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Financial Predominance and International Economic Leadership

When crisis hits the international economy, the world looks to the United States for leadership. The American dollar remains the world's primary reserve and trading currency, and the preferred safe haven for wealth when there is trouble elsewhere. There are multilateral institutions designed specifically to take the politics out of the management of the international political economy, to make it a rule-based rather than a power-based system. But these institutions remain beholden to the United States, both for their financing and their decision-making. The United States in other words, whether by its intention, the intentions of others, or simply as a result of the structure of the global economy, is an international economic and monetary leader. But this leadership has raised questions. How committed is the United States to international leadership? How has its ability to lead been affected by the various changes in relative capabilities and institutional structure in the past quarter century? How has it been affected by the end of the Cold War?

The role of the United States as an economic leader is complicated by other political roles that it plays in the international arena. A country can lead militarily, ideologically, diplomatically. Leadership is sometimes seen by contemporary analysts as a general phenomenon, in which a country acts hegemonically with respect to all aspects of the international system.[1] But various aspects of international leadership need not correlate, and historically have not always done so. Moreover, there is no reason to expect that they will necessarily do so in the future. International economic leadership, as it is understood here, does not require military predominance, and does not require broad diplomatic leadership outside of the economic sphere. It requires only that a country be willing to provide a commercial infrastructure to the international economy of the sort that governments try to provide for their domestic economies.

One can thus make some generalizations about the role of international economic and monetary leaders. They all fulfill forms of the functions that, as we saw earlier, the United States is looked to for today. They supply international commerce with a core currency, they act as a focus for confidence in the economic systems that they lead, and they provide the source for the norms and rules through which the system operates.[2] But beyond these generalities, different leaders lead in different ways, and create very different international economic systems. Leaders do not lead purely for the good of the system; they act also (perhaps primarily) to pursue their own interests as they see them, and interests can vary substantially across time and place. These interests can be purely economic, but can also be driven by security concerns or ideology. To understand how the global economy got to where it is and to speculate on where it might be going, we must understand the role of the United States in leading it for the past half century, and have insight into what paths this leadership might take in the future. To understand this particular example of leadership, we must understand the broader phenomenon, the patterns that international economic and monetary leadership can take and the constraints on it.

International economic and monetary leadership is not a new phenomenon. From the beginning of the evolution of the contemporary global economy in medieval times, there have always been economic centers that were looked to for commercial and monetary leadership and that had overwhelming influence in the creation of the norms and rules that governed economic transactions across political units.[3] The banking centers of Northern Italy and the trading centers of the Hanseatic League in Northern Europe were the catalysts for processes of economic expansion that led directly to the evolution of the global market that we have today. Since that time, periods of sustained expansion of international economic activity have been associated with leadership by specific political units, originally cities and for the last several hundred years states.[4]

Similarly, the study of international economic leadership is not a particularly new one in the field of international political economy. It has been periodically going in and out of vogue for some three decades now.[5] Yet studies of this phenomenon have tended to be, in the end, unsatisfying; they have focused on either the generalities of leadership, or certain specific historical examples, but have not succeeded in integrating the two. One study might, for example, find general measures that predict when leadership might happen,[6] another might trace the particular trajectory of a leader's participation in the management of an international monetary system.[7] The former is of limited specific utility; international economic leadership is a broad category of behaviors, and thus predicting simply its presence or absence gets us only one small step along the path to understanding the phenomenon. Furthermore, finding predictors of economic policy that work across historical eras is a tricky proposition, as economic measures, the technologies of commerce, and even basic understandings of the nature of economics change.[8] The latter, the historically specific study, is a necessary precondition for the study of the broader category of international economic leadership, but without historical comparison, without analysis in a broader context, it does not by itself constitute such a study.

The phrase 'international economic and monetary leadership' is used here with a specific, and narrow, definition. It refers to the provision to the international political economy of a particular set of infrastructural public goods, to be discussed in the next chapter. This book makes no argument about broader patterns of leadership or hegemony in international politics. How does one center of economic decision-making come to be the source of this particular kind of leadership? What forms can this leadership take, and what is the relationship on the one hand between domestic politics and national interest in these leaders, and on the other hand between the expressed national interest and the structure and norms of the international economic system that the leader builds around it? The purpose of this book is to put the phenomenon of international economic leadership into this broader context. Doing so requires both a discussion of the phenomenon as a general form, and an exploration of patterns of leadership as specific historical events. The starting point for this exploration is the year 1600, when the city of Amsterdam first appeared at the focal point of the European trading system. This appearance marked, arguably for the first time, the emergence of a truly global economy, and of a truly global economic leader, as distinct from the pattern of overlapping regional systems that had been the case previously. Regional systems remain, but the past four centuries have been remarkable for the ultimate reliance of all these systems on one central focal point.

THE ARGUMENT

The two questions previously posed can be restated in their simplest form: When will a country become an international economic leader, and what will the content of its leadership be? These two questions are distinct, but related. The answer to each depends on a number of factors, both structural constraints delimiting the scope for action, and forms of political interaction that enable the expression of interests as state policy. The logic of international finance provides a basic structure by which both states and markets are constrained; prevailing commercial technologies and accepted understandings of how economies work provide the backdrop against which decisions are made; political structures supply the conduits through which various kinds of interests are expressed, mediated, even created. It is through the interactions of these various factors in their specific historical settings that the questions posed by this book can be addressed.

The answer to the first question, that of when countries become leaders, depends on two factors, which will be referred to here as capabilities and motivation. A country has the capabilities when it possesses the requisite resources for leadership, however those resources might be defined. Motivation refers to the desire to lead, and more specifically to the set of interests that policy-makers wish to see addressed. Most studies of leadership to date have focused on one or the other of these factors, either trying to create specific measures of when a country is likely to adopt a leadership role or discussing why a country might want to become a leader, and what sort of leader it is then likely to be.[9] The two factors cannot, though, be successfully isolated. A country without sufficient capabilities, it is true, will lack the economic wherewithal to lead effectively. It can try, but it is unlikely to succeed. Britain during the periods of reconstruction following both of the twentieth century's world wars, for example, would have liked to recreate its late-nineteenth-century leadership role, but did not have the financial wherewithal to do so.

But one cannot reasonably infer that countries that have the capabilities will then choose to lead, or assume that their leadership will be of a specific type; capabilities are necessary, but are not sufficient. By the same token, one cannot infer from arguments about the motivations of a specific leader, be it Britain in the nineteenth century or the United States more recently, what leadership in general entails. For example, British economic leadership in the second half of the nineteenth century was largely unilateralist, which is to say not particularly dependent on the policies of other countries. In contrast, American leadership in the second half of the twentieth century involved an important element of multilateralism, action taken only in concert with others. At the same time, British diplomatic policy was somewhat divorced from foreign economic policy whereas American diplomatic policy was intimately intertwined with foreign economic policy. Both were leaders, but their patterns and methods of leadership differed in fundamental ways.

In other words, discussion of international economic leadership as a general phenomenon can mask important, even fundamental, differences in the foreign economic policy of the leader, and in the shape of the system of global commercial exchange that the leader underwrites. What explains these differences? To a certain extent, as with all histories, the differences can be described as historical fluke, as the result of a set of individual decisions by individual decision-makers that cumulatively lead to a result that was never part of any grand design. And these decisions are affected by the broader global contexts, both physical and political, in which leaders find themselves. The institutions of international commerce, for example, are necessarily going to be different in a computerized world than they were before the discovery of electricity, and economic leadership in a bipolar world may well be a victim of very different geopolitical pressures than the equivalent in a multipolar world.[10]

But differences in patterns of leadership are generated not only by forces outside of the leader and accidents within it. They depend to an important degree on the reason that policy-makers within the country chose foreign economic policies that fulfill the functions of leadership in the first place. In other words, they stem from differences in motivation. Put simply, policies of international economic leadership entail certain costs to the country that undertakes them, the opportunity costs of benefits that might have been had from following other policies. It is therefore reasonable to expect that decision-makers will want to have good reasons for accepting these opportunity costs and engaging in leadership behavior.[11] Leadership policies, as we shall see, benefit some domestic groups, some sets of domestic economic interests, at the expense of others. The willingness of a country to act as an international economic leader depends to an important degree on the ability of those who benefit to affect national foreign economic policy-making. An important input into the form of leadership chosen is the relative domestic political strength of those who benefit from leadership, and the policy demands of other interest groups that would rather use the means of national foreign economic policy to pursue other goals.

In short, then, the two factors of capabilities and motivation must be addressed in tandem. It is only by combining the two that we can understand, for example, why at the onset of the Great Depression in 1929–1930 Great Britain tried to act as leader and failed, and the United States was looked to as a leader but failed to try.[12] Britain was motivated but not capable, the United States was capable but not motivated. A more nuanced reading of national capabilities can tell us much about the potential strength of leadership, and a more nuanced reading of patterns of national motivation, and the domestic politics underlying those motivations, can help to answer the question of what the content of international economic leadership will be under a given leader.

Which begs the question of what gives states the capabilities to act successfully as leaders, and what motivates them to want to do so. A variety of different answers have been given to this question, ranging from broad measures of aggregate size in general to export performance in particular.[13] The argument here is that it is one very specific activity that both empowers and motivates a country to act as leader: international finance, defined as investment in other countries and in the mechanisms of international trade and commerce. A country that is predominant in international finance will be capable of acting as a leader, whether or not it is dominant internationally in other fields, be they economic or military. Conversely, a country that is not financially predominant will not be able to act as an economic leader, even if it does predominate in other economic fields, or in military capability.

At the same time, the internationalist financial community, those who invest in the international economy, have a vested interest in providing leadership, because the provision of leadership to the international economy increases the profitability of investing in it. This logic applies to international financial interests whether or not they reside in financially predominant countries, but only when they do can they participate in a domestic political process that will generate leadership. They will not necessarily succeed in getting the foreign economic policies that they want; capabilities do not always generate motivation. The degree of success of the internationalist financial community in a country with the capabilities to lead the international economy will depend on a number of factors, including the importance of income earned internationally to the domestic economy, the structure of the domestic political system, the ideological and technological milieu in which policy is being made, and the particularities of personality and circumstance. The strength, and indeed the form, of leadership depend on their success.

The idea that financial motivations underlie foreign policy is not a new one. It was, for example, the subject of a debate among leading Marxist theorists of international economics early in the twentieth century. But these theorists argued that the concentration of international finance would lead either to world war or world government.[14] The argument here is that the concentration of international finance can lead a country to provide a financial infrastructure to the international economy, without necessarily leading to either military conflict or political confederation. And that the more diffuse international finance becomes, the less likely it is that this sort of leadership will be forthcoming. The next chapter will elaborate on this argument, and provide the logic that links finance and leadership. The bulk of this book will then examine the argument empirically, through the lens of four case studies of leadership or its failure.

THE METHODOLOGY

There is already a substantial body of literature on the subject of international economic leadership.[15] This literature encompasses a variety of different disputes, both empirical and theoretical. One of the disputes that threads its way through much of the literature concerns the effects of leadership; is a leader really necessary to stabilize the international economy? This question has been addressed both theoretically and empirically, yielding a range of answers. Some argue that leadership is necessary for stability, others that it has little effect. Some argue that the benefits of leadership accrue primarily to the leader itself, others that in the long run leadership benefits the leader relatively less than its followers.[16] Finally, some argue that an individual leader is required, others that collective action among states can be an effective substitute for the leadership of an individual state.[17] This study speaks to all of these questions, which in turn provide the topic of discussion for most of the concluding chapter.

Another of the differences among entrants in this literature is methodological. Different studies tend to adopt one of two distinct approaches to the analysis of international leadership, one focused on systemic comparisons and the other on specific case studies. Those in the former group argue that a state that displays a certain characteristic will behave in a certain way. Examples run from Leninist theory, in which large-scale exporters of capital inevitably come to act as aggressive imperialists, to more recent work of quantitative or formal bents, which posit that states of a given size will, out of economic self-interest, act in a given way. These quantitative and formal analyses span the various disputes concerning the necessity of leadership, but tend to display a preference for objective measures as indicators of the positions of states in the international system, generally some measure of power or of relative economic size.

This methodological preference for the objective tends also to extend to discussions of motivation. Systemic comparisons usually address questions of motivation, implicitly if not explicitly, but generally do so by ascribing to states preferences based on generalized assumptions of national interest that do not allow for variations either across states or across time. States are usually assumed to act in a way that maximizes rational utility, understood as the maximization of anything from aggregate national income to exports, either gross or net. Marxist theories suggest that the interest being maximized is that of a particular class, the financial elite, but assume that state policy is captive to the interests of this class, meaning that the state will still act to maximize a given rational utility, that of a class rather than that of the population as a whole. Thus the discussion of motivation in this branch of the study of international economic leadership focuses on explaining why a state with a given level of capabilities would act (or not act) as a particular kind of leader, but does not allow for variations in the type of leadership engaged in. States, in short, are categorized by size rather than by content.

In contrast, studies that focus on specific cases of leadership (or of the absence thereof) tend to incorporate the subjective, discussions of what policy-makers thought they were doing rather than objective measures to predict what they would do. In his classic study of the Great Depression, for example, Charles Kindleberger ascribes the set of decisions by the United States to undermine rather than lead the international economic system in the late 1920s and early 1930s to American irresponsibility as much as anything else.[18] One can certainly infer from this argument that in the future, when global depression looms, countries that are able to do so should try to act as leaders. However, one cannot reasonably infer from arguments about what states *should* do that they will do it. Similarly, P. J. Cain and A. G.

Hopkins discuss the evolution of British imperialism from the mercantilism of the eighteenth century to the liberalism of the nineteenth in terms of the social norms underlying British domestic politics.[19] This sort of empirical approach is invaluable in understanding specific national decisions about whether or not to adopt leadership policies, and necessary in explaining the specific patterns of and political choices reflected by those policies. By the same token, though, it is of much more limited value in understanding patterns of international economic leadership more broadly.

This distinction between a focus on objective, measurable data and on subjective or interpretive history mirrors a key contemporary methodological debate in international relations theory, between materialist and constructivist approaches. At its most extreme, a pure materialist approach would have it that only objectively measurable data are appropriate to the scientific study of international politics. Conversely, a pure social constructivist approach would deny any materialist base, arguing that the international system is a pure social construct, not guided by any inherent logic. Most theorists of international relations would likely locate themselves somewhere between these two extremes, but this still leaves a wide scope for methodological disagreement. Specifying the point on the materialist/constructivist spectrum that a particular study is starting from can be very useful as a shorthand for the methodological assumptions on which the study is based. The point of departure for this study is what has been called a thin constructivism.[20]

Constructivism is an epistemology of international relations that looks at both the structure of the international system and the identities and interests of actors within that system as social constructions, as sets of shared ideas and norms rather than as the result of brute material forces.[21] A thick constructivism is one that tends toward the post-positivist.[22] It questions any attempt to study international relations objectively, or "scientifically."[23] A thin constructivism is one that accepts a basic tenet of modern science, that one can proceed with research assuming a clear distinction between researcher and data, between the student and the studied. In other words, a thin constructivism argues that the data of international relations are intersubjective rather than material, based on social constructions rather than natural logic.

Most constructivists would accept that some natural logic comes into play in social science. At a minimum, people need to eat to survive. There is some debate as to how relevant these logics are to the actual structure and conduct of contemporary international politics; most constructivists would argue that they are not particularly relevant.[24] For a study of international economic leadership, however, choosing a single point on this spectrum of relevance can be unnecessarily limiting. A traditional materialist argument would be that there is an inherent logic to an international political economy, an inherent logic to a system of economic exchange among autonomous political entities without central authority. It is by specifying this logic that we can understand patterns of leadership. The constructivist response would be that the international political economy is a social construct, and is thus historically specific. To understand the content of a particular episode of international economic leadership, we must examine the particular social construction of that episode in its own historical context.

The contention of this book is that a full study of international economic leadership must encompass both the natural logic of economics and the social construction of international politics. The seminal question of whether or not there is an objective logic to international relations can, in this instance, be avoided by looking at only a particular subset of systems of political economy, those in which states with authority over their own legal and monetary systems interact on a market basis.[25] Looking at this subset of systems assumes a given set of intersubjective parameters. It assumes that a modern state system and patterns of market exchange have already been socially constructed. This limits the scope of the study, but still encompasses much of the international political economy over the past four hundred years, and its likely form through the foreseeable future.

Once this sort of system has been socially constructed, and to the extent that it defines actor interests, it does become constrained by its own internal inherent logic, the logic of systems of market/monetary exchange that is the basis of the study of economics. This logic allows us to do two things. We can draw the connection between predominance in international finance and the capabilities to lead. Successful leadership requires that a country, among other things, underwrite a currency for international exchange and provide liquidity to the international political economy, and both these activities, as argued in the next chapter, require of the leader a reserve of international assets that is secure from the speculations of others. The logic of systems of market/monetary exchange also allows us to draw a connection between investment in international finance and motivation to lead. A well-led system, as the next chapter also argues, maximizes returns to this sort of investment. This means that it is in the direct interest of the holders of this investment to promote international economic leadership.

But this logic is by itself insufficient either to predict or explain particular instances of leadership. It is insufficient to predict an outbreak of leadership because the motivations of the internationalist financial community within the country in question do not translate directly into national policy. They are mediated through the constructs of domestic politics, and are integrated with the policy demands of other interest groups. Both the constructs of and the conflicting interests within the domestic polity of the state in question are historically specific, are the expressions of the social context and intersubjective milieu of that polity. Whether a country will adopt leadership policies depends on the outcomes of these processes of mediation and integration. The logic inherent to market/monetary systems is insufficient to explain, or even to describe, particular instances of leadership because both the outcomes of these domestic processes and the norms of international contexts within which foreign economic policy operates are historically contingent.

For this reason, this study adopts a thin constructivist approach that is particularly cognizant of the limiting role of logics inherent in certain social constructs. These limitations mean that even though an international economic system based on market and monetary exchange is a social construct, within the bounds of this construct the logic of the system dictates that certain objectively measurable financial data both enable and constrain state foreign economic policy. The case studies examine both these international financial data, the objective distribution of investment across the international economy, and the contingent social constructs within which these investments are made. The former helps us to predict when leadership will be feasible, and gives us an indication of the relative strength of internationalist financial interests within the potential leader. The latter explain both the strength and the design of leadership policies. This methodology entails an examination of such objective measures as financial statistics and governmental types, and also of the intersubjective context within which policy is made. Elements of this context include such things as the normative structure of the practice of domestic politics, the existing consensus on economic theory and on the relationship between politics and economics, and the norms and practices of the international system for which the foreign economic policy is being made.

THE CASE STUDIES

Chapter 2 discusses the arguments made to this point in more detail. The following four chapters look at four historical cases, ordered chronologically and covering the majority of the past four centuries of international political economy. These cases are the role of Dutch leadership in the international political economy of the seventeenth century, the role of British leadership in the nineteenth, the failure of leadership in the period between the two world wars of the twentieth century, and the role of American leadership in the reconstruction of an international political economy following World War Two. Taken as a set, these four cases encompass a broad sweep of the history of the evolution of our contemporary international political economy. Individually, each case presents its own theoretical and empirical puzzles, making each both methodologically and historically intriguing in its own right.

The first case begins at the dawn of the seventeenth century, and looks at the role of the Netherlands and its various component political entities in the rapid expansion of international commerce at the time. The Dutch-led system marked a transition from the set of loosely connected regional political economies that were the norm beforehand to the more integrated and global pattern of international commerce that has been the norm since. As a comparative case in international economic leadership the Dutch case is particularly interesting, for three reasons. The first is the patterns of domestic politics within the United Provinces of the Netherlands. International economic policy was made at three different levels of government, the federal, provincial, and civic levels, each of which was authoritative in different issue areas. This allows for a comparative study of the relationship between finance and leadership within a single historical case. The second is the role that the United Provinces played on the broader stage of international politics of the time, a role much more circumscribed than the roles of the economic leaders that have followed. This allows us to look at economic leadership in isolation from political and military leadership. Finally, Dutch foreign economic policy was not embedded in a liberal ideology, which allows us a broader scope for comparative study of the role of ideology in leadership.

The second case, Great Britain from the middle of the nineteenth century to the eve of World War One, is often seen as the classic example of international economic leadership; no historical study of the phenomenon would be complete without it. But historical studies of British economic leadership often fail to illuminate both the question of what made Britain capable of acting as a leader, and the question of what motivated the British government to choose to do so. A link is often drawn between industrial exports, the role of Great Britain as the original home of the industrial revolution, and British foreign economic policy. But this link does not stand up well to historical scrutiny, not nearly as well as a link between the British position in international finance and its foreign economic policy. This case is a methodologically interesting one because it shows a clear and direct link between finance and leadership in an instance when the leader was economically predominant in several other ways as well.

The third case centers on a question that has often been asked: What went wrong in the Great Depression? Why was the depression in the business cycle that began in 1929 so bad, why did it last so long, and how was it allowed to undermine international commerce as thoroughly as it did? One answer to these questions is the absence of leadership; the internationalization of the Great Depression is often ascribed to "beggar-thy-neighbor" policies, in which countries act in their own short-term interests at the expense of the good of the system as a whole, and no one acts in the interests of the system. In other words, there was no effective international economic leader; this case allows us to study the failure of leadership, as well as its success.

Finally, the fourth case looks at the leadership role of the United States in the creation and management of the international economic system that came out of World War Two. The role of the United States in this period was in many ways broader than that of Great Britain a century earlier, in that its leadership encompassed both a more formal security role and a multilateral system of formal economic institutions and rules. It was in ways, however, shallower as well. The institutional structure excluded that part of the world that was on the other side of the Cold War; much of it failed to last much more than a quarter of a century; and the American commitment to maintaining its leadership wavered rather more than the British commitment had. Why would the United States choose to take on a broader international economic role than had Britain and yet be less committed to fulfilling that role? Looking at the postwar case through the lens of this question allows us to contrast the comparative roles of capabilities and motivations in the construction of forms of international economic leadership.

The conclusion summarizes and aggregates the findings of the case studies, and puts these in the perspective of the framework presented in Chapter 2. It also addresses the broader applicability of the methodology used here. It then asks what these findings, and this framework, suggest about international economic leadership in the near- to medium-term future. The answer is that they point to a role for constructive regionalism that is perhaps greater than at any time since the economy became global around 1600. At a time when the future of the international financial architecture is much under discussion, the dialectic of the logic of international economic leadership and the normative structure of the international political economy suggests the time may well be right for the architecture to be reconstructed regionally, rather than globally.