What to read to understand the history of Western capitalism

Our senior economics writer picks **three books and two papers**

Jul 4th 2022
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It is easy to be swept up in news about the economy, especially these days. In 2020 the world saw the biggest economic contraction since the Great Depression; today we are dealing with the highest inflation since the 1980s. People rarely have time to think about the very biggest questions in economics. Why did the industrial revolution begin in the 18th century—and why in western Europe? Why do so many countries remain poor when some are fabulously rich? And what is work like today compared with the past? All the issues improve your understanding of the news. For the answers, you need to turn to economic history. Here are five resources to help you understand why we are where we are.

The Worldly Philosophers. By Robert Heilbroner. *Touchstone; 368 pages; $18.99. Simon & Schuster; £8.99*

The best book to read if you are interested in the history of economic ideas. First published in 1953, it covers some of the most consequential early economists, from Adam Smith to Thomas Malthus to Karl Marx, explaining what they thought and why. Was Adam Smith really a free-market fundamentalist? The book is written in a light, conversational style that is hard to beat—giving the reader a proper understanding of Marx's theory of capitalist collapse, for instance, without getting bogged down in debates over doctrine. And that's not the only reason it is a better starting point than Joseph Schumpeter's "History of Economic Analysis", which is more precise and nuanced about the early economists but also less fun. Heilbroner's book is short. You can read it in a few hours.

A Culture of Growth. By Joel Mokyr. *Princeton University Press; 424 pages; $22.95 and £17.99*

This book deals squarely with the question of why Europe was the first region to industrialise. It focuses on institutions—how ideas of free debate and free markets became embedded in everyday life. Mr Mokyr talks a lot about the Royal Society, a learned institution founded in London in 1660, with the motto "*nullius in verba*"—"take nobody's word for it". The Royal Society was the site of furious disagreements between different scientists, who nonetheless recognised that they were working towards a common cause: improving humanity. And why did this happen in Europe? Geography probably played a role. Fractured into lots of states, a firebrand intellectual who incurred the wrath of the authorities could easily move elsewhere. In most other places, free thinkers had few escape routes.

War as an Economic Activity in the "Long" Eighteenth Century. By N.A.M. Rodger. *International Journal of Maritime History.* XXII, No. 2 (December 2010): 1-18

This is a short journal article, but the message is profound—and deeply underappreciated. It is about the role of technology. To understand the growth of capitalism in the 17th and 18th centuries, you must understand navies. To be a successful navy, you need to have good ships—obviously enough. A country that wanted to rule the waves therefore needed to invest heavily in new technological innovations. These, in turn, spilled over to the rest of the economy. In addition, you had to have an efficient bureaucracy—for instance, to supply ships thousands of miles from home. This encouraged better government. It is no coincidence that countries with the best navies tended to have the most sophisticated economies: the Dutch in the 17th century, the French for part of the 18th century and the British in the 19th.

The Hundred Years' War, Volumes 1-4. By Jonathan Sumption. *University of Pennsylvania Press; 3,320 pages; $170. Faber & Faber; £84*

This series is set long before capitalism got going. The Hundred Years' War, effectively a French civil war which England egged on, started shortly before the Black Death around the 1340s and finished in the mid-15th century. But the book nonetheless does a fantastic job of showing how different governance and politics were before capitalism, and thus what changed from the 18th century onwards. Kings did not care about economic growth, or even know what it was: they wanted glory. They were happy to tax their subjects to oblivion to fund their missions. And they often laid waste to an opponent's conquered land, rather than using it for productive purposes. If you don't have the patience for four full volumes—soon to be five—the single best chapter of the entire series is called "Men at arms", in the fourth volume, which tells you everything you need to know about the economics of the war.

Enclosures, Common Rights, and Women: The Proletarianisation of Families in the Late Eighteenth and Early Nineteenth Centuries. by Jane Humphries. *The Journal of Economic History.* Vol. 50, no. 1 (1990): 17-42

Another paper, which nonetheless contains as much insight as an entire book. It focuses on how lifestyle changed as capitalism came about. During early capitalist development, from the 17th to the late 18th centuries, many people worked from home in small-scale manufacturing industries—producing clothes, for instance. But in the Victorian era many moved into large factories. This had an enormous impact on people's day-to-day lives. For one, it became harder to look after children. It became more difficult to grow food at home, both because people were there less frequently but also because they were now more likely to live in a city. And they had less control over their time: the factory owner would need them there at 6am sharp. The paper shows that capitalism, despite producing miraculous improvements in people's material wellbeing, has its trade-offs.

Our senior economics writer is the author of his own book on the history of economic thought.

The Classical School: The Turbulent Birth of Economics in Twenty Extraordinary Lives. By Callum Williams. *Hachette*; 288 pages; $11.99. Profile Books; £20

An intellectual tour of the 20 most significant early economists, from Adam Smith to David Ricardo to Rosa Luxemburg. "A clear, well-written, and useful introduction to the lives and thought of some of the leading classical economists," according to Tyler Cowen at the "Marginal Revolution" blog.

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Finance & economics | Covid-10trn

What is the economic cost of covid-19?

The pandemic could amount to $10trn in forgone GDP over 2020-21

Jan 9th 2021 | HONG KONG

The economic toll of the covid-19 pandemic is incalculable. But let's try anyway. A useful starting point is the semi-annual *Global Economic Prospects* report released this week by the World Bank. It calculates that the world economy probably shrank by 4.3% in 2020, a setback matched only by the Depression and the two world wars. But this dramatic figure still understates the cost. It measures the world economy's fall from where it was before the pandemic, not from where it would have been had the virus not spread.

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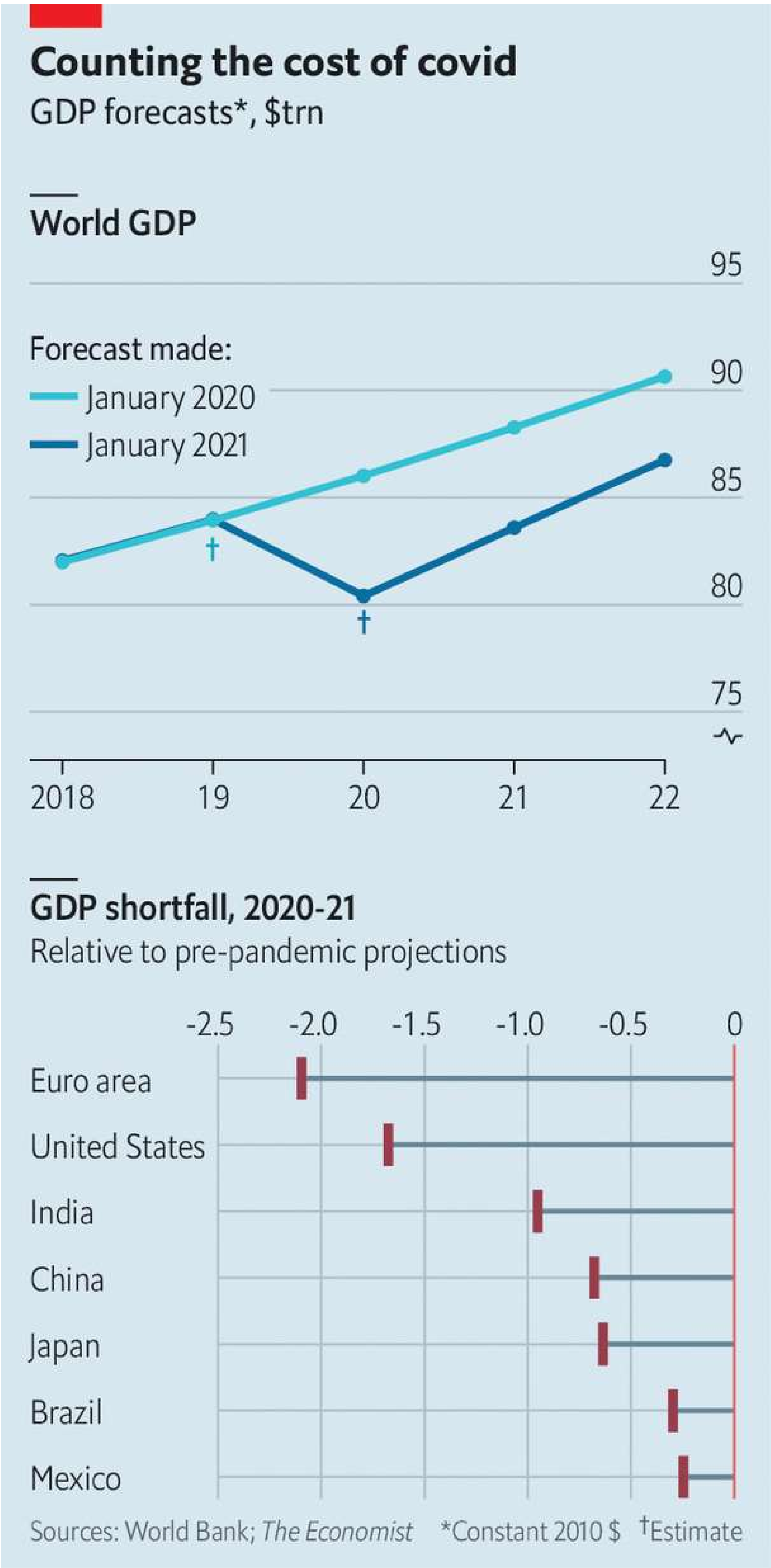
To calculate that bigger fall, economists need an estimate of how global gdp might have evolved in the absence of covid-19. One simple baseline is the World Bank's projection released this time last year, when it was still blissfully unaware of the lurking viral threat. Back then, it expected global gdp to expand by 2.5% in 2020 to $86trn. Compared with that figure, the shortfall of global gdp last year was probably more like 6.6%. That is equivalent to about $5.6trn (at the market exchange rates and prices prevailing in 2010, which the bank uses for analytical convenience).



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In 2021 the world economy should grow unusually briskly, the bank projects, helped by the roll-out of vaccines. But even if this expectation is met and no further calamities intrude, the level of output in 2021 will remain 5.3% below the bank's pre-pandemic projections: a further shortfall of almost $4.7trn (see chart).

Put these two numbers together and the cost of covid-19 this year and last will amount to about $10.3trn in forgone output: goods and services the world could have produced had it remained unafflicted. That is, to put it mildly, a big number. Only America and China have an annual gdp greater than $10trn. And there are 153 economies that produced less than that between them in 2019. Converted into today's money, $10.3trn is enough to buy the ten biggest listed companies in the world, including Amazon, Apple and Saudi Aramco. It is also enough to buy all the property in New York City nine times over.

Over $2trn of the cost will be suffered by the euro area. America will bear roughly $1.7trn. Among developing countries, India is set to endure the biggest loss in dollar terms: about $950bn (although the bank's forecast for India's growth in 2021 seems unduly pessimistic). Although China's economy is much bigger than that of India, it will suffer a smaller gdp shortfall of about $680bn.

Even these colossal numbers understate the cost, however. The economic damage, after all, will not be confined to this year and last. The World Bank expects global gdp in 2022 to remain 4.4% below its pre-pandemic predictions. It fears lasting harm to investment, human capital and, therefore, the growth potential of the world economy. It also worries that the debt that governments and companies have issued to help them weather the pandemic may harm growth in the future.

There is another reason why these figures understate the economic tab. If the pandemic had never happened, world gdp would not only have been higher, it would also have been different. Instead of masks, tests, vaccines, Zoom calls and parcel deliveries, the world economy would have produced other items. Because the pandemic is so damaging to health and society, it is worth diverting vast resources to fight it—these efforts are of enormous economic value. But if the virus had never spread, these same efforts would have been unnecessary, making them an expense the world could have been spared.

Editor's note: Some of our covid-19 coverage is free for readers of The Economist Today*, our daily newsletter. For more stories and our pandemic tracker, see our hub*

This article appeared in the Finance & economics section of the print edition under the headline "Covid-10trn"

Why inflation looks likely to stay above the pre-pandemic norm

Even as supply-chain snarls ease, wage growth and price expectations are ticking up

Jun 26th 2022 | SAN FRANCISCO
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The bad news on inflation just keeps coming. At more than 9% year on year across the rich world, it has not been this high since the 1980s—and there have never been so many "inflation surprises", where the data have come in higher than economists' forecasts (see chart). This, in turn, is taking a heavy toll on the economy and financial markets. Central banks are raising interest rates and ending bond-buying schemes, crushing equities. Consumer confidence in many places is now even lower than it was in the early days of the covid-19 pandemic. "Real-time" indicators of everything from housing activity to manufacturing output suggest that economic growth is slowing sharply.

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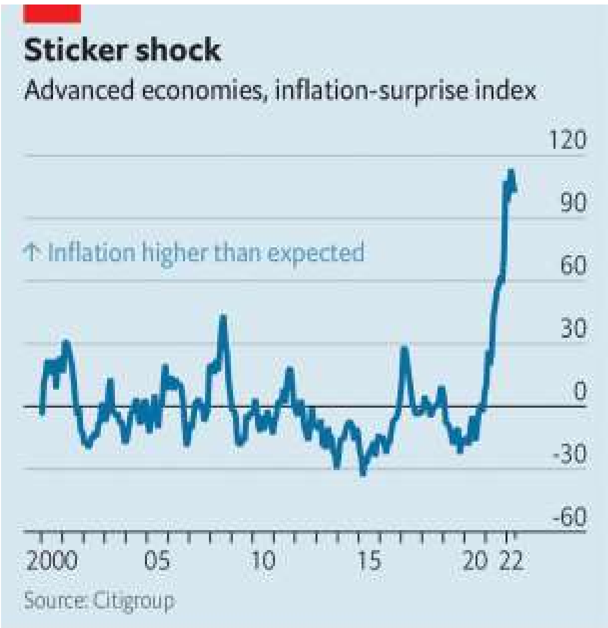
What consumer prices do next is therefore one of the most important questions for the global economy. Many forecasters expect that annual inflation will soon ebb, in part because of last year's sharp increases in commodity prices falling out of the year-on-year comparison. In its latest economic projections the Federal Reserve, for instance, expects annual inflation in America (as measured by the personal-consumption-expenditures index) to fall from 5.2% at the end of this year to 2.6% by the end of 2023.

You might be forgiven for not taking these prognostications too seriously. After all, most economists failed to see the inflationary surge coming, and then wrongly predicted it would quickly fade. In a paper published in May, Jeremy Rudd of the Fed made a provocative point: "Our understanding of how the economy works—as well as our ability to predict the effects of shocks and policy actions—is in my view no better today than it was in the 1960s." The future path of inflation is, to a great extent, shrouded in uncertainty.



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Indeed, some indicators point to more price pressure to come in the near term. Alternative Macro Signals, a consultancy, runs millions of news articles in several languages through a model to construct a "news inflation pressure index". The results, which are more timely than the official inflation figures, measure not just how frequently price pressures are mentioned, but also whether the news flow suggests they are building up. In both America and the euro area the index is still well above 50, indicating that pressures are continuing to accumulate.

Inflation worrywarts can point to three other indicators suggesting that the rich world is unlikely to return to the pre-pandemic norm of low, stable price growth any time soon: rising wage growth, and increases in the inflation expectations of both consumers and companies. If sustained, these could together contribute to what the Bank for International Settlements, the central bank for central banks, described in a report published on June 26th as a "tipping point". Beyond it, warned the bis, "an inflationary psychology" could spread and become "entrenched".

Evidence is mounting that workers are starting to bargain for higher wages. This could create another round of price increases as firms pass on the extra costs. A survey by the Bank of Spain suggests that half of collective-bargaining deals signed for 2023 contain "indexation clauses", meaning that salaries are automatically tied to inflation, up from a fifth before the pandemic. In Germany ig Metall, a trade union, has asked for a 7-8% pay rise for nearly 4m workers in the metals and engineering sector (it will probably get about half that). In Britain rail workers went on strike as they sought a rise of 7%, though it is unclear whether they will succeed.

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All this will make wage growth hotter still. Already, a tracker for the g10 group of countries compiled by Goldman Sachs, a bank, is rising almost vertically. A measure of pay pressure from Alternative Macro Signals is similarly animated. And wage floors are rising, too. The Netherlands is bringing forward an uplift to the minimum wage; earlier this month Germany passed a bill increasing its minimum by one-fifth. Australia's industrial-relations agency has raised the wage floor by 5.2%, more than double last year's increase.

Faster wage growth in part reflects the public's higher expectations for future price rises—the second reason to worry that inflation might prove sticky. In America near-term expectations are rising fast. The average Canadian says they are braced for inflation of 7% over the next year, the highest figure of any rich country. Even in Japan, the land where prices only rarely change, beliefs are shifting. A year ago a survey by the central bank found that just 8% of people believed that prices would go up "significantly" over the next year (consumer prices, indeed, rose by only 2.5% in the year to April). Now, however, 20% of people reckon that will happen.

The third factor relates to companies' expectations. Retailers' inflation expectations are at an all-time high in a third of eu countries. A survey by the Bank of England suggests that clothes prices for Britain's autumn and winter collections will be 7-10% higher than a year ago. The Dallas Fed does find tentative evidence that customers are less willing to tolerate price increases than before; a respondent in the rental and leasing business complained that "it is getting tougher to pass on the 20-30% price increases we have received from manufacturers." But that merely points to a lower level of high inflation.

The big hope for lower inflation relates to the price of goods. Fast increases in the prices of cars, fridges and the like, linked in part to supply-chain snarls, drove the initial inflationary surge last year. Now there is some evidence of a reversal. The cost of shipping something from Shanghai to Los Angeles has fallen by a quarter since early March. In recent months many retailers spent big on inventories in order to keep their shelves full. Many are now cutting prices to shift stock. In America car production is at last picking up, which could unwind some of the outrageous price increases for used vehicles seen last year.

Falling goods prices could, in theory, help douse the inflationary flames in the rich world, easing the cost-of-living crisis, giving central banks breathing room and buoying financial markets. But, with enough indicators of future prices pointing the other way, the odds of that happening have lengthened. Don't be surprised if inflation roars for a while yet. .

This article appeared in the Finance & economics section of the print edition under the headline "The top of the hill"