

## **Drivers of the Public Expenditures in the 19th Century Europe**

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### **Abstract**

*19<sup>th</sup> century is a period where nation-states have emerged and strengthened in Europe. Strengthening of the central government can be represented by the increase in public expenditures the sources of which are of great importance. In this study, relationship between the increase in public expenditures and developments in economic, political, commercial, and fiscal fields is analyzed for Belgium, England, France, Spain, and The Netherlands for the period between the beginning of the 2<sup>nd</sup> quarter of the 19<sup>th</sup> century and the outbreak of World War I. The main contribution of this study is that it helps to explore the political economic properties of the period and also the relationship between the state and market through time series analysis.*

**Keywords:** Public Expenditures, Europe, 19<sup>th</sup> Century, Time Series Analysis

### **1. Introduction**

19<sup>th</sup> century was a lively period where the French Revolution has begun to take effect and The Crimean War and The Franco-Prussian War have established the pre-conditions of The World War I. Besides, economic institutions and commercial activities have improved considerably in the same period. The development process of modern states shows parallelism with the nascence and rise of capitalist economic system. In Weberian sense, modern state which was systematic, continuous, legal-rational, extensive, bureaucratized, hegemonic and having the power of taxation, has transformed from tributary state into Laissez Faire state at the end of a long process where different factors played important roles (Bonny, 1999: 12; Pierson, 1996: 8; Morton, 2005: 500). This transformation process which continued for centuries has led to the development of trade and banking bourgeoisie, as well as the development of trade at global scale, introduction of new production and transportation technologies, and rise of nations and modern states (Beaud, 2001: 13).

The rise of the central monarchs during the Early Modern Era is attributed to the reorganization of aristocratic forces in a more centralized way to maintain their privileged status. This situation is a result of the negotiations between the central governance and local elites on the use and mobilization of the economic resources. As a result of the collapse of feudalism and the emerging of the markets due to civilization, resource generating capacity that relies on the power of use of aristocratic force was captured by the rising monarchies. These monarchies that have the power to collect taxes from their people and to establish regular armies, have cut ties with their religious linkages by the reformation process in Europe and the system of modern European states was formally accepted for the first time following the signing of the Westphalia Treaty in 1648 which ended the Thirty Years War (Nelson, 2006: 57-60).

Financial centralization, protectionism, and expansion overseas which represent the formal policy of central monarchies led to an increase in taxable income which has contributed to the state's prestige and enabled the bourgeoisie to be better off due to the creation of new job opportunities (Anderson, 2013: 20-41; Karaman and Pamuk, 2001: 9). During that era, bourgeoisie convinced the state to cooperate with them by regarding national and class interests as identical due to high costs associated with overseas trade and security reasons and thus managed to turn mercantilism into a state policy for the sake of common interests in accordance with the perception of state in Conventional Liberal.

Theory represented by Hobbes and Locke (Habermas, 2002; Aniveri, 1974: 134.). Most of the states which have adopted absolute or constitutional monarchy have provided direct support to merchant capital. The primitive capital accumulation achieved by the abovementioned economic policy and controlled interventionism organized by the state in a centralized way have paved the way to capitalist market economy (Dobb, 2008: 209; Albirton, 1986: 120; Polanyi, 2001: 140).

The rise of centralized states during the development process of modern state which was initially introduced by Machiavelli, and accordingly the expansion of financial capacity are attributed to a vast number of wars that led to substantial alterations in countries' technological, organizational and administrative structures. The progress shown in military technology following Late Medieval Era has increased the organizational cost of art of war and likewise the wars which have occurred until the Early Modern Era and the demand for armed forces caused by these wars have increased the dominance of the state in economic life and played a key role in financial change (North, 1991: 25; Bonney, 1999: 161). Similarly, Tilly (1990) puts forward that the financial costs which emerged due to wars have led the monarchs to use the national resources more efficiently by making reforms that would enhance their administrative and financial means and at the same time by shrinking the local interests and privileges. Accordingly, many of the states that adopted different regimes ranging from monarchy to republic have made alternative conventional political forces more absolute and centralized by eliminating the church, nobles, and local governments in an effort to increase the efficiency in taxation and recruitments (Tilly, 1990: 17; Childs, 2001: 17).

The reasons behind the increasing government expenditures during the era prior to the 19th century were wars and international trade rather than social and economic issues. Financial and administrative obstacles encountered during wars forced the state to take new responsibilities in social and economic areas (Harling and Mandler, 1993: 46-50). Before the industrial era, especially Republic of Netherlands and England adopted modern public finance along with parliamentary and multiparty political systems that allow for constitutional control over budget and public expenditures and thus increased their credibility. This situation has facilitated the borrowing conditions by falling rates and enabled them to make infrastructure investments (Berend, 2013: 107). Similarly, Bank of England established in 1694, was a result of the efforts to overcome the bottleneck associated with public finance and created by the war against France in 1689. The establishment of Bank of France was an outcome of a nationalization and a centralization attempt following the wars against the US between 1776 and 1783 (Roseveare, 1991: 33-34; Braudel, 1994: 479-483; Salzmann, 1995: 47-49).

However, the process of centralization represents a distinct scenario for Southern Europe and Western Europe. As Gramsci (1971) suggested, by eliminating the conventional feudal classes the French Revolution which has created the appropriate political institutions and enabled the spread of capitalism through Europe by different ways, played a key role in that process. Thus, the local power elites in France, Spain, and Portugal have transferred their power gradually to the monarchs via negotiations and eventually, central monarchies have come into being in these countries. An alternative way is adopted by England and Holland. Parliaments in these countries have acquired the power of control on financial and political issues without the definite demand of the monarch (North, 1991: 26.; Morton, 2005: 509). Finally, by mid-19<sup>th</sup> century, except for Russia and the Ottoman Empire, constitutional governance ranging from powerful central governments to parliaments under the control of the monarchs has been established in entire Europe (Bogart et al., 2010: 75).

The prevailing economic thoughts in the late 18<sup>th</sup> and 19<sup>th</sup> centuries were advocating the diminishing of the government's role in economic area. England who has limited the imports of grain between 1804 and 1846 by implementing strict Grain Laws and used its military power to overcome the local monopolies and thus supported its own merchants, adopted a liberal policy in government enterprises during mid-19<sup>th</sup> century. The state has exceeded the monetary system in 1844 by the Banking Law which confined the issuing of new banknotes to the amount of gold supplied and cleared all the protective tariffs from its trade policy by 1860s. Contrary to England, France has adopted an obsolete tariff and prohibition policy until it took a step towards moderate protectionism by signing a trade agreement with England in 1860. The success of economic liberalism in the Continental Europe that has a long history in statism, was limited compared to England. The most prominent example for this was Germany who had extensive bureaucracy along with its cameralist policies (Dormois and Lains, 2006: 13; Guran, 1999: 137-139; Williams, 2004: 114.; Berend, 2013: 110).

Following the Industrial Revolution, the states have begun to implement their basic policies to mass public, the frequency of wars has decreased, and public services have begun to represent the greater portions of the state budgets. Whereas the public expenditures and the role of the state in the economy in England have fallen by almost 50%, in France despite the low population growth rates in comparison with Germany during the entire 19<sup>th</sup> century and the high resistance against taxation that limited the public expenditures.

The declining public expenditures during the postwar period once again have taken a steeply rising course and increased fourfold between 1815 and 1880 (Harling and Mandler, 1993: 59-60, 66; Karaman and Pamuk, 2001: 36; Cardoso and Pedro, 2010: 287). However, Portugal's and Spain's public finance policies have failed in the long run due to the colonial dependence on resources that implies the efforts to maintain the existence of the imperial state and to the financial constraints associated with the institutional structure established in line with these resources (Cardoso and Lains, 2010: 280-298). In this regard, the statist heritage at the Continental Europe and the laissez faire thought that has taken hold in England led to a distinction at the entire continent in the public policies and the role of the government in economic life (Guran, 1999: 139).

Substantial changes in the tools and ends of economic policies have taken place in the capitalist world during the last quarter of the 19<sup>th</sup> century. The progress made by Germany in Continental Europe and by the US, which enabled them to reach a capacity that would rival leading English industries and the emergence of monopolist capitalism are among the most important reasons behind this development (Sweezy, 2007: 296). 1873-96 Crisis that led to the reconstruction of the Eurocentric capitalist economy represents the transition process from perfectly competitive capitalism to monopolist capitalism. The distinctive property of monopolist capitalism is that exports of goods are replaced by exports of capital. A prevailing tendency towards the establishment of industrial corporations financed by public resources and run partially or completely by the state was the case in Western countries during the late 19<sup>th</sup> and early 20<sup>th</sup> centuries, the period where the liberal era ends (Poggi, 1978: 127). Capital exports and international rivalry that were carried out by foreign investments have been represented by those corporations. State's functions and more particularly its role in economic life has shrunk to the lowest level during the competitive capitalist era whereas during the monopolist capitalist era the period that represents the pre-imperialist epoch, those functions have been maximized in every field (Hilferding, 1995: 47; Beaud, 2001: 153-158). Maximizing the interests of the capitalists internationally has been regarded basically as the main purpose of the state policy. Free trade or limited protectionism has been replaced by a fierce competition among the national monopolies. The rivalry among the imperial powers has led to the strengthening of the inner ties of the empires and to a severe policy of colonization, the most important reasons that paved the way to the World War I (Sweezy, 2007: 298-306; Gill, 2003: 125).

The rest of the study is organized as follows: Review of the literature is presented in the second section. In the third section, the model and the data set are introduced. In the fourth section, the procedures are explained. The findings are presented in the fifth section. And finally the sixth section concludes.

## **2. Literature Review**

In the Leviathan fiscal theory, state is regarded as a malevolent organizational structure which is different from a benefactor public product supplier aiming at maximizing its revenue. Although the share of public services in the government budget started to increase in association with the Industrial Revolution, the studies on government expenditures began which test especially Wagner Law, the stages of development, Displacement Thesis/Peacock-Wiseman Hypothesis, the historical - political stage approach, Baumol Effect, and Buchanan-Wagner Hypothesis since the mid-20<sup>th</sup> century (Howard, 2001: 64-73). These studies largely focus on the relationship among public expenditures, growth and development. However, there are limited number of studies related to the drivers of the public expenditures. Borchering and Deacon (1972), Bergstrom and Goodman (1973), and Deacon (1977) are among the leading studies on analyzing the increases in public expenditures. The pioneering study on analyzing the demand for public goods and services was done by Downs (1957) known as the Median Voter Hypothesis. The primary studies generally present theoretical perspective and deal with the effects of social and demographic variables on public expenditures by considering the changes in demand for public goods. Cameron (1978) analyzed the reasons of the expansion in the public economy by using the data for 18 nations for the period between 1960 and 1975.

Cameron (1978) concluded that the role of the government has increased to maintain price competitiveness in the world market, and thus advanced capitalist economies turned to the “tax state”. The empirical literature on this issue is steadily growing. For example, Doessel and Valadkhani (2003) adopted time series analysis to investigate the public expenditures in Iran for the period 1963-2000 by using economic, structural and institutional variables. The findings suggest that each pair of variables fail to explain public expenditures. Shelton (2007) tested the main hypotheses on the drivers of public expenditures. In that study, the cross sectional and inter-temporal changes in public expenditures are investigated for 100 countries for the period 1970-2000 by using the data from IMF’s online database. Public expenditures are classified into the following subgroups: defense, education, and health. They also consider the expenditures made by local governments and general government. The findings brought a new perspective to the Wagner Law and showed that trade openness causes public expenditures to increase. Other important finding of the study is that population growth and ethnic discrimination lead public expenditures to decentralize.

Shonchoy (2010) examined the recent structure of public expenditures in developing countries and estimated the factors affecting public expenditures by applying panel data techniques for the period 1984-2004 for 111 developing countries. To the findings of that study, political and institutional factors affect public expenditures substantially, so do the administrative factors. Besides, the findings reveal that public economy is associated with national wealth, a finding consistent with the Wagner Law. Abu Tayeh and Mustafa (2011) investigated the relationship between total government expenditures and its drivers in Jordan by applying cointegration analyses. The variables used in the study are categorized as follows: stabilizing political variables, demographic variables, and political variables. The main finding of the study is that population, unemployment and inflation are closely related to the public expenditures.

Okafor and Eiya (2011) examined the drivers of the public expenditures in Nigeria by applying time series analysis for the period 1999-2008. The researchers modeled the relationship between public expenditures and inflation rate, population growth rate, public debt growth rate and tax revenues growth rate. They concluded that inflation has a negative effect whereas the other variables have a positive and significant effect on the increases in total public expenditures.

Akanbi (2014) tested a model, which is developed to identify the drivers of the public expenditures and its trend in Nigeria by using time series analysis for the period 1974-2012. The main finding of the study is that capital and recurrent expenditures are sensitive to the shocks in total government expenditures and vice versa. In a methodological study, Facchini (2014) suggests that a qualitative analysis can be applied along with econometric procedures to understand the evolution of public expenditures. However, according to the findings, qualitative analysis has failed in terms of generalization and in defending causal manipulative structures.

Petrou (2015) tested the robust drivers of the public expenditures by applying Model Averaging Approach for 89 countries for the period 1971-2000. He concluded that current theoretical and empirical studies on public expenditures do not yield convincing results and therefore certain hypotheses considering alternative variables and theories have been examined in his study. 5-year averages of 23 variables have been used to avoid the effects of business cycles. The findings revealed that public expenditures are lower in the countries with a presidential system. Besides, globalization and foreign capital flows led the government to play a more substantial role in the economy. On the other hand, population growth leads public expenditures to decrease.

### 3. Model and Data

In this paper, the relationship between public expenditures and economic, political, commercial and fiscal indicators are investigated by adopting the model developed by Cameron (1978)

$$G_t = \alpha + \beta GDP_t + \gamma TRADE_t + \delta TAX_t + \varepsilon_t \quad (1)$$

In the equation (1),  $G_t$  represents public expenditures,  $GDP_t$  is gross domestic product as an economic indicator,  $TRADE_t$  is trade volume as a commercial indicator,  $TAX_t$  represents tax revenues as a fiscal indicator and finally  $\varepsilon_t$  is the error term. All variables are index values and in logarithmic form. This avoids erroneous results caused by differences in measurement units. Additionally, dummy variables are employed to represent political changes. All the data are annual and gathered from Mitchell (1998). There are different data ranges due to the data constraints. Data range and additional information are presented in Table 1.

**Table 1. Data Range and Dummies**

Countries	Period	Political Variables
Belgium	1835-1912	Franco-Prussian War (1871), Antwerp Universal Exhibition/The Foundation of Congo Free State (1885), Elections (1898)
England	1796-1913	Napoleonic Wars (1798-1815), The Long Depression (1873-1896), London Straits Convention/The Repression of the African Slave Trade (1841)
France	1815-1913	The Second Republic (1848-1851), The Crimean War (1854-1856), Prussian War (1870-1871), The Third Republic (1970-1913)
Germany	1872-1913	The Year of the Three Emperors (1888), Sammlungspolitik (1897), Financial Crisis (1907)
Spain	1850-1913	The Hispano-Moroccan War (1859-1860), The Spanish-American War (1898), A Revolt in Catalonia (1909)
The Netherlands	1845-1913	Repeal of Price Regulation (1856), The Long Depression (1873-1896)

#### 4. Methodology

In this paper, time series econometrics is applied to estimate the drivers of the public expenditures in 19<sup>th</sup> century Europe. In order to apply this methodology, it is of great importance that the variables should be stationary due to the reason that spurious regression may be the case with nonstationary data, which leads to unreliable test statistics. Time series properties of the variables are explored by Augmented Dickey-Fuller (ADF) and Kwiatkowski, Phillips, Schmidt and Shin (KPSS) unit root tests developed by Dickey and Fuller (1979) and Kwiatkowski, Phillips, Schmidt and Shin (1992), respectively. ADF tests use a parametric autoregression to approximate the autoregressive moving average (ARMA) structure of the errors in the test regression and assume that the errors are statistically independent and have a constant variance. KPSS test makes the series stationary by eliminating the deterministic trend. The main distinctive feature of this unit root test is its null hypothesis of stationarity.

After performing the unit root test procedures to determine the degree of integration for each series, cointegration relationships are investigated using Engle and Granger's two stage cointegration procedure that involves error correction modeling initially introduced by Engle and Granger (1987). This procedure is simply an ADF unit root test on the residuals. If the residuals are stationary, then one can conclude that the variables have a cointegrating relationship. Secondly, an error correction model is constructed with first differenced variables. Lagged value of the error term of the long run equation is also added to the error correction model as an error correcting term. If the coefficient of this term ranges between -1 and 0, the error correction mechanism is valid and the variables in question are cointegrated. Many econometric procedures have been developed in order to estimate the long run coefficients in regressions. In this paper, Fully Modified Ordinary Least Squares (FMOLS) procedure which was introduced by Phillips and Hansen (1990) is applied. This methodology is used to estimate a single cointegrating relationship and modifies the least squares to overcome some econometric problems like serial correlation and endogeneity in the regressors which stem from the existence of a cointegrating relationship when the dependent and independent variables have unit roots.

#### 5. Findings

All of the variables are said to be difference stationary in the light of both ADF test and KPSS test results summarized in Table 2.

Table 2. Conventional Unit Root Test Results

Unit Root Tests		BELGIUM			
		G	TAX	GDP	TRADE
ADF	Level	-0.6874 (0.8432)	0.0539 (0.9600)	-0.6513 (0.8518)	-0.5647 (0.8714)
	First Difference	-12.8155* (0.0001)	-14.9190* (0.0001)	-12.5875* (0.0001)	-10.4350* (0.0001)
KPSS	Level	1.2009	1.2077	1.2080	1.1965
	First Difference	0.2160*	0.2916*	0.1570*	0.1358*
		ENGLAND			
		G	TAX	GDP	TRADE
ADF	Level	-0.8302 (0.8064)	-1.2893 (0.6328)	-0.2164 (0.9321)	-0.7399 (0.8314)
	First Difference	-9.5701* (0.0000)	-10.5508* (0.0000)	-9.1705* (0.0000)	-11.6667* (0.0000)
KPSS	Level	0.8428	1.0311	1.2885	-0.7252
	First Difference	0.1198*	0.1502*	0.0560*	0.1296*
		FRANCE			
		G	TAX	GDP	TRADE
ADF	Level	-0.2383 (0.9287)	-0.3506 (0.9121)	-0.7821 (0.8194)	-1.2112 (0.6672)
	First Difference	-9.0955* (0.0000)	-9.5602* (0.0000)	-10.0342* (0.0000)	-14.6980* (0.0001)
KPSS	Level	1.3119	1.3440	1.3410	1.3326
	First Difference	0.1046*	0.0385*	0.1396*	0.1295*
		GERMANY			
		G	TAX	GDP	TRADE
ADF	Level	-0.1235 (0.9399)	-1.0491 (0.7264)	2.0775 (0.9998)	0.4530 (0.9829)
	First Difference	-6.3686* (0.0000)	-8.3048* (0.0000)	-6.6080* (0.0000)	-6.5807* (0.0000)
KPSS	Level	0.7007	0.8089	0.8062	0.8012
	First Difference	0.3473*	0.0685*	0.2100*	0.1700*
		SPAIN			
		G	TAX	GDP	TRADE
ADF	Level	-1.4691 (0.5427)	-2.1711 (0.2187)	-0.5915 (0.8646)	-0.8742 (0.7897)
	First Difference	-6.7989* (0.0000)	-13.3265* (0.0000)	-7.6119* (0.0000)	-5.6565* (0.0000)
KPSS	Level	0.9026	0.8193	1.0055	0.9924
	First Difference	0.1384*	0.1200*	0.0591*	0.1221*
		THE NETHERLANDS			
		G	TAX	GDP	TRADE
ADF	Level	0.2996 (0.9767)	0.5743 (0.9880)	1.0271 (0.9965)	0.1155 (0.9647)
	First Difference	-14.5731* (0.0000)	-8.0477* (0.0000)	-10.3905* (0.0000)	-8.9903* (0.0000)
KPSS	Level	1.0687	1.0733	1.0950	1.0847
	First Difference	0.2035*	0.1659*	0.2552*	0.1500*

**Notes:** 1- For ADF test: Symbol \* implies the stationarity. 2- For KPSS test: Critical values for 1%, 5% and 10% respectively: 0.7390, 0.4630 and 0.3470. Symbols \* implies the stationarity.

After applying unit root tests, an error correction model is constructed with first differenced variables. According to Table 3, coefficients of the error terms ( $u(-1)$ ) lie between -1 and 0 and are statistically significant and stationary for all countries. These findings suggest that the error correction mechanism is valid and the variables in question are cointegrated for each country.

**Table 3. Error Correction Mechanism**

Countries	Error Correction Term	Stationarity (ADF Unit Root Test Results)
Belgium	-0.6064 (0.0000)	-6.2500 (0.0000)
England	-0.4375 (0.0000)	-6.5565 (0.0000)
France	-0.3003 (0.0052)	-5.8821 (0.0000)
Germany	-0.7282 (0.0000)	-6.8763 (0.0000)
Spain	-0.4125 (0.0000)	-5.0368 (0.0001)
The Netherlands	-0.7660 (0.0000)	-3.4650 (0.0120)

**Note:** Numbers in parenthesis denote probabilities.

FMOLS is applied to estimate the long run parameters. Results are summed up in appendices. The main findings are presented in Table 4.

**Table 4. The Leading Driver of the Public Expenditures**

	Economical	Commercial	Fiscal	Political
Belgium	1	2	3	4
England	3	4	2	1
France	1	2	4	3
Germany	2	-	3	1
Spain	1	3	4	2
The Netherlands	1	2	-	3

**Table 5. FMOLS Results for Belgium**

Variable	Coefficient	Probability
<b>GDP</b>	2.7208	0.0022
<b>TAX</b>	1.0840	0.0000
<b>TRADE</b>	-1.9294	0.0025
<b>D_1871</b>	0.2318	0.0655
<b>D_1885</b>	-0.2653	0.0001
<b>D_1898</b>	0.2258	0.0518
<b>CONSTANT</b>	-3.7068	0.0004

**Table 6. FMOLS Results for England**

Variable	Coefficient	Probability
<b>GDP</b>	-0.4976	0.0747
<b>TAX</b>	0.5005	0.0000
<b>TRADE</b>	0.2567	0.0115
<b>TREND</b>	0.0149	0.0221
<b>D_CRISIS</b>	-0.1221	0.0262
<b>D_WAR</b>	0.2377	0.0101
<b>D_1841</b>	-0.1761	0.0343
<b>CONSTANT</b>	1.8097	0.0193

**Table 7. FMOLS Results for France**

Variable	Coefficient	Probability
<b>GDP</b>	-1.4073	0.0012
<b>TAX</b>	0.6113	0.0009
<b>TRADE</b>	1.2707	0.0005
<b>D_SECOND REPUBLIC</b>	0.1203	0.0700
<b>D_CRIMEA</b>	0.1943	0.0089
<b>D_PRUSSIAN WAR</b>	0.3846	0.0029
<b>D_THIRD REPUBLIC</b>	0.1892	0.0179
<b>CONSTANT</b>	2.1663	0.0001

**Table 8. FMOLS Results for Germany**

Variable	Coefficient	Probability
<b>GDP</b>	0.9460	0.0989
<b>TRADE</b>	-0.0160	0.9765
<b>TAX</b>	0.3702	0.0768
<b>TAX (-1)</b>	-0.6591	0.0015
<b>D_1888</b>	0.6033	0.0000
<b>D_1897</b>	0.3810	0.0000
<b>D_1907</b>	0.2127	0.0077
<b>CONSTANT</b>	0.3356	0.6818

**Table 9. FMOLS Results for Spain**

Variable	Coefficient	Probability
<b>GDP</b>	1.1094	0.0448
<b>TAX</b>	0.5868	0.0000
<b>TRADE</b>	-2.0948	0.0052
<b>TRADE(-1)</b>	1.3848	0.0005
<b>D_1860</b>	0.2582	0.0316
<b>D_1898</b>	0.2463	0.0412
<b>D_1909</b>	0.2280	0.0528

**Table 10. FMOLS Results for The Netherlands**

Variable	Coefficient	Probability
<b>GDP</b>	0.8060	0.0047
<b>TAX</b>	0.2672	0.3619
<b>TRADE</b>	-0.3215	0.0749
<b>D_1856</b>	0.1725	0.0006
<b>D_CRISIS</b>	-0.0827	0.0406
<b>CONSTANT</b>	0.8568	0.0002

## 6. Conclusions

The alternations in the economic systems change the share of the state in national economies. Before the 19<sup>th</sup> century, public expenditures change depending mostly on political and commercial factors. Due to the transformation process from commercial capitalism to monopolistic capitalism, the significance of the state in the economy has increased.



Political and commercial factors have maintained their importance throughout the 19<sup>th</sup> century. Following the late 19<sup>th</sup> century where public funding was frequently used these factors have been replaced by the economic determinants. In this study, time series procedures are applied to investigate the drivers of the public expenditures in the leading countries of the 19<sup>th</sup> century Europe. The main purpose in so doing is to determine the most dominant variable that explains public expenditures. According to the empirical findings, the long run relationships among the variables are statistically significant. Besides, we conclude that the main driver of public expenditures in the countries is the economic variable. Moreover, for the countries where the economic variable is not the dominant factor, political drivers are important. We also conclude that political changes and crises have played a key role as political determinants. Political factors are the primary drivers of the public expenditures in the UK and Germany. The UK experienced the everlasting Napoleonic Wars in the beginning of the period under investigation and the long depression in the last quarter of the 19<sup>th</sup> century. On the other hand, after Germany had decided a political unification in 1871, she followed a domestic policy known as *Sammlungspolitik* which implies “bringing together” the political parties and groups. These developments can be evaluated as the main reasons why the political factors are the leading drivers of the public expenditures in the UK and Germany.

Liberal economic thought that prevailed in the period is the fiscal variable that plays an insignificant role on the public expenditures. The repercussions of the liberal thought on the commercial sector are the trade agreements signed in the second half of the 19<sup>th</sup> century in order to reduce trade barriers reciprocally. The differences among trade policies of the countries led to the differentiation of the role of commercial factors on public expenditures. Thus, Belgium, the Netherlands and the UK continue to follow free trade policies while France and Germany front the protectionist policies in the 1870s.

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