

# ***State Monopoly or Corporate Business: Warfare in Early-Modern Europe***

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*The shift of the core of Europe from the Mediterranean to the north-west of the continent has been considered the outcome of military advantages which, in turn, mirror the early modernisation of the fiscal systems and constitutions of the northern European states. Bearing this in mind, the Portuguese regaining of Brazil from the Dutch, while they were fighting a war against the Habsburgs to regain political independence, is an intriguing issue which leads us to reconsider the widely-accepted connection between the outcomes of military campaigns and modernisation in financial and institutional spheres. In this paper, special attention is paid to the issue of how private and public affairs could intertwine in forming a state. An enlightened estimate of the rates of return from tax farming is provided, as well as proof that uncertainty caused by war raised profits if the commercial integration of trade and the collection of taxes levied on traded commodities was the rule. The accumulation of capital by private tax-collectors was eventually exploited by the state to regain Brazil from the Dutch by means of a compromise which privatised war in the colony. It is argued that the Portuguese solution as far as warfare was concerned was an efficient response to the colonial issue, albeit a divergence from the modern institutional limit between private and public affairs, which gives the state the monopoly over attack (or over defence).*

## **1. Introduction**

In the early modern period, colonial rivalry interlocked with fighting on European fronts, thereby creating political tension and conflict in a system of dynastic states<sup>1</sup>. War became a driving force for the emergence of the state as an organisation based on a territory, centralised politically,

<sup>1</sup> Richard Bonney, *The European Dynastic States, 1494-1660*, (Oxford 1991).

and sustained by a hierarchy of specialised officials<sup>2</sup>. These aspects of the state, according to Max Weber's ideal-types of social organisations, together with increasing financial resources, empower the state with a monopoly on warfare and governance.

The economic and institutional implications of the monopoly over warfare and governance have been a particular field of analysis focused on fiscal systems and fiscal constitutions<sup>3</sup>. A rich historiography has developed Joseph Schumpeter's ideas on the transformation of the domain state into a tax-state as a determinant path to the modern distinction between the public and private sectors of an economy<sup>4</sup>. Avoiding teleological approaches, historians and political analysts stressed the divergences in this process towards fiscal and financial modernisation, in that private and public affairs interacted differently in each nation, and in each period. However, certain fiscal constitutions found earlier in England and in the Netherlands are deemed to be not only a ratchet effect of war, but also a more effective way to increase levels of "being a state"<sup>5</sup>. These positive outcomes placed these nations at the core of the European system after 1648.

The long-lasting war against the Hapsburgs entailed fiscal innovations in the Netherlands that sustained public borrowing at unprecedented

<sup>2</sup> Max Weber, *Economy and Society*, (New York [1922] 1968).

<sup>3</sup> P.G.M. Dickson, *The Financial Revolution in England: a study in the development of public credit, 1688-1756*, (London 1967); Peter Mathias and Patrick O'Brien, 'Taxation in England and France 1715-1810', *The Journal of European Economic History*, 5 (1976), pp. 601-650. Expanded references, see for all: W.M. Ormrod, M. Bonney and R. Bonney (eds), *Crises, Revolutions and Self-Sustained Growth. Essays in European Fiscal History, 1130-1830*, (Stamford 1999); Richard Bonney (ed), *Economic Systems and State Finance*, (Oxford 1995); Richard Bonney (ed), *The Rise of the Fiscal State in Europe, c.1200-1815*, (Oxford 1999); Michael Bordo and Roberto Cortés-Conde (eds), *Transferring Wealth and Power from the Old to the New World. Monetary and Fiscal Institutions in the 17<sup>th</sup> through the 19<sup>th</sup> centuries*, (Cambridge 2001).

<sup>4</sup> Joseph Schumpeter, "The Crisis of the Tax State" in *The Economics and Sociology of Capitalism*, R. Swedberg (ed), (Princeton 1991) p. 99-140.

<sup>5</sup> Charles Tilly, "Reflections on the History of European State-making" in Charles Tilly (ed), *The Formation of National States ...*, p.32; Edgar Kiser and April Linton, 'Determinants of the growth of the State: war and taxation in Early Modern France and England', *Social Forces*, 80.2 (2001), pp. 411-448.

levels, showing public confidence in the state's financial solvency<sup>6</sup>. In spite of local riots and political tensions between the Estates General and the provincial powers to assign the fiscal burden regionally, the "national" assent to warfare was not jeopardised, resulting in Dutch independence being finally recognised at Westphalia<sup>7</sup>. Hence, the Spanish defeat appears as an inevitable consequence of a less efficient response to the financial pressures war had exerted on royal revenues. Phillip IV's bankruptcies are examples of this – despite the fact that the bankruptcy of 1627 and that of 1647 might have been a refined strategy to negotiate urgent credits with newcomers<sup>8</sup>. The rise in taxes was intolerable for Philip IV's subjects. Since the 1630s, political turmoil had threatened the stability of the composite monarchy<sup>9</sup>. Revolts sprang up throughout the 1640s, one of which gave back sovereignty to Portugal<sup>10</sup>.

The map of the European dynastic states was redesigned to include the kingdom of John IV, Duke of Braganza and King of Portugal (1640-1656). While fighting against Spanish armies for 28 years, Portugal recovered north-eastern Brazil in 1654. This part of the colony had been occupied by the Dutch West India Company (WIC) since 1630. None of

<sup>6</sup> Jan De Vries, "The Netherlands in the New World. The legacy of European Fiscal, Monetary and Trading Institutions for the New World Development, from the Seventeenth to the Nineteenth centuries" in Michael Bordo and Roberto Cortés-Conde (eds), *Transferring Wealth and Power from the Old to the New World...*, pp. 100-139; A. Fritschy, "Financial revolution reconsidered: public finance in Holland during the Dutch Revolt, 1568-1648", *Economic History Review*, 56.1 (2003), pp. 57-89; L. Fritschy, W. Van Der Ent, E. Horlings and R. Liesker, "Public Finance in the United Provinces of the Netherlands in the Seventeenth and Eighteenth Centuries" in W.M. Ormrod, M. Bonney and R. Bonney (eds), *Crises, Revolutions and Self-Sustained Growth...*, pp. 249- 293.

<sup>7</sup> Marjolein C. 't Hart, *The making of a Bourgeois State. War, Politics and Finance during the Dutch Revolt*, (Manchester-New York 1993).

<sup>8</sup> Carlos Alvarez Nogal, *El Credito de la Monarquía Hispanica en el reinado de Felipe IV*, (Madrid 1997).

<sup>9</sup> For the Portuguese case, António Oliveira, *Movimentos Sociais e Poder em Portugal no século XVII*, (Coimbra 2002).

<sup>10</sup> John H. Elliott, *The Revolt of the Catalans. A Study in the Decline of Spain (1598-1640)*, (Cambridge 1963); John H. Elliott, *El Conde-Duque de Olivares*, (Barcelona 1991); Rafael Valladares, *La rebellion de Portugal 1640-1680. Guerra, conflicto y poderes en la monarquía hispánica*, (Madrid 1998); Leonor F. Costa and Mafalda S. Cunha, *D. João IV*, (Lisboa 2006).

the Spanish attempts to rescue the colony was successful. How can the Portuguese victory be explained? Was there a financial resource which Philip IV and his “minister-favourite”, the Condé Duque de Olivares, could not access to support this new war-front effectively? How was Portuguese military enterprise in Brazil organised?

These questions make this historical event a case study. The previously implied connection between successful military outcomes and financial and institutional modernisation should be reconsidered. Other variables which are not so often discussed when analysing fiscal systems and warfare in a comparative perspective should be considered, namely the administration costs of tax, either administrative or compliance costs. The interference of private affairs in tax administration and the issue of the rates of return in tax farming are topics that deserve a deeper analysis for an assessment of military success in the early modern period, which is the aim of this paper. It is supposed that military affairs were constrained by tax administration schemes which, in turn, having impacts on the social redistribution of the “state’s spoils”, reinforced or weakened the power of the Crown facing rival claimants.

A closer look at tax farming, promoting different contexts for public and private spheres to interlock, gives further insight into the issue of divergent paths in state-making processes and colonial rivalry. This paper provides an estimate of the rates of return of tax farming and shows that uncertainty caused by war raised the profits from this financial activity. The business integration of tax administration and the transactions of commodities that were the basis of tax collection enabled an accumulation of capital that was eventually exploited for military success in Brazil. It is argued that the privatisation of warfare was an efficient solution envisaged after the Portuguese Restoration, in view of the merchant-financiers’ interference in the state’s redistributive role for two decades.

Although the event under examination dates from 1654, its explanation lies in a process which took place during the period 1630-1654, when the Dutch occupation of the colony affected the logic of tax administration and when the coup d’état in Portugal increased the costs of war. The first and the second sections present data to estimate the impact of colonial rivalry in Brazil, both on the maritime economy (first section) and on

state revenues mostly dependent on Atlantic flows (second section). It untangles the association of a state financial crisis and economic recession during periods of war. The third section presents an estimate of gross returns from tax farming and analyses the means of capital accumulation needed to rescue Brazil. The fourth section analyses the context for the recovery of Brazil. The conclusion re-evokes the interplay of private and public interests in military outcomes and thus in the creation of a system of dynastic states fighting for colonial dominions.

## **2. Gambling with War**

Portugal was part of the Hapsburg composite monarchy from 1580 to 1640. The multiple fronts of the Dutch-Spanish conflict involved the Portuguese colonial offshoots. Estado da India dominions had been Dutch targets since 1605. But only after the Twelve-Year Truce (1609-1621) did the South Atlantic regions of the Portuguese Empire suffer consequent attacks. In 1621 the Estates General conceded a charter for the next 24 years to the Dutch West Indische Compagnie (WIC). William Usselinx's previous project to establish a company to colonise and develop a plantation economy in Brazil gave way to a more aggressive strategy<sup>11</sup>. Shortly after its foundation, the company occupied the port-town of São Salvador da Bahia, the political centre of Brazil, in 1624. The rescuing of the city by joint Portuguese and Spanish forces turned the year 1625 into a glorious but short-lived time of Spanish victories, since north-eastern Brazil was conquered by the Dutch between 1630 and 1634<sup>12</sup>. Shortly afterwards, the Portuguese slave outlet of El Mina on the north-west African coast capitulated in 1637. The huge Iberian armadas set sail in 1631 and in 1639 to recover the Portuguese position in the south Atlantic regions, but achieved frustrating results, despite the efforts of the Condé-Duque de Olivares to assemble the naval forces and the financial resources of both Spain and Portugal.

<sup>11</sup> Charles Boxer, *The Dutch in Brazil, 1624-1654*, (Oxford 1957), p. 6.

<sup>12</sup> Stuart B. Schwartz, *Da América Portuguesa ao Brasil. Estudos Históricos*, (Lisbona 2003).

The region under Dutch administration, the captaincies of Pernambuco, Paraíba and Itamaracá, was the richest part of a territory which had been attracting Portuguese investment in sugar plantation since 1560/1570. The economy of the colony had grown at an impressive rate since then. The number of sugar mills and estimations of their average productivity ascertain that the north-eastern region was the most important as far as Brazilian exports were concerned. Documental sources reveal a total production of 350,000 arrobas in the whole colony in 1582<sup>13</sup>, reaching a maximum of 960,000 arrobas in 1624, of which Pernambuco contributed approximately 56%<sup>14</sup>. Thus Dutch attacks during the first years of the 1630s deprived Portuguese middlemen of about 544,000 arrobas (10,074 freight tons, 54 arrobas per ton) which were not entirely transferred to the enemy afterwards, since 40-46 mills out of 166 were destroyed or abandoned. Hence, during the first years of the Dutch occupation (1630-1634), the number of sugar chests exported from Recife was considerably small. Exports may not have exceeded 40,017 arrobas (741 tons). Only after 1635 did the economy of “New Holland” prosper. From 1635 to 1640, 14 Dutch vessels shipped 535,152 arrobas to Europe<sup>15</sup>. Meanwhile, privateering proved to be a complementary source of profits, as was expected when the WIC was founded. According to Joahannes Laet’s figures, the 286 Portuguese ships captured yielded 39,355 chests (708,390 arrobas) of sugar, besides dyewood and tobacco worth £708,861<sup>16</sup>.

Dutch military strategy in the South Atlantic had a clearly noticeable effect on the Portuguese business world, particularly in 1627 and in 1633, two years in which 38% of the Portuguese ships listed by Laet were lost.

<sup>13</sup> Frédéric Mauro, *Le Portugal, le Brésil et l’Atlantique au XVII<sup>e</sup> siècle*, (Lisbona 1983), p. 276 (table).

<sup>14</sup> Stuart B. Schwartz, *Segredos Internos. Engenhos e Escravos na Sociedade Colonial*, (S.Paulo 1995), p. 150.

<sup>15</sup> Henk den Heijer, “The Dutch West India Company, 1621-1791” in Johannes Postma and Victor Enthoven, *Riches from Atlantic Commerce, Dutch Transatlantic Trade and Shipping, 1585-1817*, (Leiden 2003), pp. 87-88 and pp. 94-95.

<sup>16</sup> Figures *apud* Joahannes Laet (Brazilian edition), *História ou Anais dos Feitos da Companhia Privilegiada das Índias Ocidentais, desde o seu começo até ao fim do ano de 1636*, (Rio de Janeiro 1925), II, pp. 621-636.

The particularly high risk in certain years had two main consequences which affected freight rates and cargo prices.

Firstly, adapting to risk altered the structure of the fleet. Large vessels, which in the Portuguese Atlantic context meant vessels that could carry 120-150 tons, shared the transportation market with small caravels that could carry less than 50 tons of freight. Each of these tonnage thresholds mirrors defensive tactics which were not mutually exclusive, although they may have protected caravels. Large vessels pushed freight-rate levels upwards, since they demanded investments for the provision of artillery on board, whereas small caravels were equipped to escape quickly from enemy fire and thus expenditure for defence was not necessary. They were riskier, but much more effective in dealing with the Dutch threat. If they met well-armed Dutch vessels, they avoided crossfire and handed over the cargo to the enemy. Both tactics were a response to the lacking defensive structure the state was supposed to provide. Escorting the merchant fleets was a project discussed several times in the Treasury Council in Portugal, but never implemented during the Hapsburg period<sup>17</sup>.

The credit based on bottomry loans to fit out ships explains why surrender was a rational choice. Given the risky environment, shipping depended increasingly on bottomry loans charged with high interest rates. The rules regulating this kind of credit bear a resemblance to gambling<sup>18</sup>. If capital was lost, the borrower was exonerated of the debt and the interest. In the case of good fortune, he had to pay capital and interest, which reached a rate of 100-120 % (*Figure 1*). The escalation of interest rates reported on notary deeds testifies that business was transacted, no matter how risky it might be. The international integration of the insurance market explains why shipping investments continued surprisingly in times of plunder. Portuguese political circles were aware that the war did not

<sup>17</sup> Leonor Freire Costa, *O Transporte no Atlântico e a Companhia Geral do Comércio do Brasil, 1580-1663*, (Lisbona 2002), pp. 180-208.

<sup>18</sup> Leonor Freire Costa, "Privateering and Insurance: Transaction Costs in Seventeenth-Century European Colonial Flows" in Simonetta Cavaciocchi (ed), *Ricchezza del Mare, Ricchezza dal mare, secc XIII-XVIII, Atti delle "Settimana di Studi"*, Istituto Internazionale di Storia Economica "F. Datini", Prato, (Firenze 2006), pp. 703-726.

destroy Portuguese international networks. The connections necessary to spread the risk and to underwrite insurances were in Madrid, Amsterdam or in Hamburg. The average insurance premium was about 10% in northern and north-western markets<sup>19</sup>. A creditor with contacts on the Amsterdam insurance market would lose 10% of the capital if the maritime venture on which he had bet had a tragic outcome. Otherwise he would have earned 90% in a single ship on a voyage back and forth to Brazil, provided the interest reached 100%. Loss-aversion, not risk-aversion, is the incentive for gambling<sup>20</sup>. The prospect of a 90% loss if one did not enter the game put business in motion. Freight rates internalised interest rates and traced a soaring trend (*Figure 2*).

Secondly, the war disturbed maritime communications which increased the difference in cargo prices in Brazil and in Europe. The boost in the arbitrage premium, shown in *Figure 3*, must have played a considerable part in the recovery of the Brazilian economy. In less than ten years, investments in the southern regions of the colony (Rio de Janeiro captaincy) and in Bahia pushed the total sugar production up again to 900,000 arrobas<sup>21</sup>.

The assessment of gross returns from trade and shipping during this period is to be compared with fiscal revenues later. Converting the maximum potential of the colony's exports into freight tonnages (1 ton = 54 arrobas), and taking price differences as a proxy of the arbitrage premium, an educated guess of gross returns is made in Table 1. The calculation of the annual average compound growth rates provides interesting results.

The period of war in Brazil (1624-1637) has one of the highest positive variations, at a 5.8 % rate. It contrasts with previous phases. The period of the Twelve-Year Truce is remarkable for the fact that growth rates, although positive, were less than 1% per year. The negative variation of

<sup>19</sup> J.P. Salvado and S.M. Miranda (editing and footnotes), *Livro I do Governo do Brasil*, (Lisbona 2002), p. 52.

<sup>20</sup> P. L. Bernstein, *Against the Gods. The Remarkable Story of Risk*, (New York 1998), pp. 273-274.

<sup>21</sup> Stuart B. Schwartz, *Segredos Internos. Engenhos ...,* p. 150.



the first decade of the seventeenth century should be imputed to a downward trend in prices after the production rush during the period between 1580 and 1600. The decreasing rates of return between 1600 and 1612/1614 were hardly compensated afterwards, because price differences did not broaden significantly during the Truces, and ascertain that the arbitrage premium was low in years of peace and regular communications.

The crisis evident in *Figure 3* between 1612 and 1623 in Brazil was common to other markets in Europe, particularly between 1618 and 1623<sup>22</sup>. The factors for a recession of the plantation economy have been under discussion<sup>23</sup>. The coincidence between crisis and peace is noteworthy; this contrasts with signs of economic recovery during one of the most dangerous periods of war in Brazil. It is seldom remembered that regular transatlantic communications and a loose policy of embargos on Dutch shipping were common only during the infrequent periods of peace. War, not peace, was the environment for transactions. Thus years of peace and of regular communications favoured the integration of markets but brought fewer opportunities for speculative rates of profit. In seventeenth-century colonial business, there was a crisis whenever market conditions prevented profitable returns. This was the case of the Twelve Year Truce, which was perceived as a time of crisis by the merchant élite most active in colonial trade<sup>24</sup>.

A long period of decreasing premiums and a poor recovery in the years of truce drove the wealthiest merchants out of Brazilian trade flows. They focused on other more promising branches of colonial trade.

<sup>22</sup> Rogiero Romano, 'Tra XVI e XVII secolo. Una crisi economica: 1619-1622', *Rivista Storica Italiana*, 74.3 (1962), pp. 408-531; Charles P. Kindleberger, 'The Economic Crisis of 1619 to 1623', *The Journal of Economic History*, 51.1 (1991), pp. 149-175.

<sup>23</sup> Evaldo Cabral de Mello, *Olinda Restaurada. Guerra e Açúcar no Nordeste, 1630-1654*, (Rio de Janeiro 1998); Russell R. Menard, 'Law, credit, the supply of labour, and the organisation of sugar production in the colonial Greater Caribbean: a comparison of Brazil and Barbados in the seventeenth century' in John J. McCusker and Kenneth Morgan (eds), *The Early Modern Atlantic Economy*, (Cambridge 2000), pp.154-162.

<sup>24</sup> Leonor Freire Costa, 'Caravelle et Flottes Escortées: risque et affaires au XVIIe siècle dans l'Atlantique Portugais' in Silvia Marzagalli and Bruno Marnot (eds), *Guerre et Économie dans l'Espace Atlantique du XVIe au XX Siècle*, (Bordeaux 2006), pp. 180-184.

Supplying slaves to Spanish South American colonies, trading Indian textiles, providing credit to the Crown and tax farming were their business. The access to silver gave coherence to this “global” business strategy, which was also aimed at the Far East regions of Macao and Japan<sup>25</sup>. And silver was also the commodity that drove the merchant élite to Madrid around 1625 to act as the King’s bankers<sup>26</sup>.

That part of the merchant élite that remained in Portugal, the majority of whom were new Christians, considered Brazil a minor investment and left room for others to enter the sugar trade during the 1620s. The characteristics of this emergent merchant class is the subject of one of the best studies in historical sociology by David Grant Smith<sup>27</sup>. The author highlighted the presence of old Christians, questioning the traditional views on merchant-financiers and financial intermediation in the Iberian kingdoms as being the exclusive business of new Christian or Jewish families.

Although not found in Smith’s study, another feature of this renewed “merchant class” was the business networks which gave Oporto an important role in fitting out ships for Brazil<sup>28</sup>. Old Christian merchants’ networks integrated trade and shipping and connected the Portuguese northern port-towns to Lisbon, where information about political and economic decisions made at the Treasury Council could be more accurate than in peripheral ports. However, Castilian supervision of Dutch shipping became extraordinarily tight in Lisbon after the *Almirantazgo* (1634), this institution having facilities in the capital that were lacking elsewhere. Thus Portuguese secondary ports were better located than Lisbon for intermediary trading<sup>29</sup>.

<sup>25</sup> V. Magalhães Godinho, “1580 e a Restauração” in V. Magalhães Godinho, *Ensaio II*, (Lisbona 1978).

<sup>26</sup> James Boyajian, *The Portuguese Bankers at the Court of Spain, 1626-1650*, (New Jersey 1983); A. Dominguez Ortiz, *Política y Hacienda de Felipe IV*, (Madrid 1983).

<sup>27</sup> David Grant Smith, *The Portuguese Mercantile Class of Portugal and Brazil in the Seventeenth Century: a socioeconomic study of the merchants of Lisbon and Bahia, 1620-1690*, PhD dissertation, (Texas, Austin, 1975).

<sup>28</sup> Leonor Freire Costa, *Império e Grupos Mercantis. Entre o oriente e o Atlântico (século XVII)*, (Lisbona 2002).

<sup>29</sup> Jonathan I. Israel, *The Dutch Republic and the Hispanic World. 1606-1661*, (Oxford 1982), pp.138-139.

Agencies in Portuguese ports, new means of spreading the risk of bottomry loans charged with high interest rates, and the integration of shipping and trade in times of soaring freight rates provide conditions for capital accumulation. In due time, these competitive newcomers would confront the established oligarchy of merchant-financiers, still involved in the Indian trade, to reap tax farming contracts. They collected taxes levied on commodities they themselves traded: this is another business diversification deserving further attention in Section 4.

The competition between established merchant financiers (such as Pedro Baeça da Silveira or Diogo Rodrigues de Lisboa) and rising newcomers (such as Duarte da Silva, Gaspar Pacheco and the Malheiro brothers) in the tax-farming business was not fierce enough to increase the values of tax-farming contracts. After all, connections between old and new factions weakened previous internal tensions. Consider the case of the new Christian Diogo Rodrigues de Lisboa and his son Jorge Gomes Alamo who became partners of old Christian newcomers such as Gaspar Pacheco. Despite the group's cultural and religious heterogeneity, and its availability of capital for farming the state's revenues in times of crisis, its cohesion made the King the weakest party in negotiation.

### **3. The Losing Party**

The Portuguese fiscal system mirrors the extent to which the Crown's revenue depended upon the empire. The majority of income was based on indirect taxation on imports from Europe and on re-exports of exotic goods from the Empire. In the early sixteenth century, maritime flows already accounted for 65% of the total income collected in the kingdom<sup>30</sup>.

<sup>30</sup> The pioneering work: V. Magalhães Godinho, "Finanças públicas e estrutura do Estado" in V. Magalhães Godinho, *Ensaios II*, (Lisbona 1978), pp. 31-74. Last synthesis, A. Ferreira da Silva, "Finanças Públicas" in P. Lains and A. Ferreira Silva (eds), *História Económica de Portugal, 1700-2000*, 3 vols, (Lisbona 2004), I, p. 253; Jorge B. Macedo, A. Ferreira Silva and Rita M. Sousa, "War, taxes and gold. The inheritance of the real" in Michael Bordo and Roberto Cortés-Conde (eds), *Transferring Wealth and Power from the Old to the New World...*, pp. 187-228.

A 10% tax *ad valorem* on imports and tolls levied at different rates on exports were collected at custom-houses in a few of the kingdom's port-towns. Lisbon customs formed a separate administration, implying that any contract envisaging the "general" farming of customs did not embrace the "Houses" of Lisbon.

A 3% tax on imports and exports called *consulado* was also collected in a separate department. Unlike any other tax on foreign trade, the administration of *consulado* included taxation in Lisbon, but not at *Casa da Índia* (the institution which managed the route of "Carreira da Índia" and whose warehouses were used to collect taxes levied on commodities imported from India). Hence, values referring to the *consulado* tax do not include the taxation of commodities sent and received through the Cape Route. Originally, this tax was implemented to subsidise the protection of the coast from Muslim piracy and from other perils in times of war. From 1593 to 1604 the mercantile class was responsible for its administration, following the Castilian model in which the *Consulados* were both institutions representing the interest of merchants and also tax departments. However, in Portugal the institution was short-lived. The reason for its failure has never been studied, but the issue is not relevant here, since the tax remained as part of the fiscal system until the nineteenth century, although the mercantile institution had been extinct since 1604.

Apart from customs, other budgetary items related to Atlantic flows, namely the Crown's rights over the slave trade in Cape Verde and Angola, formed a set of revenues to be considered in this section.

The contemporary perception that customs were crucially dependent on sugar must be emphasised. The administrative staff were convinced that foreign ships called at Portuguese ports loaded with cargoes to supply the market in Portugal and in her colonies merely to return with sugar. In 1636, the Treasury Council reminded the Madrid authorities that receipts for the *consulado* tax in Lisbon had been almost frozen from January to August, awaiting the arrival of the Brazilian fleets. Once they arrived, the chests of sugar provided about 7,000,000 réis in one single month<sup>31</sup>.

<sup>31</sup> Lisbon Archives, Arquivo Histórico Ultramarino, *Conselho Ultramarino*, cod. 42, fl. 44 ss.

If customs revenues were overwhelmed by *ad valorem* taxes on sugar, inflation after 1625 and the recovery of production in Brazil during the 1630s suggest the likelihood of a positive variation of the state's income in nominal values after 1625. It is to be assessed whether customs duties varied at a lower or higher rate than prices of an important commodity. Estimating the variation of customs yields and comparing it with the variation of gross returns from Brazilian flows assess to what extent businessmen were richer than the state in times of war in Brazil.

Long series of customs duties prior to the second half of the eighteenth century are not available in Portuguese archives<sup>32</sup>. Furthermore, figures regarding the state's income necessitate several sources. A few budgets were recorded, but are somewhat meagre. And tax-farming contracts registered in books of the Treasury Council, albeit few, provide intriguing information. Thus, budgets and Treasury Council records are the documental sources considered here.

*Table 2* gathers figures on five budgetary items that may be related, directly or indirectly, to the Atlantic trade, with regard to the benchmarks that oriented analysis in the first section. The annual average compound rate asserts that customs yields did not rise from 1625 to 1637. In spite of increasing prices, all the items varied at a negative rate of about -2% and -3%, displaying a rather distinct trend of state revenues compared to gross returns of trade and the shipping of sugar, varying about 5% (*Table 2.1* and *Table 3*).

The Dutch assaults on the Portuguese fleet might have had a disastrous effect on the quantity of sugar actually unloaded in Portuguese ports. Thus, the basis of taxes collected in the kingdom might have been more restricted than figures on the revival of the sugar plantations suggest. Furthermore, while agents used different tactics to spread the risk, the state merely acknowledged the consequences of plunder and of communication hindrances in decreasing yields. To consider this responsible for the declining values forecasted in state budgets would be merely to scratch the top of the iceberg.

<sup>32</sup> Except in the case of Oporto.

Administration procedures are relevant factors for budgetary values, in this case for their negative variation, since they stem from a negotiation between tax farmers and the Treasury Council<sup>33</sup>. The risk in maritime economy was evoked as a variable in negotiations. But it was to the tax farmer's advantage to over-rate this risk in order to press the state to accept low bids. If the aim of the Treasury Councillors was to remain close to a group of merchant-bankers who provided annual lump-sums, the acceptance of an underestimation of tax yields was a decision of surrender. Hence, budgets do not express the extractive potentials of the economy; on the contrary, they express expectations with which tax farmers and the state were willing to establish an agreement.

According to documentary sources available, it was only from 1635 that contracts for tax farming contained forward clauses, foreseeing the recovery of Pernambuco. If this event occurred during the time of the contract, lump-sums delivered to the Treasury should be raised. Consider, for instance, the following two cases. As for the Angola contract, dating from 1635, tax farming procedures started with an auction at the Treasury, as usual, followed by particular negotiations with the best bidder (Pedro Rodrigues de Abreu in this case). The definitive version of the agreement obliged the contractor to pay an extra 5,000,000 réis (20% more) besides the 25,000,000 réis annuity (forecast in budgets and taken into account in Table 2), if the conditions were fulfilled<sup>34</sup>. As for the farming of the *consulado* tax being negotiated in 1638, if Pernambuco were recovered and if a general peace treaty in Europe were signed, the 50,000,000 annuity was increased by 12,000,000 réis (24% more)<sup>35</sup>. Such clauses

<sup>33</sup> As it is recalled by John H. Munro, *The Usury Doctrine and Urban Public Finances in Late-Medieval Flanders (1220 - 1550): Rentes (Annuities), Excise Taxes, and Income Transfers from the Poor to the Rich*, Working Paper 288, 2007, p.21: <http://www.economics.utoronto.ca/index.php/index/research/workingPaperDetails/288%3E>.

<sup>34</sup> Frédéric Mauro, *Le Portugal, le Brésil et l'Atlantique...*, p. 180. The bid of 24,000,000 réis of Estêvão Rodrigues was declined. See Lisbon Archives, Arquivo Histórico Ultramarino, *Conselho Ultramarino*, cod. 41, fl. 93v<sup>o</sup>.

<sup>35</sup> Contract for the period 1640-1642; José Justino de Andrade e Silva, *Collecção Chronologica da Legislação Portuguesa*, (Lisboa 1855-1856) <http://www.iuslusi.taniae.fcsh.unl.pt>.

implied that the Dutch occupation of north-eastern Brazil was costing the state a loss in customs revenues of between 20% and 24%. It created, however, new chances for tax farmers to profit from uncertainty.

Contracts, including forward clauses, required an estimation (or at least an accurate perception) of the risk in the economy at the time negotiations were carried out. Meanwhile, the disturbances of war and communication hindrances raised the cost of information, which was unequally distributed among the parties in fiscal contracts. Tax farmers, who also traded in Brazilian commodities, were better informed on the economic environment than the Treasury officials, and were thus in a position to exploit the state's risk-aversion. Unequally distributed information worked to the benefit of tax farmers, who managed their investments in fiscal collection by signing worthwhile contracts and abandoning the others. While the *consulado* tax and duties on slaves from Angola continued to attract positive decisions on the part of agents, the contract for Cape Verde slaves did not find a bidder from 1636 onwards<sup>36</sup>.

The strategy of tax farmers was not perceived as such by the Treasury Councillors, who merely wondered about some contracts still having bidders and considered low values in auctions an inevitable consequence of the crisis. Tax farmers, however, were adapting to the different impacts the war had on Atlantic trade. The Dutch presence on the West African coast deprived the Portuguese of the slave trade in El Mina, but boosted Portuguese trade with Angola. Slaves from Angola provided the recovery of the Brazilian sugar economy, which responded to an arbitrage premium varying at an annual average rate of 5%. Profits from trade in times of war enabled returns to be spread in investments in safer business, such as financing the state. Unlike English tax farmers in other war contexts, who considered this kind of investment unattractive, tax farmers in Portugal deemed colonial rivalry in Brazil a suitable environment, which may be taken as a significant signal of worthwhile rates of profit<sup>37</sup>.

<sup>36</sup> Lisbon Archives, Arquivo Histórico Ultramarino, *Conselho Ultramarino*, cod. 41, fl. 93v<sup>o</sup>.

<sup>37</sup> Patrick O'Brien and Philip A. Hunt, "England, 1485-1815", in Richard Bonney (ed), *The Rise of the Fiscal State ...*, p. 71.

#### 4. Profits from Taxes

Gross returns from tax farming regulated by forward contracts depended on the estimations of risk in the economy, for which merchants who were also tax-farmers had better skills than the Treasury Councillors. The difference between the risk within tax farming, diminishing state revenues by 20% to 24%, and that incurred by private organisations, which collected taxes levied on commodities exposed to privateering assaults, is a surrogate for profits from dealing with state spoils. The risk in economic flows may be assessed from information on insurance premiums and from estimations of capital loss over the maximum potential capital invested. The aforementioned information on the international insurance market should be borne in mind. According to Treasury officials' sources, the insurance premium for voyages to Brazil was then at 10%. On the other hand, an enlightened estimate of risks in South Atlantic Portuguese flows, deemed at 10 -12%, seems realistic<sup>38</sup>. Hence, considering such a rate of risk in maritime flows, the profit from tax farming could have reached 10-14%.

A comparison with other national contexts would help to validate this estimation, but data are rather scanty. Tax farming may have afforded a 10% profit in the Netherlands too, the only known case for comparison because it also was based on an estimated rate<sup>39</sup>. Although auctioned by men and women of moderate means, tax farming granted higher returns than public loans (annuities), which had interest rates of 4%<sup>40</sup>. There is comparatively more information available on short-term public credits in the Habsburg kingdom. Higher returns were fairly plausible, since time lags between borrowing and reimbursement could capitalize interest

<sup>38</sup> Leonor Freire Costa, *Fiscal innovations and the making of the modern state: which war did really matter in the Portuguese case?*, paper presented at the *Third Iberian Economic History Workshop: Iberometrics III*, Valencia, March 23 and 24, 2007.

<sup>39</sup> Marjolein C. 't Hart, *The Making of a Bourgeois State...*, p. 193.

<sup>40</sup> L. Van Der Ent, W. Fritschy, E. Horlings and R. Liesker, "Public Finance in the United Provinces of the Netherlands in the Seventeenth and Eighteenth Centuries" in W.M. Ormrod, M. Bonney and R. Bonney (eds), *Crises, Revolutions and Self-Sustained Growth...*, p. 262.



rates of 8-9% for several years<sup>41</sup>. However, interest was just a small part of the rewards in this business. Reimbursements in silver, which had an exchange premium, and social honours redistributed in the highest financial circles in Madrid led part of the Portuguese merchant élite to banking at the court of Philip IV<sup>42</sup>. As for those who remained in Portugal with connections in the Brazilian South Atlantic world, their diversification of investments included bottomry credits with an interest rate of 100%, the sugar trade and contracts for tax farming. Although lower than other returns from banking in Madrid, profits from taxes in Portugal were certainly more rewarding than long-term public loans (*juros*) or private credits subjected to a regulated rate of 5-6.25%.

Official papers, however, suggest profits could have been higher than those estimated. The Angola contract with Estêvão Rodrigues de Estremoz for the period 1628-1636 provides an impressive example. Perhaps it is too unique for us to be able to draw conclusions from it. However, it must be quoted, since it provides actual figures, and above all, it ascertains that Crown officials had access to account registers of taxes collected by private agents. The annual lump-sum agreed in this contract increased to 29,000,000 réis. There is no information about forward clauses. Consulting the accounting books of the tax administration assured the decision makers in the Treasury Council that the average annual sum collected amounted to 42,819,156 réis. As far as this particular contract is concerned, gross returns achieved a rate of 46.7%<sup>43</sup>.

The story highlights two important issues. Firstly, it testifies the state had a means of assessing the contractor's profit. However, the negotiation of the next contract for the period from 1636-1644 ended up by fixing an even lower amount (25,000,000 réis). The clauses foreseeing changes in the diplomatic environment are the only innovation, the weakest party in the deal trying to constrain the other party as far as it could. This is worthy

<sup>41</sup> A. Dominguez Ortiz, *Política y Hacienda de Felipe IV* ..., p. 92; Carlos Alvarez Nogal, *El Crédito de la Monarquía Hispánica* ..., p. 202.

<sup>42</sup> Juan Gelabert, "Castile, 1504-1808" in Richard Bonney (ed), *The Rise of the Fiscal State in Europe*..., p. 217.

<sup>43</sup> Lisbon Archives, Arquivo Histórico Ultramarino, *Conselho Ultramarino*, cod.44, fl. 56.

of a comment recalling the Stuarts' decision to abandon tax farming in the reign of Charles II. In the uncertainty of war the state sought to control tax farmers' profits by seeking "all the information required to renegotiate contracts on more favourable terms". The acknowledgement that tax farming did not have the intended benefits led to a significant change in tax administration, and led to the replacement of tax farming by a "centralised supervision and direct administration by paid servants of the Crown"<sup>44</sup>. The second issue stems from comments on the first: if Crown officials were aware of the actual numbers involved in the merchant's collection of duties on slaves from Angola, it seems that the administration procedures of tax farmers were not hidden from the state or else that the administration of tax collection was not totally in the hands of contractors. In any event, although private organisations were called upon to participate in fiscal affairs, tax farming did not release the state from funding a bureaucracy. The main purpose of farming out taxes was not to free monitoring devices that would decrease administration costs. A centralised tax-administration was already created, albeit in its early stages, customs and the Treasury accounting for 37% of all civil servants<sup>45</sup>. In fact, the transition towards an organisation based on a hierarchy of agents in a Weberian sense had already begun quite some time before. But the fact that certain positions still allowed patrimonial rights over the posts, besides an annual salary, prevented tax farming from being an effective means of releasing the state from the costs of a bureaucracy.

Historical and sociological approaches to forming a state have underlined the need to analyse features commonly found in economic studies on developing countries. Collection costs and the potential gross revenues collected tend to be related to economic development. Levels of illiteracy, technological constraints and a high degree of self-consumption are characteristic of non-modernised economies and explain the high costs of tax administration. And so bureaucracy may not be an efficient device

<sup>44</sup> Patrick O'Brien and Philip A. Hunt, "England, 1485-1815" in Richard Bonney (ed), *The Rise of the Fiscal State...*, p. 73.

<sup>45</sup> A. Hespanha, *As Vésperas do Leviathan. Instituições e poder político. Portugal, século XVII*, (Lisbona 1994), p.175; pp. 204-209.

to increase the gross revenues of the state<sup>46</sup>. Tax farming, instead, may be the only feasible method of collection, avoiding the volatility of receipts and responding efficiently to principal-agent problems<sup>47</sup>. Similar documented assertions regarding solutions for the state's limited monitoring capacities do not accurately describe the case of tax farming in Portugal, nor in Iberia in general.

If tax farming was submitted to auction and if no bidders could be found for contracts, a bureaucratic staff had to be allocated to the collection of taxes which was intermittently transferred to private organisations. In England, not only was tax farming a scheme regularly applied to certain taxes – such as customs and excises – but also tax farmers organised and paid for the administration. This enabled private agents to improve tax management with the aid of skilled officials who went on to be integrated into the state's bureaucracy when tax farming was abandoned<sup>48</sup>. Hence, compared to the English case, tax farming in Portugal delayed a bureaucratisation that would, in fact, make the state's marginal income equal the marginal costs of administration. At the same time, profits from tax farming influenced the redistribution of state spoils more than elsewhere, while enabling a group of merchants to accumulate capital.

What drove the Iberian states to adopt a scheme that apparently transferred fiscal income to private organisations, thereby acting to the state's disadvantage? The explanation is two fold. Firstly, as was the case everywhere, the close connection between the collection of taxes and short-term loans, making the contracts under analysis a negotiation for securities; secondly, and this was more evident in Iberia than elsewhere,

<sup>46</sup> Edgar Kiser and Joachim Schneider, 'Bureaucracy and efficiency: an analysis of taxation in Early Modern Prussia', *American Sociological Review*, 59.2 (1994), pp. 187-204; Edgar Kiser and Joshua Kane, 'Revolution and State Structure: the bureaucratization of tax administration in Early Modern England and France', *The American Journal of Sociology*, 107.1 (2001), pp. 183-223.

<sup>47</sup> Eugenia Froedge Toma and Mark Toma, 'Tax collection with agency costs: private contracting or government bureaucrats', *Economica*, 59.1 (1992), pp. 107-120; Eugene N. White, 'From privatized to government-administered tax collection: tax farming in eighteenth-century France', *The Economic History Review*, 57.4 (2004), pp. 636-63.

<sup>48</sup> John Brewer, *The Sineus of Power. War, Money and the English State, 1688-1783*, (New York 1989), pp. 91-93.

the state's aversion to risk, which aimed to reduce the volatility of revenues and thus sought regular delivery of lump-sums in periods of increased expenditure.

A long period of war resulted in this strategy lasting for many years in Iberia. The tax farmers' involvement in public short-term loans strengthened their negotiation position and determined their high social rank within the moneyed classes, in contrast to the Dutch experience of tax farming as a middle-class business. The system in Iberia might not have always acted to the state's disadvantage, because the relationship between parties could occasionally change the imbalance of power. Amounts that had not been actually delivered by tax farmers could be used as state bonds on future occasions, lowering the interest rate for future borrowing. However, debt accumulation was also a factor for the same parties to meet in contracts. The Treasury Councillors were aware that the scheme was dangerously self-enforcing, reducing the number of individuals interested in the business<sup>49</sup>. The more the state acted indirectly to shrink the number of bidders, the less auctions boosted the sums at stake. Hence, a second factor explaining the endurance of tax farming, in spite of decreasing receipts, was the state's risk-aversion and its consequences in creating a cohesive group of merchant-financiers.

The management of debt through repeated contracts created personal links between the Treasury Councillors and a rather small number of merchant-financiers, which were only somewhat disturbed by the political events of the 1640 rebellion. However, as far as the role of merchant-financiers in supplying the state's demand for funds is concerned, events during the restoration of Portuguese independence appear to be a continuation of the Hapsburg inheritance rather than a break with it.

After the *coup d'état* on 1 December 1640, the mercantile group were wary of the political turmoil. A few months after the revolt, one of the wealthiest bankers, Pedro Baeça da Silveira, the brother of a powerful *asientista* living in Madrid, conspired against King John IV. During his

<sup>49</sup> Lisbon Archives, Arquivo Histórico Ultramarino, *Conselho Ultramarino*, cod. 40, fl. 47 (document dating from 14 October, 1634).

trial, he claimed to have dragged his peers into the conspiracy. The King condemned the leaders of this counter-coup and acted magnanimously by releasing other wealthy merchants, such as Jorge Gomes Alamo and his elderly father, Diogo Rodrigues de Lisboa. Pedro Baeça da Silveira was executed, together with a few members of the aristocracy charged as guilty of treason against King John IV. After this spectacularly gory episode in Lisbon's central square in August 1641, anyone who had ever had any doubts about the sustainability of the revolt was forced to side with the new *status quo*<sup>50</sup>.

Having tamed the wealthy élite, King John IV counted on them to fund the war in the Iberian Peninsula against the Hapsburgs, increasing the number of opportunities for credit that created a symbiotic relationship between public and private interests. Thirty-six individuals in the entire country regularly contracted army provisioning, such as gunpowder, bread and barley and the payment of *soldos*, which was envisaged in a contract designated "frontiers". The sums for funding military expenditure and other sorts of short-term loans, reproducing the Spanish system of *asientos*, amounted to over 4,000,000,000 réis in nine years. A direct tax called *décima*, levied on any kind of income, an innovation in the Portuguese fiscal system and rather "revolutionary" for early-modern Europe patterns, was the security for the state's war debt<sup>51</sup>. However, the sums quoted above (approximately 4,000,000,000 réis) were 4.6 times the total receipts annually forecasted in the collection of the *décima*. While the state incurred the administration costs of this entirely new income tax, warfare concentrated fiscal revenues in a small group of merchants, exerting a huge influence on the social redistribution of income within the Kingdom.

<sup>50</sup> Leonor F. Costa and Mafalda S. Cunha, *D. João IV...*, pp. 105-128.

<sup>51</sup> About *décima*, Vitorino Guimarães, *As Finanças na Guerra da Restauração, 1640-1668*, in *Revista Militar*, (Lisbona 1941); António M. Hespanha, "As Finanças da Guerra" in Manuel Themudo Barata and Nuno Severiano Teixeira, *Nova História Militar de Portugal*, 3 vols, (Lisbona 2004), II, pp. 176-195; Joaquim Romero Magalhães, 'Dinheiro para a Guerra: as décimas da Restauração', *Hispania*, 64.1 (2004), pp.157-182; Leonor Freire Costa, "Fiscal innovations and the making of the modern state: which war did really matter in the Portuguese case?"... *Iberometrics III*, Valencia, March 23 and 24, 2007.

Credit to the King was not confined entirely to capital owned by merchant-financiers. They performed banking activities, investing in state loans capital borrowed from members of the aristocracy<sup>52</sup>. The income expectations of the aristocratic rationale were met by a safe interest of 5-6.25 % paid by those financiers who were promoting a financial intermediation which included the powerful landed classes in lending money to the state. Intermediation of this kind committed potential centripetal forces to the successful outcome of the revolt and the war in the Iberian Peninsula, creating political capital that was indeed determinant in revolutionary situations<sup>53</sup>. If the revolt's sustainability became a necessity for the future reimbursement of loans, public debt forged a "national" compliance to a much heavier fiscal burden than ever during the Hapsburg period<sup>54</sup>.

Nevertheless, the huge share of war credits counted on the brokerage of merchant financiers whose regular transactions with the state led them to become familiar with important political people. Public debt was far from being actually "public". It was rather a means of binding the King to his bankers. It is important to remember that these bankers never specialized in financial intermediation, because they followed a strategy of diversification. They dealt in banking, rights over fiscal revenues and, above all, commerce with Brazilian ports, namely in Dutch Pernambuco, where several of them had agents and relatives instigating and subsidising the revolt that sprang up in June 1645 to expel the Dutch WIC administration.

The question about the availability of financial resources for the recovery of Pernambuco finds an answer in two decades of capital accumulation by a rather narrow social group that still had interests in the sugar business.

<sup>52</sup> David Grant Smith, *The Portuguese Mercantile Class of Portugal and Brazil ...*, p. 129.

<sup>53</sup> Considering Tilly's concept of "revolutionary situations": Charles Tilly, *European Revolutions, 1492-1992 (Making of Europe)*, (Oxford 1996).

<sup>54</sup> Castile was the Kingdom within the Habsburg composite monarchy having the greatest fiscal burden and was spared social turmoil: Juan Gelabert, "The evolution of the Spanish Monarchy's expenditure between 1598 and 1650. The "asientos" of Philip III and Philip IV" in W.M. Ormrod, M. Bonney, and R. Bonney (eds), *Crises, Revolutions and Self-Sustained Growth...*, pp. 224-248.

But the organisation of the military expedition that gave the colony back to Portugal required the King to declare to his merchant-bankers that Pernambuco was a war of their own. Such a split in financial and political circles was consistent with the new diplomatic scenario of 1648, when the peace of Westphalia increased the threat of Philip IV's armies invading Portugal.

## **5. The Recovery of North-East Brazil from the Dutch**

The restoration of Portuguese independence in December 1640 could have opened the way to a peaceful agreement for the Brazilian issues. In fact, the principal mission of Francisco de Sousa Coutinho, Portuguese Ambassador in the Hague, was the secret instruction to purchase the north-eastern region of Brazil for 2,400,000,000 réis<sup>55</sup>. The proposed transaction was not new. The Condé-Duque de Olivares had thought of trading Breda (one of the most celebrated victories of the Hapsburg army in Europe), for Pernambuco. It became a rejected path to peace, certainly as far as his political reputation was concerned<sup>56</sup>.

To continue his mission successfully, the Portuguese ambassador in the Hague closely monitored the WIC's political situation from 1643. The Company's charter expired in 1645. He presumed its renewal was strictly dependent on economic variables. In his correspondence with Lisbon, he seemed to be well informed about the stock market in Amsterdam. According to his sources, between April 1643 and October 1644 the Company's shares had been devalued by 30%. He presumed this was facilitating his mission, since he assumed capital devaluation reduced the Company's chances of obtaining a new charter<sup>57</sup>.

<sup>55</sup> Evaldo Cabral de Mello, *O Negócio do Brasil. Portugal, os Países Baixos e o Nordeste, 1641-1669*, (Lisbona 2002). Still irreplaceable for a broader view: Edgar Prestage, *The Diplomatic Relations of Portugal with France, England and Holland from 1640 to 1668*, (Waltford 1925).

<sup>56</sup> John Lynch, *España Bajo los Austrias*, 2 vols, (Barcelona 1991), II, p. 156.

<sup>57</sup> Correspondance of the ambassador in Edgar Prestage and Pedro Azevedo, *Correspondência Diplomática de Francisco de Sousa Coutinho durante a sua embaixada na Holanda*, 3 vols, (Coimbra 1920-1926), I, p. 29; p. 131.

The revolt in Pernambuco led by Portuguese owners of sugar plantations in June 1645 aborted the talks about a peaceful solution for Brazil and shaped an entirely different diplomatic environment. While the war in the colony drove the Estates General to approach the WIC's economic situation as a public issue, factions within political circles in Portugal were inclined to regard Pernambuco either as a lost cause or as a matter to be solved by private corporate enterprise. The divergent national opinions on colonial rivalry being a public or a private affair must be taken into account when analysing the outcome of these historical events.

The importance the Estates General attributed to the Brazilian war gave a renewed charter to the WIC in 1645. The coincidence between the year of the revolt and the deadline of the first charter is not accidental. But the circumstances in which the revolt sprang up are not relevant here<sup>58</sup>. However, it is to be remembered that public resources were invested in the Company to provide it with the means to control the territory. The Estates General granted the company military facilities and forced the VOC to lend a huge amount of capital (f. 1.5 million), which resembles other extortions to which these more prosperous corporate enterprises involved in the Indian trade were submitted<sup>59</sup>.

The links between states and corporate business show how public and private social spheres were interwoven in early-modern Europe<sup>60</sup>. Although chartered companies were the organisational model promoted to exploit resources overseas and to undertake long-distance trade, the relationship these companies established with the state often forced them to act as creditors in times of crisis. The regular extortions exerted by the Stuarts on the English East Indian Company are just another example of an institutional framework that made corporate business

<sup>58</sup> For the revolt in Pernambuco, Brazilian historiography is the best: José Antônio Gonsalves Mello, *João Fernandes Vieira. Mestre de Campo do terço de Infantaria de Pernambuco*, (Lisboa 2000); Evaldo Cabral de Mello, *Olinda Restaurada...*

<sup>59</sup> Henk den Heijer, "The Dutch West India Company, 1621-1791" in Johannes Postma and Victor Enthoven, *Riches from Atlantic Commerce...*, p. 97.

<sup>60</sup> Robert B Ekelund Jr. and Robert D. Tollison, *Politicized Economies. Monarchy, Monopoly, and Mercantilism*, (Texas 1997), pp. 154-184.



depend upon the good grace of kings who granted property rights in royal dominions<sup>61</sup>.

The economic consequences of these blurred institutional boundaries have been under discussion for some time in economic history. The political power and the monopoly rights of these companies entailed confidence in investments in risky economic ventures, pushing the scale of international transactions upwards. Nonetheless, the management of these gigantic enterprises, incurring corruption and facing agency problems, had drawbacks that hindered an increase in the economic efficiency of long-distance trade<sup>62</sup>.

The Portuguese ambassador's comments on chartered companies, as he observed a new business world in Holland in 1644, highlighted the advantage that was expected of chartered companies in spreading risk. Furthermore, the ambassador's words reveal a contemporary view on the relationship of political regimes and interest groups. To assess the WIC's probabilities of getting its charter renewed, he asked well-informed people within the Estates General what drove Dutch public opinion to comply with monopolies. In his view, a Republican regime should not trade off property rights to particular groups, favouring some to the disadvantage of others. He was told that chartered companies were the best institutional device to deal with risk in long-distance trade<sup>63</sup>.

This contemporary – at least Portuguese – pre-conceived idea of the Republican regime as being less prone to the penetration of private interests in political decisions is remarkable. It means that, in the ambassador's view, monarchies, on the contrary, were based on the infiltration of particular interests in centres of economic regulation

<sup>61</sup> Glenn O. Nichols, 'English government borrowing, 1660-1688', *The Journal of British Studies*, 10.2 (1971), p. 87.

<sup>62</sup> Ann M. Carlos and Stephen Nicholas, 'Theory and history: seventeenth-century joint-stock chartered trading companies', *The Journal of Economic History*, 56.4 (1996), pp. 916-924; Jones, S. R. H. and Ville, Simon P., 'Efficient transactors or rent-seeking monopolists? The rationale for early chartered trading companies', *The Journal of Economic History*, 56.4 (1996), pp. 898-915.

<sup>63</sup> Edgar Prestage and Pedro Azevedo (eds) *Correspondência Diplomática de Francisco de Sousa Coutinho ...* letter to King John IV of 9 August 1643, p. 29.

shielded from public scrutiny. Hilton Root called such discretionary access to means of influencing power “cronyism”, this being typical of the French regime; it was not the same as corruption and lobbying in Parliamentary England<sup>64</sup>. When lobbying was an institutionalised means of interfering in economic regulation on the part of private interests, Parliament was the proper forum to make it a public issue. The activity of interest groups may have become a time-consuming and information-demanding political practice, but it was certainly open to competition. In the long run, lobbying became more difficult to promote in Parliamentary regimes than in monarchical regimes where the Crown allowed merchants to lobby for regulations which would serve both the lobbyists and the fiscal priorities of the government<sup>65</sup>. Patronage and clientele were institutions suited to this political practice. According to Root, cronyism meant to keep lobbying a private issue, thus making it subject to discretionary decision<sup>66</sup>.

The Brazilian issue triggered a variant of “cronyism” in Portugal. The company founded in 1649 to respond to the colonial interests of a group – named Companhia Geral do Comércio do Brasil – is, on the contrary, the outcome of the King lobbying his merchant-financiers, seeking to transfer the burden of war to private corporate enterprise. Diplomatic and economic contexts favoured the King’s desire.

Immediately after the revolt had broken out in Pernambuco in 1645, the Dutch reacted quite effectively. The plundering carried out by a Zeeland company (with the WIC’s compliance) caused the loss of about 200 Portuguese ships in two years (1647 and 1648)<sup>67</sup>. The risk reached 40%, but insurance premiums did not exceed 15% which made this period critical, even for those who had known how to gamble with bottomry

<sup>64</sup> Hilton Root, ‘The redistributive role of government: economic regulation in old regime France and England’, *Comparative Studies in Society and History*, 33.2 (1991), pp. 338-369.

<sup>65</sup> John Brewer, *The Sinews of Power...*, p. 171; Tim Keirn, “Monopoly, economic thought, and the Royal African Company” in John Brewer and Susan Staves (eds), *Early Modern Conceptions of Property*, (London- New York 1996), pp. 427-466.

<sup>66</sup> Hilton Root, ‘The redistributive role of government...’, p. 343; p. 355.

<sup>67</sup> Charles Boxer, *The Dutch in Brazil...*, appendix.

loans<sup>68</sup>. Meanwhile, political circles in Portugal saw the peace signed in 1648 as entailing conditions for Philip IV to invade Portugal. Fighting on different fronts, both in the Empire and in the Iberian Peninsula, could challenge the outcome of the revolution begun in 1640. Giving up Brazil was the counterpart of a strategy that sought to focus on the Peninsular War. The ambassador himself recognised that leaving north-eastern Brazil to the Dutch was the only and inevitable course of action. He negotiated a peace treaty with the Estates General on the basis of Portuguese surrender. The treaty was to be ratified in Portugal at the end of 1648.

In Lisbon, the King and a few members of the Treasury Council summoned the merchant-financiers to a meeting where they were informed about the diplomatic solution foreseen in The Hague. It caused the expected consternation. The next step was convincing the merchant-financiers that war in Brazil was no longer a public priority and that the foundation of a company to provide an escort for the sugar fleets and eventually to rescue the colony could be the solution<sup>69</sup>. A few years later, members of the merchant group were honoured with the knighthood of the Order of Christ as a reward for their own efforts in lobbying their peers to accept the royal intention of privatising this war<sup>70</sup>.

A so-called contract between the King and the “body of merchants” formalised the statutes of the *Companhia Geral do Comércio do Brasil*. Some clauses assured the parties that this was a private business and so the right of yielding profits had to be assigned to the enterprise. The monopoly over four main commodities (flour, oil, wine and cod) exported to Brazil responded to this condition. As for the escort, this was thought of as a protection cost for which the state had to transfer to the Company fiscal rights on freight and commodities imported.

<sup>68</sup> Insurance premium referred to in the statutes of the *Companhia Geral do Comércio do Brasil*. The statutes published in José Justino de Andrade e Silva, *Collecção Chronologica da Legislação Portuguesa*, (Lisboa 1855-1856) <http://www.iuslusitaniae.fcsh.unl.pt>: see legislation from 1649.

<sup>69</sup> Leonor Freire Costa, *O Transporte no Atlântico ...*, pp. 505-515.

<sup>70</sup> Fernanda do Olival, *As Ordens Militares e o Estado Moderno. Honra, Mercê e Venalidade em Portugal (1641-1789)*, (Lisbona 2001), p. 297.

The Company's military aims required a fair amount of capital. The enterprise agreed by contract to send two convoys escorted by 18 large vessels at a time when the King's navy consisted of 21 ships. Apart from the vessels, the costs of which are unknown, manning this escort would imply an expenditure of about 410,600,000 réis<sup>71</sup>. The Company's accounting books were burned in the fire that followed the Lisbon earthquake of 1755. Indirect sources reveal that the Company raised 520,000,000 réis of capital in less than one year for its launch (approximately 72% of the total collected in one year in the whole Kingdom, by means of the income tax created to fund the war in the Iberian Peninsula). In spite of the fact that, during its first years, the Company was allowed to lease vessels to the King's navy, the capital for the launch was quickly raised.

In 1653, the third convoy left for Brazil, stopped in Recife and forced the Dutch to surrender. The Anglo-Dutch war created the opportunity. The Estates General could not send any military help. The event required diplomatic recognition which would take a few years more (1661). Meanwhile, the King defended the Company from its opponents in Portugal. To defend the enterprise, he was entitled to write in an official paper in 1654 that:

*"This Company which has done so much harm (so it was claimed), conquered Pernambuco without costing me a penny (vintem,) something that the King of Spain desired so ardently and for which he spent so much without any result and for which I would have given the Dutch nearly six million (cruzado)"*<sup>72</sup>

The Portuguese military success in Brazil was due to an organisational innovation that transferred the state's defensive functions to a corporate business. In the King's own words, the recovery of Brazil became the problem of a group of merchant-financiers whose wealth was rooted in the sugar trade. Given the chance of a peaceful and diplomatic solution, fighting for Brazil was no longer a public issue.

<sup>71</sup> Lisbon Archives, Biblioteca da Ajuda, *Manuscripts*, 51-VI-19, fl. 120.

<sup>72</sup> David Grant Smith, *The Portuguese Mercantile Class of Portugal and ...*, p. 173.

If war could be considered a private affair, the explanation for the relative advantages of states in early modern Europe needs to enquire whether or not private interests were always appropriated as “public” matters. Indeed, chartered companies are impressive examples of this indistinct border-line between public and private spheres. But in the Portuguese case, the means of politicising private interests triggered irrevocable outcomes by enforcing Portuguese monopoly in South Atlantic regions.

## **6. Conclusion**

Linking fiscal and financial modernisation to the shift in the core of the European state-system from the Mediterranean to the north-west Atlantic regions is certainly true in the long term. But diplomatic agreements that enforced political boundaries in colonial areas could also mirror short-term variables in this process.

Military campaigns and their financing also occurred within an institutional framework where the private and public sectors of the economy and society were interwoven. In the early-modern period, public affairs were confined to granting political sovereignty and the state’s power over rival claimants. Public interest, in this sense, meant the monopoly of force and the means to legitimise the state’s potential for extracting income. This paper has discussed how public interest, as defined above, generated contradicting results when tax administration fed the accumulation of capital on the part of moneyed elites, upon which the state depended. It would lead to a point where private organisations had a financial potential for warfare, which the state lacked, enabling them to reap the monopoly on violence.

In the Iberian case, throughout two decades the war forged the context for a narrow social group of merchant-financiers to control state income. They controlled two paramount sources of income: colonial trade and the yield from taxes levied on commodities they themselves transacted. Colonial rivalry widened the chances for this group to exploit the state’s aversion to risk. They over-estimated rates of risk in the economy while they contracted the delivery of lump-sums funded by

taxes they farmed. The diminishing amounts delivered assured the contractors' profits, using to their benefit the uncertainty in maritime sectors caused by war.

Given this context and the tax administration schemes, the Habsburgs' incapacity for military success in Brazil was not a matter of capital scarcity or even a matter of fiscal policy limits that would have impeded access to resources to pay for the war. It was the aim of this paper to demonstrate that the Habsburgs' failure in the conflict was due to an ineffective allocation of resources for colonial warfare. As long as war on any front was conceived as a public issue because of its implication in the political reputation of the monarchy, victory in the colonies was a remote event.

Portuguese independence created a totally different political environment, and shows how the emergence of short-term variables play a big part in the fight for Brazil. The Portuguese monarch had to choose between two war fronts, one considered a public matter, the other delegated to private interests. The defence of the territory in the Iberian Peninsula became the state's priority, while the defence of the colony was thought of as a problem for those who had grown rich with it.

The "privatisation" of war appears to be the efficient Portuguese response that the Habsburgs missed. Privatising war is a departure from the path of political modernisation. Nonetheless, in economic terms, efficiency means the allocation of resources "to the user who has the highest value for them, which is measured by the user's willingness and ability to pay"<sup>73</sup>. This is what King John IV and his councillors envisaged when they lobbied the merchant-financiers to create a company. And this is what Philip IV and the Condé-Duque de Olivares failed to admit was an opening for a monarchy strangled by conflicts on several fronts.

<sup>73</sup> Hilton Root, 'The redistributive role of government...', p. 361.

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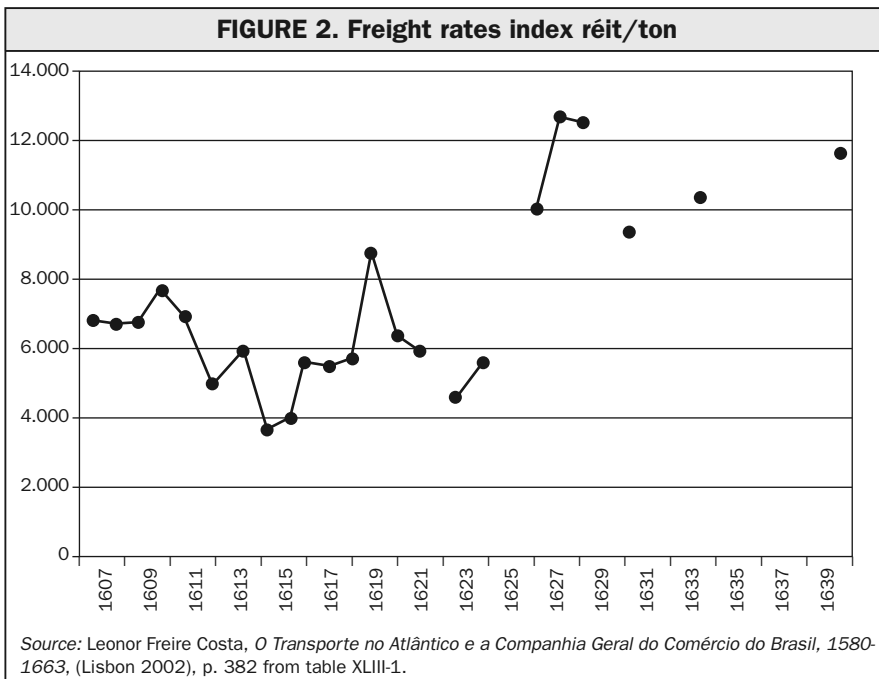
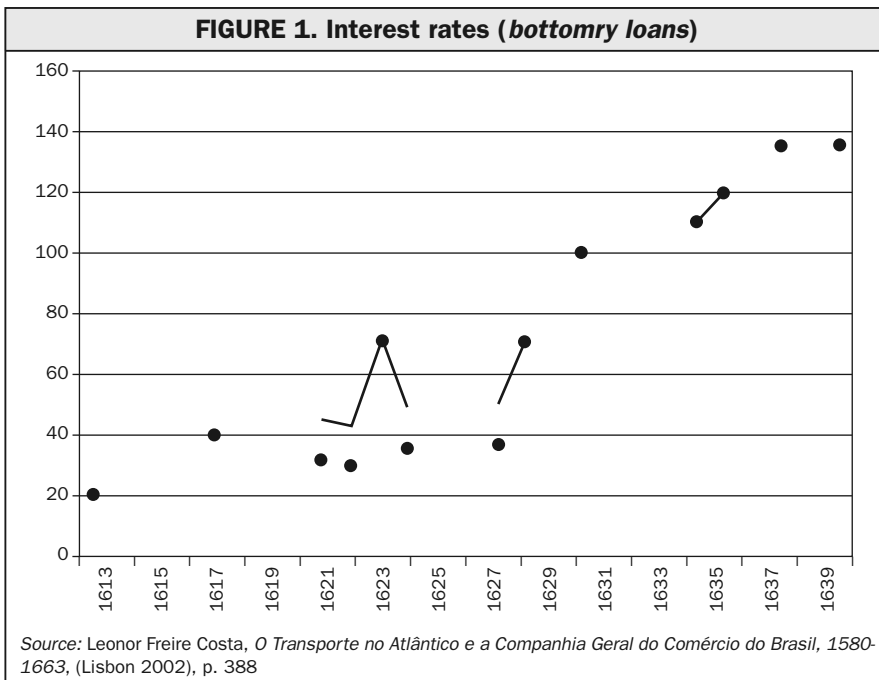
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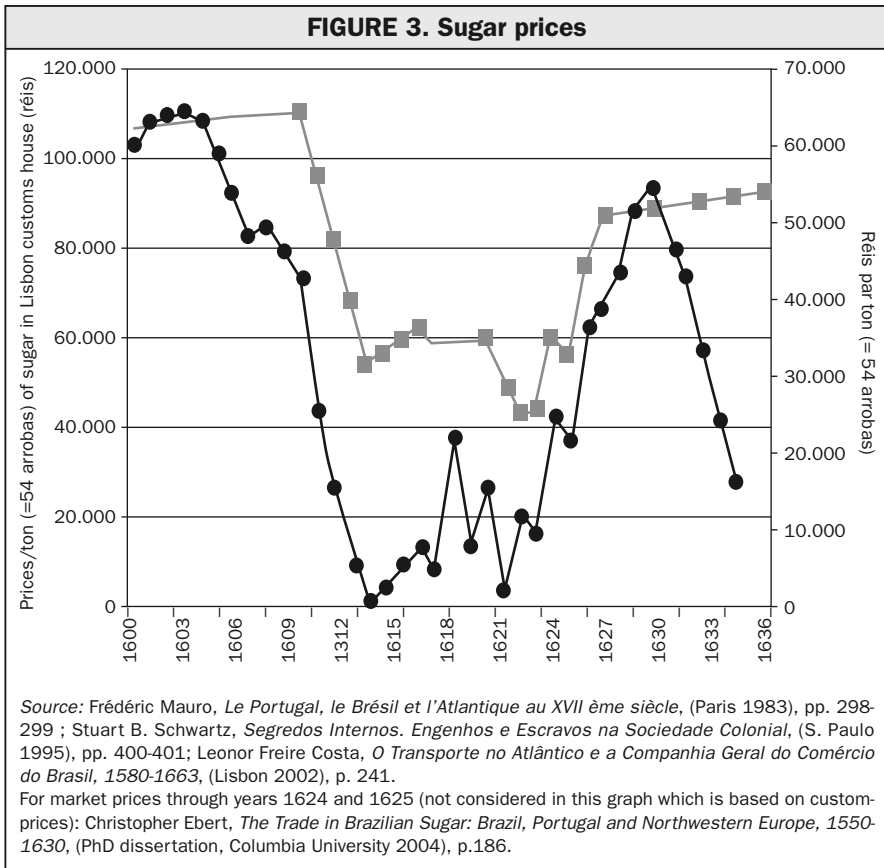
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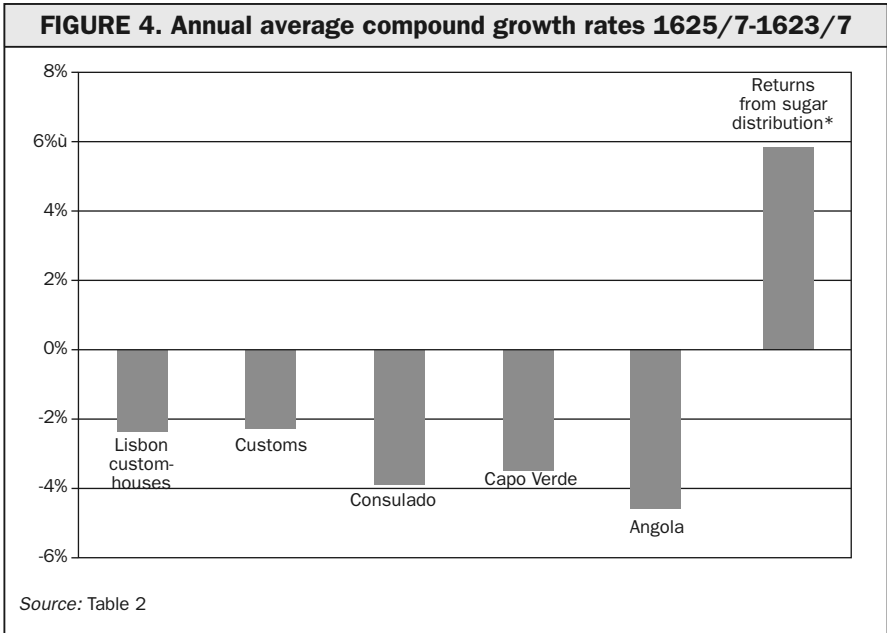
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# *Appendix*

Monopoly or Corporate Business:  
Warfare in Early-Modern Europe







<b>TABLE 1. Capital in Sugar Distribution</b>						
	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>
<b>Years</b>	<b>Estimations of total production (arrobas)</b>	<b>Total freight tonnage</b>	<b>Freight rates per ton (réis)</b>	<b>Gross return in freights (réis)</b>	<b>Price differences Lisbon and Brazil</b>	<b>Gross returns distribution (4+5)</b>
1600	600,000	11,111	10,700	118,888,889	665,566,667	784,455,556
1612	700,000	12,963	8,280	107,333,333	205,100,000	312,433,333
1624	960,000	17,778	10,000	177,777,778	165,600,000	343,377,778
1637/1639	900,000	16,667	18,000	300,000,000	271,800,000	571,800,000
<b>Annual average compound rate of growth</b>						
	<b>1600-1612</b>	<b>1612-1624</b>	<b>1624-1637</b>			
	-7,38%	0,79%	5,83%			
<i>Source: Leonor Freire Costa, O Transporte no Atlântico e a Companhia Geral do Comércio do Brasil, 1580-1663, (Lisbon 2002), apud data from pages: 169; 242; 371; 382.</i>						



<b>TABLE 2. State Revenues (réis) (Items depending upon Atlantic flows)</b>					
<b>Years</b>	<b>Lisbon custom-houses</b>	<b>Custom of the kingdom (general farm)</b>	<b>Consulado</b>	<b>Angola*</b>	<b>Capo Verde*</b>
1588	97,890,351	125,150,000			
1593	86,183,773	170,205,500		11,000,000	
1607	76,100,000	186,500,000	55,000,000	24,000,000	27,000,000
1612	70,000,000	185,367,585	50,000,000	24,000,000	16,000,000
1617			62,965,000	24,000,000	13,500,000
1619	107,900,000	170,000,000	80,000,000	24,000,000	13,500,000
1623			65,000,000	27,000,000	13,500,000
1625	101,144,000	187,230,000		40,000,000	14,700,000
1627	101,143,644	187,292,774	70,000,000	40,000,000	13,400,000
1632	86,000,000	160,000,000	75,000,000	29,000,000	9,400,000
1637			47,000,000	25,000,000	
1640			50,000,000		
Sources for each year:					
1588	National Library, Lisbon, Reservados, cod. 637, f.17. v.º24; A. Hespanha, <i>As Vésperas do Leviathan. Instituições e poder político. Portugal, século XVII</i> , (Lisbon 1994), pp.114 and 154.				
1593	Francisco Carneiro, <i>Relação de todas as rendas deste reino de Portugal</i> , F. Mendes da Luz, (editing and footnoting), (Lisbon 1949).				
1607	Luís Figueiredo falcão, <i>Livro em que se contem toda a fazenda e real património dos reinos de Portugal, Índia e Ilhas adjacentes</i> (source from early 17th century) (first published Lisbon 1859).				
1612	"Receita e despesa dos almoxarifados do reino", Lisbon Archives, Biblioteca da Ajuda, Manuscripts, 51-VI-54, fl. 128-135.				
1617	Lisbon Archives, Arquivo Histórico Ultramarino, Conselho Ultramarino, cod.31, fl. 36v.º.				
1619	Nicolau de Oliveira, <i>Tratado da Grandeza de Lisboa</i> , data provided by V. Magalhães Godinho, "Finanças públicas e estrutura do Estado" in V. Magalhães Godinho, <i>Ensaio II</i> , (Lisbon 1978), pp.31-74.				
1623	Lisbon Archives, Arquivo Histórico Ultramarino, Conselho Ultramarino, cod. 35, fl. 89-89v.º and fl. 126.				
1625	A. Hespanha <i>As Vésperas do Leviathan. Instituições e poder político. Portugal, século XVII</i> , (Lisbon 1994), pp.114 and 154; Lisbon Archives, Arquivo Histórico Ultramarino, Conselho Ultramarino, cod.37, fl.74.				
1627	Lisbon Archives, Arquivo Histórico Ultramarino, Conselho Ultramarino, cod.37, fl.74.				
1632	Archivo Pitoresco, III, p.342-343; 352; "Lisbon custom-houses" in A. Hespanha, <i>As Vésperas do Leviathan. Instituições e poder político. Portugal, século XVII</i> , (Lisbon 1994), p. 156.				
1637	Lisbon Archives, Arquivo Histórico Ultramarino, Conselho Ultramarino, cod.43; fl. 185.				
1640	José Justino de Andrade e SILVA, <i>Collecção Chronologica da Legislação Portuguesa</i> , (Lisbon 1855-1856), available in <a href="http://www.iuslusitaniae.fcsh.unl.pt">http://www.iuslusitaniae.fcsh.unl.pt</a> .				
* Cape Verde and Angola contracts according to Frédéric Mauro, <i>Le Portugal, le Brésil et l'Atlantique au XVII éme siècle</i> , (Paris 1983).					

<b>TABLE 2.1. Annual average compound growth rates</b>			
	<b>1593-1612</b>	<b>1612-1627</b>	<b>1625/27 1632/37</b>
Lisbon	-1,1%	2,5%	-2,3%
Customs	0,5%	0,1%	-2,2%
Consulado*	-1,9%	2,3%	-3,9%
Capo Verde	-9,9%	-1,2%	-2,3%
Angola	4,2%	3,5%	-4,6%
Gross returns from sugar distribution	-7,4%	0,8%	5,8%
* Estimations based on 1607 for the first period.			

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