THE EMERGENCE AND DECLINE OF MARKET ECONOMIES THROUGHOUT HISTORY

STATE OF THE ART AND A NEW APPROACH

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1. Markets, their historiography and some main assumptions

This paper wants to look at the current ideas on market economies as a historical phenomenon and to some alternative ways of doing so.[1] It starts with a broad overview of some of the main assumptions about the history of markets, focusing on factor markets..

If we define markets as systems of exchanging and allocating resources by way of monetary transactions, with the prices primarily determined by the forces of supply and demand, and with competing actors who are mainly geared towards their own economic profit, then a main general assumption – mostly implicit – is that markets are a modern phenomenon. This modernity would hold even more for market economies, that is, economies which use the market as their main coordination and allocation system, and not only for goods and products, but also for the production factors: land, labour and capital, with the owners of these factors of production being able to trade these in the market.

Markets for goods and products are generally considered to have been present to some extent in many of the more advanced pre-industrial societies, from Antiquity onwards, with ancient Babylonia, Egypt, Roman Italy and China and their thriving commodity markets as examples. Only much later in time, it is assumed, some societies started to use the market as the *main* system for the exchange and allocation of goods and products. Economies which not only organize the exchange of goods and products, but also that of land, labour and capital through the market are much rarer and are even more explicitly deemed modern. The latter economies are assumed to have grown out of older, more stagnant ones, which had more traditional mechanisms of the exchange and the allocation of land, labour and capital, and this shift has presumably helped these societies develop and become wealthy. Further, and especially in neo-classical economics, there is the tendency to see these markets as a kind of abstract playing field where supply and demand meet, or as a playing field where as few regulations as possible should obstruct the working of the forces of supply and demand, which would allow these markets to continuously adapt to changing circumstances and to cater changing needs. It is often

[1] This paper will be part of the introduction of a new book on markets and market economies as a historical phenomenon I am finalizing at the moment. The book is provisionally called *The Invisible Hand?* (OUP).

assumed that markets, if unfettered, offer flexibility and dynamism, and they create economic growth and enhance welfare.

The latter assumption has a long pedigree, and is often ascribed to Adam Smith in particular,[2] and it has regained strength and respectability in the 1980s and 1990s, in an interaction between academic scholarship and the trends in politics and societies. Both in academia, with the dominance of the Chicago School and neo-classical economists such as Milton Friedman, and in politics, with the rise of Thatcherism and the adoption and propagation of neo-liberal policies by the World Trade Organization, the International Monetary Fund and the World Bank, the idea of free, perfect markets, deregulation and privatization as the most secure road to growth and welfare was widely accepted.[3]

Equally widely accepted is the link between markets and political and individual freedom, and the suggestion that the economic freedom to act within free markets on the one hand and political and legal freedom on the other hand will, or should, mutually reinforce each other. This idea was pioneered by Friedrich Hayek and his influential *The Road to Serfdom* (1944), where he argues how state planning and government coercion, and the associated reduction of free markets, go hand in hand with tyranny and lack of personal freedom.[4] These ideas were elaborated by Milton Friedman, who states that in the nineteenth and early-twentieth centuries "political freedom clearly came along with the free market and the development of capitalist institutions" and that – although it is not a sufficient condition - "capitalism is a necessary condition for political freedom".[5] According to Friedman, the market is able to offer coordination without coercion, it provides economic freedom, permits a wide diversity and it prevents the concentration of power. In the 1980s, these ideas were enthusiastically embraced by neo-liberal thinkers and policy-makers.

Since the late 1990s some of these assumptions came to be criticized, however, or at least refined. There has been a growing stream in the field of sociology, sparked off by Mark Granovetter, which stresses that there are no "free", abstract markets where rational. Atomized actors with perfect information operate, contrary top the assumption of many neo-classical economists. Rather, any market is socially embedded and consists of social structures, where social relations, rules and thus power disparities are at play.[6] Also, there is influence of the New Institutional Economics, and the works by Douglass North in particular, which made an impact in the field of economics and subsequently in economic history. They have demonstrated how markets are a web of formal institutions (e.g., property rights, contracting rules and informal institutions (norms, customs), that is,

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[2] Friedman, *Capitalism and freedom*, 133. For the nuances on this assumption made by Adam Smith himself: below.
[3] Van Horn and Mirowski, 'The rise of the Chicago School'.
[4] Hayek, *The road to serfdom*.
[5] Friedman, *Capitalism and freedom*, 9-10 (where these citations are taken from) and 13-15.
[6] Granovetter, 'Economic action and social structure'; Fligstein & Dauten, 'The sociology of markets'.

as a complex and varying set of rules of the game of exchange, and not an abstract, empty playing field where supply and demand directly meet.[7] The specific arrangement of these institutions lends the market its specific characteristics and effects, which can either be positive or negative. The idea that markets are intrinsically flexible and adaptive, is also nuanced now. It is clear that market institutions can become frozen and sometimes do not adapt to changing economic, technological or ecological circumstances and requirements, even in cases where their inflexibility hurts growth, or where changing trade flows, waning success in international competition or ecological challenges would require institutional adaptation. The concept of institutional sclerosis, as put forward by, for instance, Mancur Olson and Douglass North in his later work,[8] albeit each stressing different causes of possible sclerosis, has now found broad acceptance, also in relation to market institutions.

Also, the popular but problematic notion that institutions develop more or less spontaneously because they provide a good answer to economic or ecological needs, is questioned now. This notion suggests that efficient institutions - 'efficient' being defined as contributing most, in a given set of circumstances, to the welfare of society - will gradually, more or less automatically prevail over less efficient alternatives or, as a result of competition between socieites, weed out the inefficient ones.[9] Unfortunately, as has become clearer over the past years, reality is different. Many societies end up with obviously inefficient institutions simply because powerful groups or individuals create and sustain institutional arrangements that support their own interests, or protect their own investments, if necessary at the expense of aggregate welfare. A more credible way to account for the development of institutions is the 'social conflict view': the notion that institutions are the effect of a confrontation of various social groups.[10] This view implies that the institutions in place are not automatically the most efficient ones for society at large; they rather suit best the interests of the group or groups in power.

Lastly, in recent years more people - both inside and outside academia - have come to question the welfare-enhancing effect of markets again. One argument they bring forward is the seeming inability of markets to benefit all parties involved in market exchange, as can be seen most conspicuously in many developing countries. Although it is clear that market exchange is not a zero-sum game, and it will drive up economic growth through specialization, division of labour and the necessity of ongoing investments, the fruits of growth can be distributed very unevenly and may even make one of the parties involved worse off than before this exchange started. An example of the detrimental effect of market exchange is food being bought, exported and shipped from countries

[7] North, *Institutions*, and Williamson, 'The New Institutional Economics'.
[8] Olson, *The rise and decline*, 36-74, esp. 53-58 and 69-73 (stressing the negative role of special interest groups)
[9] As in the tradition of Demsetz, 'Toward a theory', a notion also found in the earliest works by Douglass North.
[10] This point is made more generally in the literature on political economy, and was forcefully made again by Ogilvie, '"Whatever is, is right"?'.

where people are desperately in need of food but unable to pay for it with the wages they receive in the labour market, away to foreign markets, perhaps bought in order to be used as fodder for cattle in the wealthy importing countries. When peasants in developing countries lose their direct access to land and the means of production, and become reliant on markets for food, land and wage labour, they can actually become more dependent and even more vulnerable than they would have been in a peasant society with limited market influence, and markets can well result in draining food from areas where it is most needed.[11] Other critics of the market point to the economic downfalls and recent problems in financial markets - and would hold that these are at least in part the result of the fact that these were allowed to operate more freely in recent decades and their functioning to become isolated from democratic control and regulation. Again other critics point us to the negative social and ecological effects associated with market competition.[12]

These criticisms are not shared by all, however. The latter one is especially contentious, since many neo-classical and other economists would hold that the ecological and social problems are not the intrinsic result of markets but rather of the malfunctioning of markets because of obstructions, interference by governments, influence exerted by special interest groups, or flaws in the current market frameworks. Correcting these flaws, and having markets function more freely, would solve these problems; a position also held by Douglass North and by Deirdre Mc Closkey, who argues that problems are not the result of having too much market but rather of insufficient access of people to markets.[13] More in general, despite the nuances mentioned above, the assumptions that factor markets are modern, help dynamism and stimulate economic growth, still stand and are widely held; not only by neo-classical and neo-institutional economists but also by many neo-marxists,[14] who at least see them as instrumental or even crucial in helping traditional, feudal societies to escape from stagnation and to develop their productive forces.

Their ideas go back to the founding fathers of these intellectual and ideological currents: Karl Marx and Adam Smith. Marx offered the first comprehensive analysis of capitalism, which could be defined as a society in which there is a pronounced division between property-less wage-earners and entrepreneurs who privately own the means of production, and thus have a way to appropriate the surplus, and in which both producers and entrepreneurs are dependent on the market.[15] Through the

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[11] Vanhaute, 'From famine to food crisis', for the negative role markets may play in famine, using the example of the Bengal famine of 1943: Sen, *Poverty and famines*.

[12] Among these critics are welfare economists like Robin Hahnel, development economists and ecological economists, but also established economists like Joseph Stiglitz and Paul Krugman. See Stiglitz, *Freefall*.

[13] D.C. North, xxx, and McCloskey, *The bourgeois virtues*.

[14] See Rigby, *Marxism and history*, 9, 41, 44-48, and below, pp. x-x.

[15] This is the definition suggested by Hilton, 'Capitalism', and Van Bavel, 'The transition in the Low Countries'. In order to avoid the connotations the term 'capitalism' carries – either positive or negative ones -, the term will not be often used throughout this paper.

market, in the words of Marx, each of them became subjected to the anonymous power of capital.[16] At the same time, and despite its negative social effects, under capitalism - and enabled by the dynamism of capitalism and the effects of competitive markets that force capital owners to keep on investing , productive forces would grow and help paving the way for the transition to a socialist and later communist society. Although Marx later suggested that also alternative paths to communism might exist, such as a direct step from peasant communal ownership in Russia to a communist society, he mostly saw capitalism as a necessary stage, following upon earlier stages in history, most notably the stage of feudalism.[17] Also, he expected other countries to follow the capitalist ones in their footsteps.

In this respect, Karl Marx' ideas were akin to those of Adam Smith, who used a four stage framework (which comprises hunting, pastoralist, agricultural and commercial societies) with each society having its own form of justice, property, and social and political organization, growing in size and complexity.[18] Although Smith did not sketch history as a fully unilinear development towards commercial society, and neither did see commercial society and especially its most developed form – labelled by him as natural liberty – as an inevitable end stage, most later commentators have interpreted his story as one of progression, with commercial society forming the peak.[19] Although Marx was less interested in the market per se than in the whole of social relations, he and Smith shared their positive appraisal of the opportunities offered by markets and market economies to greatly enhance productivity. Market competition, and the associated necessity of innovation and scale-enlargement, was exactly the reason that Marx attributed to capitalism the unique ability to develop a society's productive power.[20] His ideas, and those of Adam Smith, continue to influence our thinking about markets, if only implicitly. As we will see in the next section, their assumptions about the modernity and positive effects of factor markets on development and economic growth are underpinned by much of today's historical research.

2. On the modernity of markets: the verdict of recent historical research

Most research into the history of markets, some of it conducted by sociologists, archaeologists and economists but mainly by economic and social historians, essentially treats markets for land, labour and capital as a modern phenomenon. The main result of recent, empirical studies is that the dating of the rise of factor markets is pushed somewhat further back in time. Polanyi in the 1940's and 1950's

[16] Clarke, 'Marx and the market'.
[17] This led to teleological reasoning, found with many marxist thinkers, including Cohen, *Karl Marx's theory*. See Rigby, *Marxism and history*, 106.
[18] Smith, *Wealth of nations* II, 689-694, and also 606-607 and 687-688. See also: Kim, 'Adam Smith's theory of economic development'.
[19] The nuances made by Adam Smith are highlighted by Alvey, 'Adam Smith's three strikes'.
[20] Marx, *The poverty of philosophy,* 122, Marx and Engels, *Economic and philosophic manuscripts,* 210-216 (the communist manifesto), Clarke, 'Marx and the market'.

had still asserted that comprehensive factor markets were a revolutionary innovation of the nineteenth-century England economy. Profit maximizing behaviour, and the supply and demand price mechanism in fully open markets for land and labour, were not found earlier, according to him, and neither later, as in the twentieth century redistribution became more important again, now by way of the growing welfare state.[21] In stating this, and proposing a very strict definition of the market, he offered a useful warning against those who would too easily project our present ideas about modern, open and free-functioning markets on the markets of the past. In doing so, however, Polanyi seems to have overestimated the extent to which nineteenth-century markets and those of the present-day market economies conform to abstract ideas about freely-functioning markets. It is clear, for instance, that no land market in the past or the present is ever fully open and free, since land markets are always heavily influenced by tradition, familial relations and personal attachment, but to a growing extent also by zoning laws and state legislation.[22] Even the United States, as the champion of free markets, has its factor markets at present clearly influenced and regulated by the public authorities, by way of legislation, agricultural subsidies, monetary regimes, and regulation of financial markets, for instance.

North, in grappling with Polanyi's ideas, has done a lot to break the supposed dichotomy between market and non-market elements in the organization of exchange, and shown how they interact, complement each other and often are integrated within the market framework, with a crucial role of the state, especially in enforcement.[23]As North observes, if we would follow the strict definition of Polanyi, we would find markets nowhere at all, not even at present. Not only non-market elements play a fundamental role in the functioning of all markets, but market economies are also capable of accommodating and integrating non-market forms of exchange and allocation, and even make elements seemingly inimical to the market into a vital part of their functioning, as was the case in eighteenth- and early-nineteenth-century Britain and the United States with its slave labour and forms of indentured labour, used for instance on plantations, which were developed by entrepreneurs who used land markets and financial markets, and used complementary wage labour, and which produced for the commodity market.[24]

Moreover, market exchange often presupposes social relations between the exchanging parties. Human actions within markets are seldom atomized and solely driven by the pursuit of self-interest,

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[21] Polanyi, *The Great Transformation*, xxx, and Idem, *The livelihood of man*, 6-11, 43 and 276 (on ancient Greece). Finley, *The ancient economy*, 22-24, 33-34 and 158-160 equally argued against the existence of factor markets and market forces in antiquity.

[22] Van Bavel and Hoppenbrouwers, 'Landholding'.

[23] North, *Institutions*. See also North, 'Markets and other allocation systems' and Didry and Vincensini, 'Beyond the market-institutions dichotomy'.

[24] See Steinfeld, *The invention of free labor*, passim. For the integration of slaves in a capitalist market system: Bhandari, 'Slavery and wage labor', and for the Roman era: Temin, 'The labor market'.

but mostly embedded in social relations, if only by way of implicit trust or morality.[25] This is an insight elaborated by several historians, especially for markets characterized by insecurity, agency-problems or multiple-part transactions, as in long-distance trade or the credit market.[26] Ethnic ties or common beliefs and normative systems may be vital in this, as argued by Avner Greif for the so-called Maghribi traders, the group of Jewish merchants that held a firm position in the Mediterranean trade in the tenth to twelfth centuries.[27] However, even if exchange sometimes is virtually impersonal, as in some modern markets, still notions of fairness, honesty, reputation and trust play a role, bargaining between people may take place and all kinds of social mechanisms are at work. Formal and informal institutions complement each other within the market, and informal constraints that stem from personal and social relationships play a crucial role in guaranteeing the quality of market exchange and they buttress the more formal rules.[28] Also, markets require a government, public authority or third party, if only to protect property rights, enforce contracts and reduce insecurity in markets. To a large extent, state enforcement and formal institutions can form an alternative for social constraints, allowing for exchange to become more impersonal.[29] Although also social networks and social control, or guilds and trade associations, can offer some of this oversight, protection and third-party enforcement of contract, the role of government and public authorities in market systems is crucial and almost inevitable.[30] Even in the modern period, markets thus are socially and politically embedded, and markets and market economies are never fully free and ruled by the forces of open market competition alone.

Not only Polanyi *over*estimated the openness of "free" markets, but at the same time, and exactly because of his too strict definition of markets, he *under*estimated the role of factor markets in the past and their volume and dynamism.[31] Polanyi's ideas on the absence of real markets for land, labour and capital in the past, although highly influential over the past decades, have been nuanced in recent years. Recent economic historical research has highlighted the fact that factor markets did exist before the nineteenth century, and analyzed the ways in which they functioned. This attention for the history of factor markets was long overdue. Apart from scattered investigations, especially into the English land

[25] Classical statement: Granovetter, 'Economic action and social structure', Fligstein & Dauter, 'The sociology of markets'; and Nee and Swedberg, *The economic sociology of capitalism*.
[26] Muldrew, 'Interpreting the market: The ethics of credit'.
[27] Greif, 'Contract enforceability and economic institutions'. Compare, however, the critical notes by Edwards and Ogilvie, 'Contract enforcement' and Ogilvie & Carus, 'Institutions', who rather stress formal, legal rules and the role of public authorities.
[28] Nee and Ingram, 'Embeddedness and beyond'.
[29] Block and Evans, 'The state and the economy'.
[30] Block and Evans, 'The state and the economy'; Fligstein & Dauter, 'The sociology of markets', 113-116.
[31] McCloskey, 'Other things equal'. For ancient economies: Feinman and Garraty, 'Preindustrial markets', and Silver, 'Karl Polanyi and markets'.

market,[32] the rise and development of factor markets has hardly ever been systematically studied and was a rather neglected topic. Even though all kinds of assumptions were made in the literature, actual empirical research for the earlier periods was scarce.

This has changed from the late 1990's, as a stream of studies was published on the rise of markets for land, lease, labour and capital in late medieval and early modern Western Europe. Again the land market historiographically led the way, with four big volumes containing about a hundred studies on the pre-industrial land markets in Europe, appearing within only one decade.[33] In contrast, the pre-industrial lease markets remain relatively under-investigated, but still saw the publication of one volume on leasing in the pre-industrial North Sea area.[34] Similarly under-represented remain the labour markets, apart from separate studies on England and the Low Countries.[35] The pre-industrial financial markets have become much better investigated, with an influential monograph on credit in early modern Paris, various studies on markets for public and private debts in the late medieval period and a volume with papers on credit in the rural economy,[36] all published in recent years.

These recent studies, with their focus on (North-)Western Europe in the late medieval and early modern period, have yielded several insights. First, it is now clear that factor markets in many regions already at this time were large, not only in the towns but also in the countryside. These studies have broken, for instance, the pre-existing idea that private capital markets were an innovation of the eighteenth century; their rise started already in the late Middle Ages. Also, it is clear now that most of the agricultural land was regularly exchanged in the land market, with annual turnover rates at 1-3 %, which are not dissimilar from modern rates.[37] Moreover, large shares of the land were also leased out in competitive lease markets. In many regions, and especially along the southern shores of the North Sea, in the sixteenth century half to three-quarters of the land was leased out. Also, a substantial part of rural labour was performed for wages; in the sixteenth century this was between a quarter and half of all labour, with peaks up to 60 %.[38] The towns probably had similar shares of wage labour - defined as economically dependent but legally free contractual labour performed for an employer for payment of a wage. At that point, most of the land, labour, capital and commodities in these economies was

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[32] These studies emerged in the tradition of Vinogradoff, Maitland and Tawney. See, for instance: Harvey, *The peasant land market*.

[33] Feller and Wickham, *Marché de la terre*; Cavaciocchi, *Il mercato;* Van Bavel and Hoppenbrouwers, *Access to land*; and Béaur and Schofield, *Property rights*.

[34] Van Bavel and Schofield,*The development of leasehold*.

[35] For instance: Van Bavel, 'Rural wage labour' and Idem, 'The transition in the Low Countries'. See also Whittle, *The development of agrarian capitalism*, 225-304.

[36] Hoffman, Postel-Vinay and Rosenthal, *Priceless markets*, and Schofield and Lambrecht, *Credit and the rural economy*. For a short historiographic discussion: Zuijderduijn, *Medieval capital markets*, 5-13 and 249-268.

[37] Van Bavel and Hoppenbrouwers, 'Landholding', 28-31. For leasing: Van Bavel, 'The emergence and growth', esp. 189-195.

[38] Van Bavel, 'Rural wage labour'.

exchanged and allocated through competitive markets. The market had become the dominant allocation system there.

Second, the recent studies show that these markets were dynamic, fairly flexible and responded to changes in supply or demand. The functioning of the price-mechanism had already for long been investigated for late medieval and early modern grain markets, and these studies yielded important insights into the growing correlation of prices and integration of these markets especially in Northwestern Europe.[39] The price-mechanism is also shown to have worked in markets for land, lease, labour and capital. An example is the lease market in sixteenth century Holland, which quickly responded to the population growth and increasing demand for land by massive rises of lease prices, with nominal prices rising fourfold between 1520 and 1570. Likewise, there is the labour market, which all over Northwestern Europe showed a sharp rise of wages in the late-fourteenth century and a decline in the sixteenth century as a result of population movements. Equally sensitive was the capital market, which showed a robust decline of interest rates following the Black Death and the associated changes in the people/capital ratio.[40]

Compared to the commodity markets, however, the integration of these factor markets was generally less, and responses to shifts in supply or demand slower, especially owing to the non-economic elements within these markets. This is observed especially in the land market, with familial relations, customary rules, government legislation and lordly influence forming main elements in the exchange of land and the functioning of this market.[41] The same applies to the labour market, which was often interspersed with forms of dependency or customary rules, resulting in wage-stickiness, for instance.[42] It can be remarked again, however, that this is not fundamentally different from factor markets today.

The insight that these formal and informal rules of exchange and behaviour - the institutions -, shape markets, has led to many of these recent studies stressing the importance of the exact institutional arrangement of these markets for their functioning and highlight the changes in this arrangement over time. This emphasis links up with the rising popularity of New Institutional Economics, providing a lot of the theoretical background against which the same studies were framed. Also linking up with New Institutional Economics and its generally optimistic outlook on the progress of historical development, many of these studies show how non-market elements were reduced over time and allowed factor markets to function more openly. Most researchers would stress that this was not a uniform and unilinear development, but rather one with regional nuances and temporal ups and

[39] Tits-Dieuaide, *La formation;* Persson, *Grain markets in Europe*; and Jacks, 'Market integration'.
[40] For lease prices: Kuys and Schoenmakers, *Landpachten in Holland*. For interest rates: S.R. Epstein, *Freedom and growth*.
[41] Van Bavel, 'The land market in the North Sea area'. For wages: Van Zanden, *The long road*.
[42] Munro, 'Wage-stickiness'.

downs. Still, the same researchers often focus more on the rise of these markets than their stagnation or decline, and generally suggest that in Northwestern Europe this protracted process led to secure and open markets already at an early stage, that is, in the late medieval and early modern period.

These studies have even further sharpened the contrast with the picture sketched for other parts of the world. Studies on the exchange of land, labour and capital outside Europe are much scarcer, and they rather stress the absence of factor markets in the late medieval and early modern period. They show that especially the markets for labour and land remained weak and small almost all over the globe, up to the nineteenth century. This applies to areas like India and Southeast Asia, Africa and the Ottoman empire, but also to highly-developed societies like China and Japan.[43] A more optimistic picture of factor markets in China is offered by Kenneth Pomeranz, who especially stresses the favourable institutional framework of these markets.[44] In China, and perhaps even more in Japan, the exchange by way of the market indeed grew in importance in the early modern period, and Japan in the eighteenth and nineteenth centuries even possessed well-developed, secure markets for land and capital,[45] but the pace of this development had been much slower than in the North Sea area and the size of these markets remained modest.

Another observation is that the recent historiography on the topic shows a numerical dominance of English and Dutch researchers, and of studies focusing on these areas surrounding the North Sea. These are also among the few countries for which studies have attempted to assemble the newly-won insights into an overview of all factor markets. Bruce Campbell for England and the present author for the Low Countries, for instance, have done this for the high and late medieval period.[46] These syntheses show that several parts of England did see the emergence of factor markets in the twelfth and thirteenth centuries, and after some stagnation these further developed in the early modern period. In the northern parts of the Low Countries their rise was even more potent. These areas saw the rise of factor markets in the thirteenth and fourteenth centuries, and had most of the land and very substantial share of labour and capital exchanged by way of the market already by the sixteenth century. At that point, also the large majority of goods were produced for the market, and were allocated by way of the market, in order for market exchange to remain dominant since then.

Although this recent literature pushes back the rise of the prominence of markets and the development of market economies several centuries from what was commonly believed some years

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[43] Pamuk, 'Changes in factor markets', Van Bavel, De Moor and Van Zanden, 'Factor markets', and the contributions to this issue by Tirthankar Roy (on India), Gareth Austin (Africa) and Osamu Saito (Japan).

[44] Pomeranz, *The Great Divergence*, 69-82, and Idem, 'Land markets'. Much more negative is Huang, *The peasant family*.

[45] Saito, 'Land, labour and market forces'.

[46] Campbell, 'Factor markets', Van Bavel, 'The organization and rise', and Idem, 'The transition in the Low Countries'.

ago, the resulting chronology still suggests that factor markets are a relatively modern phenomenon – with other parts of the world bound to follow the leading example of Northwestern Europe at some point later in history. It also suggests that the rise of factor markets – which as a result of this recent research is now located even more clearly in Northwestern Europe, must have stimulated development and created wealth, since we are much wealthier now than in the past and also much wealthier than parts of the world where factor markets remained weak and restricted longer, or are still weak and restricted.

The latter impression, that is, the relationship between the rise of markets and growing wealth, seems to be underpinned by the reconstructions of GDP per capita, most obviously those by Angus Maddison. Even though he discredited the old, Malthusian view, that had assumed that before the modern period societies were unable to generate economic growth and were stuck at subsistence level, his survey for the different parts of the globe over the period from the first millennium up to the present-day still shows low levels and a modest growth of GDP per capita before the modern era. Maddison thus offers a powerful, compelling picture of how wealth growth took place especially in the last two centuries and how this was concentrated in the Western World, where this wealth growth was unilinear. More specifically, his figures show how societies in the pre-industrial period experienced low levels of wealth, just above subsistence level, that is at $ 400, where the bare bone subsistence level is mostly set at. Around 1300, GDP per capita in Western Europe, according to Maddison's estimates, was still barely above this level, at c. $ 600, slowly rising further to $ 800 around 1500 and $ 1,000 around 1700 and $ 1,200 around 1820, in a unilinear process of growth.[47] This growth in Western Europe accelerated from 1820 onwards, from about $ 1,200 to the high levels of the present. The wealth rise would thus have taken place in exactly the same period as factor markets in the traditional literature were thought to have developed.

In recent years, however, not only the dating of the growth of factor markets in Western Europe has been revised, which resulted in this growth now located a few centuries earlier than thought before, but also Maddison's chronology of wealth growth has come under revision. The start of this process, too, is now located earlier in time. The latest reconstructions of GDP per capita in the pre-industrial period show much higher levels for the late Middle Ages than assumed by Angus Maddison. Around 1300, most Western European economies according to these latest estimates would rather seem to have been at GDP per capita levels of $ 800, and many of them witnessed quite substantial growth in the following centuries, to levels of $ 1,000 – 1,500 in the sixteenth century.[48] Italy, where commodity and factor markets had developed earliest, had reached this high level first, already around

[47] Maddison, *The world economy: A millennial perspective*, 244-265, esp. 264.
[48] Broadberry, Campbell et al., 'British economic growth', table 24.

1300.[49] Growth took place later, but was even more pronounced in Holland, the western part of the Netherlands, with its late medieval development of thriving markets. Here, the growth of GDP per capita started around 1300, rising from c. $ 800-900 to $ 1,400-1,500 around 1500 and no less than $ 2,400-2,600 around 1600.[50]

Table I.1

Estimates of GDP per capita in Western Europe and in Holland (1300-1700, in 1990 $), by Angus Maddison ("traditional") and by recent investigators ("revised", by the authors mentioned in the notes 47-49).

	1300	**1500**	**1700**
Traditional (av.)	600	800	1,000
Revised (av)	800	1,000-1,500	1,200-1,600
Revised Holland	850	1,400	2,600

These recent calculations push back the start of economic growth in Western Europe several centuries. They form a welcome revision of earlier estimates, and they result in a fuller and more correct picture of developments, but still they point to the same causality as the older studies did, since the rise of markets and the start of economic growth still seem to coincide.

It seems hard to argue against the logic which links the rise of open and dynamic markets to wealth and productivity. And this is roughly the teleological story which is explicitly told, or at least implicitly suggested, by most of the few economists who discuss long-term economic developments, including David Landes and Douglass North. Actually, in their pioneering book Douglass North and Robert Thomas already in 1973 pointed to the Dutch case and the precocious development of markets there in the period 1500-1700 to demonstrate the value of their institutional approach.[51] A similar story

[49] Lo Cascio and Malanima, 'GDP in pre-modern agrarian economies', and Malanima, 'The long decline', esp. 186-188. See also the papers for the conference "Quantifying long run economic development", held in Venice in 2011.

[50] See broadly: Van Zanden and Van Leeuwen, 'Persistent but not consistent'. The underlying figures were kindly provided by Bas van Leeuwen, 4-2-2013.

[51] North and Thomas, *The rise of the western world*, 132-145.See also Landes, *Wealth and poverty,* 42-44, 59 and 442-458.

is told in 1997 in the study of Jan de Vries and Ad van der Woude on the economy of the Netherlands in the early modern era.[52] They posited that already in the sixteenth century especially its western part, Holland, possessed a highly developed market economy, characterised by a large market freedom, efficient markets and low transaction costs, resulting in "modern" economic growth. Even more optimistic about the effect of dynamic markets is Graeme Snooks, who claims that in twelfth-century England, and even under the difficult circumstances and mounting population pressure of the thirteenth century, the growing size and the efficiency of factor markets promoted a more effective allocation of resources, which in its turn allowed for a simultaneous growth of population numbers, technological innovation and real GDP per capita.[53] A not dissimilar story, but rather for the early modern period, is told by neo-marxist Robert Brenner, who links the English transition of the rural economy, the rise of agrarian capitalism and the working of competitive lease markets to the subsequent Industrial Revolution and the associated rise in labour productivity.[54] According to Brenner, loss of the means of subsistence and direct access to surpluses, which makes all actors fully dependent on commodity and factor markets, is necessary to have markets perform their favourable work and generate sustained economic growth. On this point, despite sharp differences in opinion on other issues, neo-marxists and neo-smithians are in broad agreement.

Recent empirical research also seems to underpin the idea that favourable market development and political and personal freedom reinforce each other. This is a point suggested by Jan de Vries and Ad van der Woude, who hinted at the absence of a genuinely feudal past as the main underlying case for the rapid growth of open markets in late medieval and early modern Holland. Similarly, the present author has associated the late medieval rise of dynamic land, lease and labour markets around the North Sea, and the different chronology in this, to the dissolution of manorialism and other forms of non-economic coercion, and showed how these reinforced each other in a positive feedback cycle.[55] Market development, increasing freedom and economic growth seem to have reinforced each other, in a process starting already in the late Middle Ages.[56]

The idea that open polities and open markets strengthen each other in a positive feedback cycle, resulting in economic growth, is stated in its most general form, and by surveying the whole of history, by Acemoglu and Robinson, and even more clearly by North, Wallis and Weingast.[57] North, Wallis

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[52] De Vries and Van der Woude, *The first modern economy,* 159-165.
[53] Snooks, 'The dynamic role of the market', 49-54 and 194-195. See for the criticisms on the work by Snooks: section V.1, x-x. See also Persson, *Pre-industrial economic growth*, esp. 65-67, 82 and 86.
[54] Brenner, 'The agrarian roots', and idem, 'Property and progress', 60-61.
[55] Van Bavel, 'The organization and rise', and idem, 'The transition in the Low Countries'. For Holland: De Vries and Van der Woude, *The first modern economy,* 159-165.
[56] Van Zanden, *The long road.*
[57] Acemoglu and Robinson, *Why nations fail*, esp. 76-77; North, Wallis and Weingast, *Violence and social orders*, esp. 129-133.

and Weingast make the robust claim that thriving market economies facilitate and sustain the stability of "open access societies", in several ways. Competitive markets provide for long-run economic prosperity and, therefore, promote the stability of the system, which in its turn provides for open markets. Also, the price mechanism promotes pluralism and civil society, since it signals disturbances and forces governments to act responsibly. Likewise, the international competition in open markets precludes the possibility of governments to take resort to rent-seeking policies and it forces them to offer credible commitments and secure property rights.[58] In some respects, this is a story not dissimilar from the one told by Friedman a few decades earlier.

North, Wallis and Weingast date the rise of these open access societies fairly late in time, in the nineteenth century, as first Britain and the United States made this step, but the first moves towards this type of society in their view were made in the sixteenth to eighteenth centuries.[59] In view of the recent investigations cited above, the start of these developments towards open markets, freedom and wealth can now be traced even further back in time, in the late Middle Ages. Even though some of the authors involved warn us that this was not an inevitable movement towards more efficient arrangements, they still all contribute to sketching a teleological process in which open polities and open markets reinforced each other, a process which started in Northwestern Europe and from here spread over the world. This seems to have become the new orthodoxy in economic history.

3. A new approach to market economies: the cases

Summarizing the preceding overview of the historiography, we can see how between the 1940's and the 1970's many influential scholars tended to situate the rise of markets - and especially factor markets – and sustained economic growth both in the nineteenth and twentieth century, suggesting a strong link between the two. The research of the following, most recent decades has pushed back the rise of factor markets in Western Europe to the late Middle Ages, and at the same time this research has now also located the start of "modern" economic growth in the late Middle Ages, in Western Europe. As a result, the advent of the two phenomena of factor markets and economic growth is now pushed back several centuries in time. This is to a large extent a justified and necessary correction of the older historiography, but still the notion remains that factor markets are a relatively modern phenomenon and part of a modernization process, with other parts of the world bound to follow the leading example of Northwestern Europe at some point in history. Also, the notion remains that the rise of factor markets must have stimulated growth and made us wealthy, and their rise in an interactive process was intimately linked to political and personal freedom.

[58] North, Wallis and Weingast, *Violence and social orders*, esp. 129-132. For the latter argument also: [North and Weingast, earlier work, *Structural change*, 1981?].
[59] North, Wallis and Weingast, *Violence and social orders*, 27 and 69 ff.

These notions, which emanate from more abstract, theoretical works and also from recent historical, empirical research, will probably stick in the economic and historical literature for the coming period. The field of economics is not likely to change this conception in the coming years, since it deals mainly or even almost exclusively with the modern period, and more specifically with its contemporary part, and can hardly be expected to develop a new view on the pre-modern period. Mainstream economists either focus on short-run analyses, and not on long-term economic changes, or their knowledge of these changes is highly abstract and based on theoretical concepts.[60] We, therefore, run the risk of ending up with a picture of markets rising and economies growing, and of these phenomena happening more intensively and earlier than we thought before, while we do not have a picture – let alone an explanation – for markets declining and economies stagnating after these periods of growth. Are the rise of markets and economic growth indeed connected, and how are the exact chronology and causality? And is this a one-way development or can market economies and their markets decline again, and how?

In this paper, and more extensively argued in a coming book, I argue that the insights of the recent period, combined with new, empirical research of the last years, could allow for an alternative approach, or perhaps even require us to adopt such an approach. True enough, markets are now more dominant worldwide than ever before, and perhaps they are less influenced by non-economic elements than in the past, but such an approach would break the one-sided or even teleological view which associates dynamic markets – and especially factor markets – with modernity and with modern welfare. Using and combining the insights from recent, empirical research on early market economies,[61] we can show that factor markets are not modern, but existed in several periods throughout history. This early appearance in history even applies to market economies, that is, economies which to a large extent, or even predominantly used markets to exchange not only goods but also land, capital and labour.

Earlier studies on markets and their effects in the very long run mostly focused on commodity markets,[62] but here the focus is especially on *factor* markets. Whereas commodity markets are almost universal in history, and thrived in many places and times,[63] factor markets were more rare, since many other, feasible ways of exchanging and allocating land, labour and capital exist, including those offered by the state, family and kin, and horizontal associations. Factor markets are much more intriguing.

[60] Snooks, *Economics without time*, 39-44.
[61] Here, I am endebted to many colleagues, in Utrecht, the Low Countries and elsewhere in the world, but especially I would like to mention the young scholars who worked with me at Utrecht University in recent years: Michele Campopiano, Daniel Curtis, Jessica Dijkman, Erika Kuijpers, Auke Rijpma and Jaco Zuijderduijn.
[62] See, for instance: Persson, *Grain markets in Europe*.
[63] Braudel, *Les jeux de l'échange*, 93-110 ('Partout des marchés et des boutiques').

They do not deal with inanimate goods and products, but directly affect each person's labour power and their most valuable assets, their land and capital. Land is not just a commodity but, especially in agrarian societies, the main source of status, power, continuity and subsistence, a role in part taken over in industrial societies by capital and capital goods. As a result, the rules regarding the exchange of land, labour and capital are often much more elaborate and influenced or even dictated by values, norms and traditions than those regarding goods and products. Market exchange of labour and capital possesses another complexity, which generally is not found in market exchange of commodities, that is, it requires an ongoing, repeated interaction between the parties involved, which cannot be fully determined on beforehand and will only be completed at some point in the future, in contrast to a one-time sale of a commodity. This creates insecurity, and requires a more elaborate institutional arrangement, with a potentially large role of informal institutions. Combined, factor markets differ far more in their institutional arrangement, and therefore arguably also in their effects, than commodity markets do.

For one more reason factor markets differ more in their effects. While commodity markets may allow for some degree of wealth accumulation, especially in the hands of those who are successful in these markets, the presence of land (sale and lease), labour and capital markets is required to make accumulated wealth really profitable and to allow for higher degrees of wealth accumulation. Factor markets, therefore, may enable monumental changes, including changes in the distribution of resources and power over social groups, especially when they become dominant. These cases of market economies, and the differences in arrangements, their changes over time and their long-run effects, are central to this paper.

Most of the research on market economies focuses on the modern period and on those cases where markets are clearly dominant at present, that is, on Western Europe and the Western offshoots. This easily leads to teleological reasoning and it disallows a more systematic approach. Here, I will try to avoid this, by employing the full opportunities history has to offer and making an inventory of those societies in history where markets at some point have become the dominant form of allocation and exchange of land, labour and capital. In compiling this inventory, I include economies with markets that are not fully open, competitive, impersonal and free, since if we would rule them out, we would find market economies nowhere at all, not even at present, as observed above.[64] Neither do the market economies in this inventory have the market as the sole system of exchange and allocation. Other systems do co-exist next to the market in these cases, but the market is the dominant one.

[64] See the remarks on Polanyi's approach, which is too strict and – in a way perhaps surprising to Polanyi himself - anachronistic: section I.2, x-x.

When we want to compile an inventory of early market economies, that is, economies where the market was the main system of exchange and allocation, we are hampered by the scarcity of sources, especially for the periods far back in history. In several cases, we can only rely on indications and we can in any case not assess the importance of markets in a quantitative way. Still, the number of qualitative indications we can rely on has grown considerably over the past years, thanks to the progress made in this field. Even though the following survey still cannot claim to be exhaustive, we know much more now than only a few decades ago.

A first case to consider as a possible market economy is Iraq, or Babylonia, in the first centuries of the second millennium BC. Babylonia in this period possessed thriving markets for goods and products, but also for land, lease and labour. From at least the middle of the third millennium BC, temples and notables leased out their land for part of the crop - usually one-seventh or one-eight - or a fixed amount of silver. In the nineteenth century BC written lease contracts start to appear, with the numbers rising in the eighteenth and seventeenth centuries.[65] Also, loans with interest of silver and grain between or with private parties involved, did exist in the late-third millennium BC, with interest rates of 50 % or 33.3 % per year, although the volume and competitiveness is perhaps not sufficient to label it a real market.[66] Wage labour had become important around the year 2000 BC, and gained further importance in the subsequent centuries.[67] In later periods, references to wage labour dwindled again, and hiring labour was often alternated, or became mixed, with corvée labour, dependent labour or even outright coerced labour. Likewise, the other factor markets declined again.

A next case is perhaps Iraq in the neo-Babylonian period. The long sixth century BC, which is relatively well-documented thanks to thousands of remaining tablets and became well-investigated thanks to the recent work by Michael Jursa in particular, showed a strong demographic growth and urbanization, monetization of exchange and the growth of land and especially labour markets, with an associated rise of cash crop production, regional specialisation and occupational specialisation.[68] Another candidate as an early market economy is the northern part of China during the fourth to second centuries BC, as the society became market-oriented, combined with first the introduction and later an enourmous boom in the production of copper, bronze and other coins used in market transactions.[69] This part of China became highly monetized, as witnessed by an extensive administration of salaries paid in the private sector and by the state, and by the evidence on the buying and selling on credit.

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[65] Mauer, *Das Formular der altbabylonischen Pachtverträge*; Leemans, 'The rôle of landlease in Mesopotamia'.
[66] Steinkeller, 'Renting of fields', 141-143.
[67] Silver, 'Karl Polanyi and markets'; van Bavel, 'New perspectives'.
[68] Jursa, *Aspects of the economic history*; and Idem, 'Factor markets in Babylonia'.
[69] Scheidel, 'The monetary systems', and Wang, 'Official salaries'.

Italy in the second century BC to the third century AD also may be also qualify as a market economy. In this period, from the second century BC, Italy saw the rise of commodity and also factor markets. Even though there was the widespread use of slavery, Rome had a well-functioning labour market, with the wages of free labour fluctuating, influenced by supply and demand, and organized through clear labour contracts.[70] This period was characterized by rising urbanization and economic growth, with GDP per capita in Roman Italy perhaps reaching levels of $ 1,400, that is, similar to seventeenth-century England.[71]

A next case is Iraq in the early medieval, or early Islamic, period.[72] Land sales in this period became easier than before and sales of land were widespread, as all kinds of indicators show. Also, leasing and later sharecropping leasing became more important.[73] Most labour was performed within forms of tenancy and through free or semi-free independent labour, while also wage labour was employed. The rural economy in this period was highly monetized and market-oriented, within a system of private landownership. Moreover, and in contrast to common ideas about Muslim restrictions, credit and capital markets started to blossom. Iraq developed highly advanced financial markets and it counted numerous money changers, pawnbrokers and merchant-financiers, and the latter employed sophisticated instruments including convertible bills and promissory notes as early as the mid-eighth century.[74] This period of dynamic factor markets lasted to around the turn of the millennium.

Perhaps the Lower Yangtse delta in China in the period between c. 1000 and 1400 forms a similar case. Especially in the eleventh and twelfth centuries, during the Song dynasty, as all kinds of restrictions on market activities were removed, markets have flourished.[75] The output of copper coins, used by people involved in dynamic markets and indicating the prevalence of labour and commodity markets, was bigger than in any earlier or later period, at 800 to 1,300 million coins a year.[76] This major coin production – and especially of small coins used in small-scale transactions in labour and commodity markets – may be used as an indicator of deep monetization and dynamism of markets.[77] Also, in the eleventh century, paper money made its appearance, next to an increasing use of bills and promissory notes, and a proliferation of credit. The Song period was also one of remarkable urban

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[70] Temin, 'The labor market'; Temin, *The Roman market economy*.

[71] Lo Cascio and Malanima, 'GDP in pre-modern agrarian economies', revising earlier estimates, including those by Angus Maddison.

[72] Van Bavel, Campopiano & Dijkman, 'Factor markets in early Islamic Iraq'. See also Shatzmiller, 'Economic performance and economic growth in the early Islamic World'

[73] Campopiano, 'Land tax ʿalā l-misāha and muqāsama'.

[74] Udovitch, 'Reflections on the Institutions of Credit and Banking'.

[75] Shiba, *Commerce and society*, 127-130; Liu, *The Chinese market economy, 1000-1500*.

[76] Lucassen, 'Coin production'; Glahn, *Fountain of fortune*.

[77] As argued by Lucassen, 'Deep monetization'.

growth, including the rise of smaller market towns, perhaps even an urban revolution, associated with growing trade and specialization of the economy.[78]

The next one is the first case where the sources, which are available to a much larger extent than for the earlier cases, allow us to assess the importance of factor markets at least somewhat more quantitatively. This is the center-north of Italy in the late Middle Ages. Here, next to the already existing commodity markets, also markets for land, lease, labour and capital, after a stage of growth in the eleventh century, developed and grew especially in the twelfth and thirteenth centuries.[79] By 1300, for instance, short-term leasing here had become highly important; in some parts of the areas up to three-quarters of the land was leased out for fixed or sharecropping leases.[80]

A little bit later, in the thirteenth and fourteenth centuries, a similar rise of factor markets took place in the Low Countries.[81] In the sixteenth century, these markets had become dominant and most of the land and very substantial parts of labour and capital were exchanged by way of the market, especially along the southern shores of the North Sea. Half to three-quarters of the land there was leased out and between a quarter and half of all labour, with peaks up to 60 %, was performed for wages.[82] In the fourteenth century, thriving credit markets also developed, both in town and countryside.[83] Also, by far the most of the goods were produced for the market, and were allocated through the market.

A next, even more familiar case is England. After the growth of factor markets in the fifteenth and sixteenth centuries, more than half or even up to three-quarters of all agricultural land in England around 1600 was leased, while the proportion of wage workers in the total rural population amounted to between a quarter and a third.[84] At that point, large shares of even most of land, lease land and labour allocated through the market, even though many customary and non-market determined elements continued to play a role in these markets. In the seventeenth century, many of the remaining non-economic considerations were removed and replaced by the cash nexus.[85] The remaining manorial and customary restrictions on land transfer were targeted, while the growing availability of mortgage finance also pushed up the activity of the land market, which was buoyant in the seventeenth century.[86]

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[78] Elvin, *The pattern*, 117-118, 128-130, 146-150 and 167-178.

[79] Van Bavel, 'The organization and rise of land and lease markets'.

[80] Cherubini, *Signori, contadini, borghesi*, 73-83, 295-298 and 358-364, and for the Florentine countryside: Conti, La formazione, 97-102, 245 and 395-411.

[81] Van Bavel, 'The medieval roots'.

[82] Van Bavel, 'Rural wage labour in the sixteenth-century Low Countries'; van Bavel, 'The emergence and growth of short-term leasing in the Netherlands'. See also: de Vries & van der Woude, *The first modern economy*.

[83] Zuijderduijn, *Medieval capital markets*.

[84] Whittle, *The development of agrarian capitalism*.

[85] Overton, *Agricultural revolution*, 147-188.

[86] French & Hoyle, 'The land market', 353-359.

Especially after c. 1650, market competition for land led to small peasant landowners losing their landownership to yeoman farmers or big landholders, who subsequently leased out the land. In this period, England developed into a market economy, with very substantial and dynamic markets for land, lease and labour. The last market to emerge was the financial market, in the late-seventeenth century.[87] At that point, investment capital had become abundant and financial services more advanced, while newly-established joint-stock companies offered new opportunities for investment and speculation.

Surprisingly, the number of potential market economies does not grow exponentially now we have entered the modern period, as we would have to wait another one of two centuries to find a next society where factor markets became dominant, the United States. Here, the growth of factor markets can be located particularly in the eighteenth century, and their breakthrough to dominance in the period around 1800, as with the credit market, or in opening decades of the nineteenth century, as with the rural labour market.[88] The years 1800-1820 saw a westward flood of farmers and speculators, who bought and sold land, used credit markets, hired wage labourers and stimulated transport and banking services.[89] At that point, the United States, had become a market economy. Only six to ten other cases we know of in world history preceded the United States. Only from the nineteenth century onwards, the number of market economies starts to grow and multiply, a growth accelerating in the final decades of the twentieth century. Still, this does not mean earlier periods, before the nineteenth century, did not have any market economies, as the preceding shows.

Table 1

Cases / possible cases of market economies, with a rough indication of the period

??Babylonia	Ur III / old-Babylonian period	c. 2100 - 1600 BC
?Babylonia	neo-Babylonian period	c. 700 - 300 BC
??North China		c. 400 – 100 BC
?Italy	Roman period	c. 200 BC – 300 AD
Iraq	early Islamic period	c. 600 – 1000 AD
?Lower Yangtse	Song period	c. 1000 – 1400 AD
Italy		c. 1100 – 1500 AD
Low Countries		c. 1300 – 1700 AD

[87] Murphy, *The origins of English financial markets*, 11-25 and 37.
[88] Rothenberg, 'The emergence of farm labor markets'; Rothenberg, 'The rise of a capital market'.
[89] Larson, *The market revolution*, 29 (land speculation), 63 and 71-72 (wage labour); Kulikoff, *Agrarian origins*, 44.

England	c. 1500 –
United States	c. 1800 -

Some of these cases have been identified earlier as examples of pre-industrial "golden ages", as by Jack Goldstone, for instance, who singled some of them out as economies which witnessed an efflorescence or significant upturn.[90] Indeed, all of the cases listed in the table above also were the economic leaders of their periods and operated at the cutting edge of economic development. Here, however, the focus is not primarily on economic rise and decline, but on an aspect of these economies that seems not to be noted by Goldstone, that is, that they all were market economies and primarily used the market to allocate and exchange land, labour and capital. The rise and decline of these cases as market economies will be central to the remainder of this paper.

4. A new approach to market economies: hypothesis

Of the cases listed above, especially the three major, pre-industrial examples of successful market economies in western Eurasia are relevant for further research: Iraq in the early Middle Ages, Italy in the high Middle Ages and the Low Countries in the late Middle Ages and the early modern period. These three cases are the main examples of market economies in this part of the globe during these successive periods. These societies used the market as a major or even the main system of exchange and allocation, not only for goods and products but also for land, labour and capital. In this sense, Iraq was exceptional in the early medieval period, and to a large extent this also applies to Italy in the high Middle Ages and the Low Countries in the late Middle Ages. These cases thus stand out because of the importance of the market and the dynamism it created. Also, in contrast to some of the earlier possible cases, as most notably Babylonia, these three cases have left us sufficient source material to thoroughly investigate all relevant aspects of their development.

Each of these cases in its period underwent a clear cycle, and at some point reached the highest level of economic development in Western Eurasia, or even in the world as a whole: Iraq in the eighth and ninth centuries, Italy in the thirteenth and fourteenth centuries, and the Low Countries in the sixteenth and seventeenth centuries. Each at that point reached levels of market involvement and levels of GDP per capita higher than anywhere else. If positive effects of market development can be expected anywhere, it would be in these three cases that operated at the extreme margin of economic development and growth. Despite this dynamism and growth, however, they all three witnessed stagnation or even decline after some time and they lost their leadership to another area, and saw their markets dwindle. The development of these early market economies thus shows that markets are not

[90] Goldstone, 'Efflorescences and economic growth'.

always rising, but after some time they stagnate and decline again. This already severs some of the assumed link between markets and modern wealth, and they may form a powerful antidote against teleological assumptions on markets and their beneficial effects.

On the basis of the research done recently into these cases, we can go even further by probing an alternative explanation of the formation, functioning and development of market economies in the long run. This explanation would envisage the development of these market economies as a cycle. I hypothesise, firstly, that factor markets emerge and become dominant especially in societies characterized by an already high level of welfare and development and, even more conspicuously, by a social balance emerged in the previous period. In all cases analysed, this balance originated from a series of large-scale social revolts, social upheaval and growing freedom and self-organization of ordinary people, in which the power of old elites was broken and gave way to a relatively wide dispersal of property and power. At the same time, the systems of exchange and allocation connected to these old elites were undermined or even done away with, whether they be systems of serfdom and manorialism, arbitrary levies by lords or heavy taxation by state elites. The destruction of these allocation systems also meant that exchange and allocation of land, labour and capital by way of the market became more feasible.

After their rise, factor markets in these cases created dynamism, especially in the exchange of land, labour and capital, but less real growth, apart from the first stages of development. The economic growth they brought in the first stages of their rise, was mainly the result of the flexibility they offered in the exchange of production factors, which enlarged the scope for specialization and division of labour. For another part, however, the economic growth these markets generated was no more than the commodification of social wealth created by these societies in the period preceding that of market dynamism, in which they had used other exchange and allocation systems than the market to build this wealth. More specifically, the dynamism that resulted from the rise of factor markets allowed a few groups to transform the social welfare and social gains amassed in the previous period (such as social networks, services produced outside the market, leisure time, social security) into economic assets and to appropriate them. This seemingly pushes up economic growth, because formerly unpriced assets now pop up in calculations of GDP per capita, but this increasingly happened at the expense of social welfare and equity.[91] In the longer run, and combined with the effects of market competition, it created social polarisation and an ever more skewed distribution of property and power.

[91] One way to observe this discrepancy between economic growth and declining social welfare for early periods is through the analysis of average heights: Steckel, 'Strategic ideas in the rise of the new anthropometric history'.

It is hypothesized, also on the basis of an analysis of the main cases of market economies, that the balance between social groups of the first phases is bound to become disrupted when, in the next phase, the market became dominant as the mechanism of allocation of land, labour and capital. This phase was in Iraq in the eighth and ninth centuries, in Italy in the thirteenth and fourteenth centuries, in the Low Countries in the sixteenth and seventeenth centuries, and in England in the mid-seventeenth century to the nineteenth. Even if alternative exchange and allocation systems did not fully disappear, the market at that point assumed a dominant position. This allowed the group, or groups, who benefited most from this organization of exchange and the ensuing economic developments to gradually acquire a dominant position, by the accumulation of property and, subsequently, of political leverage. This can be demonstrated by reconstructions of the distribution of land and capital, and the changes in this distribution over time, and of the control various social groups could exert over offices, legislative bodies and other forms of authority, both at the time of the emergence of factor markets and during their functioning. These show a growing skewdness in the course of the period. This process particularly occurred as a result of exchange and allocation being organized by way of factor markets, because of the keen competition and dynamism they bring, and the opportunities they offer for accumulation of land and capital, that is, of wealth.

In this sense, the markets for land, labour and capital were suitable instruments for elites or nascent elites to break up restrictions on the accumulation of land and capital, to better gain access to surpluses, to acquire and accumulate more capital and land, to make it easier to invest surplus capital, to make it more profitable to possess more land and capital than needed for subsistence and to get access to wage labour in order to make land and capital goods profitable. This formed an incentive for these groups to further stimulate the rise of markets, and especially factor markets, either directly or indirectly by way of their increasing hold over the state which offered them the opportunity to dismantle obstructions or alternatives for the market, as were offered by the guilds or the commons. At the same time, other social groups, forming the majority of the people, lost agency and saw their opportunities to shape economic and political life dwindle.

This development, it is hypothesized, subsequently created sclerosis of the institutional organization of exchange and allocation, or even the deterioration of these institutions. Alternative institutions outside the market which had earlier sustained development and growth, like the guilds and communal associations, now might become eroded or were pushed aside, and their positive effect on market exchange was lost. Even more detrimental would be the effect of the interference of the ever more dominant social groups which had benefited from the growing market exchange. They tended, it is hypothesized, to freeze and preserve the market institutions which had exerted their beneficial effect to them and had helped them to come to the fore, or even skew these institutions to

better suit their interests. Next, the sclerosis and deterioration of market institutions blocked any necessary adaptations, and this reduced the quality of markets, and finally caused them to stagnate or decline again. Different from North (and Wallis and Weingast), I see this process not as a result of the detrimental effect of non-market forces, but rather as the endogenous effect of the forces called forward by the dominant markets themselves and the market elites they created. This forms a self-reinforcing process: power-holders solidify their economic and later political domination and acquire formal-legal power as well, which they use to sustain the institutions that benefit them.[92] Because the now dominant groups increasingly used their revenues to obtain means of coercion and luxuries, and less to make productive investments – for instance in new technology -, and they also left other groups fewer opportunities and means to make these investments themselves, the economy stagnated or even declined. Combined with the social polarization and the negative externalities of market competition, this led to a decrease of average welfare.

An important element in this hypothesis is the link between markets and the social distribution of property and power, an element missing in most neo-classical and neo-institutional analyses of the formation, functioning and effects of markets. This absence of the social dimension is remarkable, when viewed in the light of the legacy of both Karl Marx and Adam Smith. Obviously, Karl Marx stressed the political economy of markets and their resulting accumulation of capital and social polarization, but the same applies to Adam Smith. The latter is hoisted on the shield as the champion of neo-liberal thought by many present-day commentators, but perhaps they would not have done so if they would have read his works. Smith's ideas about the functioning and the effects of markets can only be understood when taking into account the social context and the social distribution of property in which he envisaged these markets to function.

Smith argued that accumulation of capital is necessary for production to improve, but he saw this preferably as the result of the accumulation of smaller, individual savings, and he reasoned from a situation typical of the early-modern, pre-industrial world in which he lived, which was characterized by relatively small-scale, owner-managed production.[93] Commodity markets, according to him, would exert a positive influence and allow for specialization and division of labour, but they would work best with individual, small-scale buyers and sellers, who had symmetrical exchange relations and could not individually influence the market, in a situation of atomistic competition. Also, Adam Smith, although mostly optimistic about the commercial society, discussed the greed and selfishness that might be

[92] More in line with Acemoglu, Johnson and Robinson, 'Institutions as a fundamental cause', 388-396.
[93] Smith, *Wealth of nations*, volume 1, 14-30. For exactly this idea, Adam Smith was criticized by Brenner, 'Where Adam Smith went wrong', who sees productive rises only occur if producers are fully market-dependent. See also Clarke, 'Marx and the market', 9 and 11.

associated with the growth of commerce and with growing numbers of merchants and manufacturers, despite their useful role in the economy, and he was concerned about the poverty and inequality that would remain even in a well-functioning, free market economy, which would require the state to step in.[94] This contrasts with the ease with which many of his later adherents leave out any considerations of power and property, and believe that these markets will reinforce a situation of equity, since the effect of the market system in the long run would be relatively egalitarian compared to other systems with their much higher inequality in income and wealth, while they also assume that monopolies would be negligible in a free market economy, if only individuals are freely allowed to pursue their own interest.[95] These are assumptions which can be questioned on the basis of closer scrutiny of the known, historical cases of market economies. These allow us to look at the long-term effect of market exchange on the distribution of property and power, and at the effect of changes in the distribution of property and power on the organization of market exchange, and this shows a very different picture.This picture is rather one of a feedback-cycle between institutions, economic development and society, in which the rise and dominance of dynamic factor markets changes the social fabric and results in a new, negative institutional framework in which markets and welfare decline again.

[94] Smith, *Wealth of nations*, [I.i.10.2 par 61, V.i.b.2], 668-670 and 781-782. See also Sen, 'Uses and abuses', esp. 262 and 266.
[95] Friedman, *Capitalism and freedom*, 121-136, especially 133 where he invokes Adam Smith's invisible hand, and 161-176.

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