the student of economic history has memories only of distasteful encounters with things like marginal revenue, which never seemed to occur in historical time, and no one explains how the idea is developed for use in historical studies. I seek in this book to explain economic ideas so that they can be related to historical interests and to persuade students who have done an economics principles course that the subject was not as irrelevant as they thought. (I have not assumed any previous economic background.)

These problems do not exist only in Britain. In Australia, New Zealand, and the United States, for example, it is usual for students of economic history to take more courses in economics, but the difficulty of relating theory to historical studies remains. Even in the United States, training economists with a prime interest in economic history is mostly a graduate activity, although undergraduates also should find this book useful. I have been told that the situation is much the same in Spain and Italy, and it is probably true of other European countries too. Nevertheless, I have kept the historical examples discussed in the book mostly to Britain, partly because of the main readership I have in mind and partly because, as will become clear to the reader, there is a particular merit in having several examples recur throughout the book. I think that readers in other countries will readily find local examples analogous to those used in the text, and I do not think British history is so old-fashioned that it detracts from the interest of the book.

There is a much wider group of people who seek to understand economics so that they can participate in current political and social discussions. They too may find this book useful, especially if they realise that it is an understanding of economic ideas and not a mastery of particular techniques which they want. But my focus is firmly on historical interests (which I think a good route to understanding current issues), and I have not been willing to sacrifice that for a wider immediate appeal.

The main principle by which the content of this book has been chosen is that it should deal with economic analysis that has been used in historical studies. This is at one and the same time the main justification for the book and the main difficulty in its composition. The economics which has been used in historical work is not conveniently organised relative to orthodox introductions to economics; it includes ideas usually included in intermediate rather than elementary texts, it omits material often used as building blocks towards ideas which have been used, and single historical studies usually draw on several aspects of economics, often widely dispersed in an orthodox treatment. An introduction designed for historians is not just the usual text with some reference to events in the past.

I have not used the usual labels of macroeconomics and microeconomics, that is, very roughly, the areas concerned with

whole economies and with individual people and firms respectively. The usefulness of these labels is often debated by mainstream economists, but they clearly have little relevance to the way in which economics has been used by historians. I have found it more useful to think in terms of two strands of thought; those economic ideas developed in the course of analysing the level of wealth achieved in a society, and those developed in the context of exchanging one commodity against another. These two strands have frequently intertwined and they do not play a major role in the book itself, but they provide the basis for the order in which ideas are presented.

After Chapter 1, which is designed to bolster the reader's confidence while introducing some fundamental economic ideas in precisely the style used in historical texts, we have a group of chapters which follows the former stream. We begin with the concept of income. I have sometimes speculated that the essential difference between economic historians whose primary allegiance is to economics and those whose primary allegiance is to history is that the former first identify a central process and then analyse it while the latter build up an overall picture from its component parts. Chapter 2 is intended to familiarise the reader with the former means of study, and to set out, by example, the way in which economic concepts are related to empirical reality. Chapters 3 and 4 deal with ideas which have arisen in looking at the determinants of income from various points of view. In Chapter 5 attention is turned to monetary matters but with the focus still on the analysis of wealth.

Chapters 6 to 8 turn to the exchange tradition. The first of these is headed 'Relative Prices' to avoid the usual emphasis on the psychology of individuals and keep attention on the issues associated with individual prices in historical studies. This enables us to go further in topics such as consumers' surplus than many introductory texts without incurring great costs. Similarly, Chapter 7 treats those aspects of international economics used in history while avoiding many of the policy issues found in most textbooks. And contrary to what might be expected, much of the modern development of growth economics lies mostly in the stream of ideas about exchange, and that part which is important to historians is introduced in Chapter 8.

My emphasis is on economic ideas. It would be easy to write

corresponding 'applications' chapters, but I do not wish to write a forbidding tome. Chapter 9 is partly an exception to this self-denying ordinance, and it is included because historians are accustomed to a heavy emphasis on government activities. Examples of the development of economic ideas are otherwise incorporated in the text, using the historical literature. In teaching economics and economic history, I am often aware of a tension between talking about theoretical issues in a particular context (which is often useful for retaining student interest) and isolating a theoretical construct so that it can be recognised in a number of guises. That the shape of the production possibilities curve which is often introduced in some abstract puzzles about international trade has something to do with apparently conflicting measurements of the rate of growth in the Soviet Union in the 1930s often comes as a revelation to undergraduate students. Hence, I have tried to vary the degree to which my references to the historical literature are built into the economic analysis. In most cases (Chapters 3, 5, and 6-9) they are scattered through the text, but the extent to which they are detached or detachable is varied, and in Chapters 2 and 4 they are kept for a separate section at the end of the chapter. This has the additional advantage of showing the different degrees of abstractness of ideas within economics; the study of money has always had a more immediate connection with observation than has discussion of economists' rent.

Chapter 10 draws the book together and returns to some of the themes of the first chapter. Readers who have worked through the book are guided towards an assessment of how it has affected their perception of the part of economics in historical inquiry. I hope there are such readers, but I have been conscious of the likelihood that readers will want to refer to particular topics, and the chapters and even sections within chapters are substantially self-contained.

The intended readership of this book imposes constraints on the way it is written. Given students whose interest does not have to be retained by some device to create 'relevance', I have no doubt that the most efficient way to teach elementary economics is to start with some mathematics (although I do not think that mathematics should be permitted to absorb economics, including the essentially historical processes of relating concepts to re-

ality and interpreting empirical evidence). But the readers of this book are unlikely to tolerate mathematics; indeed, they probably have an active antipathy to it. Consequently, the mathematical demands are very slight. Some equations are introduced in Chapter 4, but the text carefully steers around them. I hope that the treatment shows even the most timid reader that the equations are not incomprehensible and that the few later topics where equations are essential can be digested without undue difficulty.

I have used 'mathematical' here to mean primarily 'algebraic', since that is the sense in which historians usually use the word. The more subtle aspects of 'mathematics' in a sense close to logic are indeed present but expressed in the language used by historians. There is also a frequent use of diagrams. I am aware that history students are often not accustomed to reading diagrams thoroughly, but I do not think that economics can be expounded, or a great deal of economic history literature read, without an understanding of simple diagrams. The necessary skill requires little learning, merely a modicum of persistence and practice. I have, on the other hand, avoided the arithmetic examples usually found in introductory economics texts. My experience is that history students are diverted rather than assisted by such devices, the labour of following the arithmetic taking attention away from the important principle being illustrated. My usual approach is a direct exposition of economic ideas. This makes the text look difficult to those familiar with conventional treatments, but I am convinced that history students can handle more abstract thinking than is usually appreciated. I took a related approach in two earlier books and their reception has permitted me to retain my view [G. R. Hawke, *The Development of the British Economy, 1870-1914* (Auckland: Heinemann, 1970) and *The Evolution of the New Zealand Economy* (Auckland: Heinemann, 1977)]. Indeed, I think the pupils to whom those books were addressed find less difficulty with them than their teachers do! But one of the values of this present book may well be to show conventional British economic historians that they use economic theory a great deal more than they realise and that they can make it easier for their students to gain the necessary knowledge.

A first draft of this book was written while I enjoyed the hospi-



tality extended to a Visiting Fellow at All Souls' College, Oxford. Seminars at the Universities of Cambridge, Edinburgh, Glasgow, Leeds, London, and Sheffield commented generously on some of its ideas. I am even more indebted to friends and colleagues who have favoured me with advice, especially Margaret Arnold, F. Capie, S. L. Engerman, R. C. Floud, J. D. Gould, T. B. Layton, D. N. McCloskey, P. K. O'Brien, and D. C. M. Platt. I should thank too the writers of abstracts for an AN-ZAAS conference in Auckland in January, 1979. The dullness of the abstracts, which was not justified by the meetings I did attend, contributed greatly to the speed with which the final revision of this book was accomplished.

G. R. Hawke

*Wellington, New Zealand*  
*January 1980*

---

---

## Contents

---

Preface	<i>page</i> vii
<b>1 History and economics</b>	<b>1</b>
Historical skills in economics	1
Economics, academic and practical	4
Economics as an engine of analysis	7
Rationality, prices, cost, and wealth	9
Terminology, abstraction, mathematics, and quantification	13
Economic history, old and new	15
<b>2 Income</b>	<b>16</b>
Productive capacity and welfare	16
Conceptual issues	18
Measurement procedures and problems	27
Historical uses	35
<b>3 Factors of production</b>	<b>37</b>
Land, labour, and capital	37
Land	38
Labour	42
Capital	48
Production functions	53
Conclusion	60
<b>4 Income determination</b>	<b>62</b>
Keynes	62
Multipliers	63
Accelerators	68
Historical applications	73

<b>5 Money</b>	<b>75</b>
Monetary history	75
The two triads	76
Banking	81
Nonbank financial institutions	87
Monetary economics	90
<b>6 Relative prices</b>	<b>98</b>
Prices and income	98
Demand curves	98
Supply curves	111
Market clearing	118
Theory of the firm	124
<b>7 International economics</b>	<b>132</b>
Introduction	132
Comparative advantage	132
Tariffs	139
Balance of payments	147
Capital exports	154
<b>8 Growth</b>	<b>157</b>
Growth and history	157
Labour surplus	158
Investment	164
Technical change	173
Conclusion	182
<b>9 Government</b>	<b>184</b>
Government in history and economics	184
Balanced budget multiplier	185
Tax incidence	190
Market failure	193
Transaction costs	198
Objectives of policy	200
<b>10 History and economics again</b>	<b>202</b>
An injustice to economics?	202
Economics in history	206
Historical periods	210
Conclusion	214
Notes	215
Index	233

## **History and economics**

---

### **Historical skills in economics**

Historians are much too deferential to economics. Economists have an apparent mastery of sophisticated mathematical techniques, and they are able to earn high incomes in public administration or business, presumably because of those skills. For a profession which claims little but trained common sense for its own members, economists appear high powered. Furthermore, unlike most other mysterious disciplines, economics is said to contribute to history itself, to an understanding of the evolution of human societies in the past.

There are indeed claims to be made for the usefulness of economics in a variety of fields, and in the last twenty years or so economic history has benefited from a renewed infusion of economic theory. But in applied work, whether in public policy, business administration, or economic history, the aspects of economics which are most fruitful are not particularly arcane. Rather, applied economics is characterised by the intelligent deployment of some simple concepts, the understanding of which is not beyond anybody who has mastered techniques regarded as commonplace by historians.

Furthermore, those who understand the processes by which knowledge and understanding are derived from the partial and fragmented empirical remains from the past are already halfway to the intellectual equipment needed for applied economics and have, perhaps, gained that equipment in the best possible way. There is a field of study known as decision making under uncertainty which usually occupies a prominent place in the training of economists and which looks mathematically demanding and even frightening to most historians; but in any piece of applied

economics it is likely to be much less useful than the process of forming judgment on the basis of incomplete information which, for historians, is the most familiar activity of all.

There is yet another comfort for the historian who feels the need to understand economics. Economics is itself becoming a more historical discipline. The recent textbook by Robinson and Eatwell,<sup>1</sup> while generally regarded as idiosyncratic and indeed erroneous in places, is widely approved as having more historical sensitivity than earlier texts such as those by Samuelson.<sup>2</sup> Perhaps even more telling is the extent to which the recent work of some leading economists gives markedly greater attention to history,<sup>3</sup> both the history of the subject and the history of the economies which particular pieces of economic analysis were designed to illuminate. This is partly an incidental byproduct of a desire by economists to improve their analysis of the way in which economies grow. But there is also a more general recognition that the process of intellectual thought itself occurs in historical time and that much can be learned by looking carefully at the sequence of innovations by which analysis is forwarded.<sup>4</sup> As changes over time in both perceived problems and in the responses of disciplines such as economics become more prominent, the skills of historians are likely to be more highly esteemed.

It is not to be expected that the barriers which seem to stand between many historians and economics will easily be swept away. To begin to follow the reasoning of economists, a historian must be prepared to tolerate some differences of style and approach. An economist tends to emphasize the abstract and to be selective in the things to which he devotes his attention. Economic analysis is usually presented as a tentative or conditional answer to a particular set of issues. To the historian advised to include in his ambit all the available evidence and to seek definitiveness in his writing, these characteristics seem simply misguided. The conflict of practice is not nearly so stark. Historians do employ abstraction but mostly in terms and concepts which have come to be part of common language or which were familiar in the society about which they are writing. Historians are selective in their choice of topics or themes, but divisions such as those between politics at Westminster and political organisations in the constituencies are different from the divisions employed

by economists. No historian really expects finality in the interpretation of a major historical process, and errors in the handling of evidence are culpable in any study.

Differences of degree do remain significant. The usefulness of a selective discussion of an issue and the extent of incompleteness which should be permitted in publication remain matters for individual judgment – about which there is likely to be some difference between economists and historians. But these are hardly matters crucial enough to prevent each discipline from learning from the other.

There is a deeper matter which we have already hinted at. Historians frequently use expressions like ‘understanding the past in its own terms’, while economists want to employ concepts developed more recently in their studies of past societies. The point might be described as a conflict between ‘past centred’ and ‘present centred’ studies. Again, the difference is one of degree. No historian can sensibly restrict himself entirely to the words and concepts of the society which he is studying; nor, even more, can he divest himself of the knowledge and outlook of his own time. Similarly, no economist can hope to explain the motivation of a past action in terms of modern concepts unless he can translate those concepts into notions which might have been present in the mind of the historical actor. But merely narrowing the difference would miss the main force of the point. *Historians and economists do not always ask the same questions.* It makes sense to the latter to ask whether a particular investment was a sensible use of resources, even if the historian knows perfectly well that it was made because the king believed that the well-being of his immortal soul depended on it.<sup>5</sup> There is surely no conflict between these positions, inasmuch as different questions usually have different answers. Historians interested only in the motivations of people may still find it useful to know what economists can tell about the nature of the society in other respects; other historians with less restricted interests may welcome the same gain and more. Economists too may come to understand more of the results of their analyses from what historians with other concerns can tell them; in particular, few economists really have no interest in motivations.

Historians and economists are likely to have overlapping rather than identical interests. Because of the way in which the

disciplines have grown, there are always likely to be differences of taste and style between them.<sup>6</sup> Nevertheless, they have a great deal in common.

### **Economics, academic and practical**

'Economic history has been well defined as that part of history which requires a knowledge of economics for its full understanding.'<sup>7</sup> This simple aphorism by a senior British economic historian, who is not normally considered a leader of recent trends in economic historiography, would be acceptable to most historians. It obviously provokes further questions such as how much knowledge is required and what is meant by 'full' understanding. Even more basically, it directs our attention to what economics is.

The most common definition of economics, usually attributed to Robbins<sup>8</sup> and hinted at in the title of Court's book, *Scarcity and Choice in History*, is that economics is the logic of choice, the study of how scarce resources should be allocated among competing ends. It does capture an important part of economics in an interesting way, but it slights some aspects of the subject which are less concerned with sharing out something in short supply such as studies of the incidence of unemployment and the distribution of income. Indeed, the whole field of economic growth is concerned with increasing the total resources of a community as much as with their competing uses and so it does not fit entirely comfortably within such a definition. Against such disadvantages, we can set the way in which the notion of choice provides a cover of respectability for economists who wish to invade areas usually thought to belong to other disciplines (for example, the institution of marriage and the control of crime). Choice of some kind is exercised in nearly all human activities, and economists adopting this definition of their subject have few fetters on their activities.

A definition which neither includes areas thought to lie within the province of economists nor excludes fields of inquiry which belong to other disciplines might not seem to be a good starting point. But other definitions which have been proposed in the history of economics fare no better. Two suggestions of leading economists were the 'study of mankind in the ordinary business

of life'<sup>9</sup> and the study of 'that part of social welfare that can be brought directly or indirectly into relation with the measuring rod of money'.<sup>10</sup> Economics does not include the whole of the ordinary business of living and it does include some extraordinary aspects of life; it includes some things which cannot be valued in cash and excludes some that can. This illustrates only the difficulty of summing up a varied field of learning within a short and simple phrase.

It is better to begin in a more empirical frame of mind by noting that the label, 'economist', is attached to people engaged in very different activities. An economist in the public service, an economist engaged in private business, and an economist in a university are likely to be occupied differently with only a small amount of knowledge or purpose being common to their work. It is from academic economics that historians hope to learn, and it is well to begin by emphasizing that academic economists are justified mostly by their role as educators and only secondarily by the practical relevance of their subject. Economics, like mathematics, philosophy, or any of the humanities, holds its place in the university curriculum because it is a suitable vehicle for the training of minds in honest and consistent thought. It so happens that some of the material contained in economics has been found useful in fairly direct applications, more so than is true of pure mathematics, philosophy, or history, but economics would retain its academic value independently of that feature.

Its academic value is derived from the usual array of intellectual processes found in various balances in any of the humanities. Comprehension of abstract ideas, manipulation of concepts, collection and verification of empirical material, and comparison of observations against a priori implications are common to economics and many other subjects. The context within which these processes are stimulated can vary widely while remaining within the subject of economics. There is little more in common between many courses in econometrics and in labour economics than the most general academic processes just identified.

The point we are approaching indirectly is that the demarcation of subjects relates to university teaching and not to research. Economics is what it is convenient for a university to teach under an economics rubric of some kind, while no scholar, in particular,



no economic historian, has to ask whether he is an economist or something else while he is engaged in research. The content of economics courses has grown as the preoccupations of teachers and scholars have changed. Such questions as

Why are some societies richer than others?

Why do prices behave as they do?

Why do periodic fluctuations in prices occur?

What is the relationship of money to the supply of goods?

What is the effect of the introduction of banks?

What is the relationship between agriculture and industrial activity?

How do individuals choose to spend their incomes on a selection of goods from those available?

What difference does it make if a significant proportion of the total output of a good is under the control of an individual?

What amount of taxation should be raised and in what form? and a host of others have produced a body of thought and information about which courses can be organized and conveniently labelled 'economics.'

The literature so produced is very rich. It can cater to a taste for abstract mathematics or to careful sifting of a mass of empirical observation. It is commonly thought that most prestige attaches to the more abstract and mathematical kind of economics, but while there is some justification for that view, it is not always so. Even the Nobel Prize in economics, a dubious but common measure of distinction, has gone to Kuznets who would normally be regarded as towards the 'empirical' end of the spectrum. More generally, economists prize the originator of a notion on which abstract reasoning is subsequently built, whether that notion is a striking empirical observation or a simplifying abstraction. The reputations of two modern economists, Phillips of the 'Phillips Curve' and Friedman of 'money supply' fame, conveniently exemplify these possibilities.

Furthermore, the economics used in government or business is mostly the less abstract kind of reasoning. The cost-benefit analysis by which the World Bank decides to support a development project or Ford decides to build a new engine plant in Wales pays scant regard to the complexities known to be involved in valuing time or in interpersonal comparisons. Tariff negotiations are likely to reflect notions of 'effective protec-