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UNIVERSITY OF CALIFORNIA

Los Angeles

Managing Hegemonic Decline: Dilemmas of Strategy and Finance

A dissertation submitted in partial satisfaction of the requirements for the degree Doctor
of Philosophy in Political Science

by

Steven E. Lobell

1997

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The dissertation of Steven E. Lobell is approved.


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1997

To Art for showing me the way
and
to Gwen, my family, and Paul
for helping me get there

TABLE OF CONTENTS

LIST OF TABLES	vii
ACKNOWLEDGMENTS	viii
VITA	x
PUBLICATIONS AND PRESENTATIONS	xi
ABSTRACT OF THE DISSERTATION	xii
Chapter	
1. INTRODUCTION	1
Chapter Overview	
Previous Research	
Selection of Cases	
2. DILEMMAS OF STRATEGY AND FINANCE	31
The Dilemma of Balancing Capabilities and Global Commitments	
A Regionally Differentiated Framework of World Politics	
Managing Hegemonic Decline	
Conclusion	
3. THE NEW COURSE IN BRITAIN'S FOREIGN POLICY: DEVOLUTION OF REGIONAL HEGEMONY (1889-1912)	75
The Emerging Contenders for Regional Hegemony: A Regionally Differentiated Framework of World Politics	
Domestic Constraints on Britain's Foreign Policy Adaptability	
Britain: A Declining Liberal Hegemon	
Britain's Response: Managing Hegemonic Decline	

Conclusion	
4. BRITAIN'S FOREIGN POLICY OF ACCOMMODATION (1932-1939)	123
The Emerging Contenders for Regional Leadership	
Britain: Declining Imperial Hegemon	
Domestic Constraints on Britain's Foreign Policy Adaptability	
Britain's Response: Managing Hegemonic Decline	
Conclusion	
5. THE DISSOLUTION OF THE SPANISH MONARCHY: SPAIN'S FOREIGN POLICY OF RESOURCE EXTRACTION	167
The Emerging Challengers for Regional Leadership	
Spain: Declining Imperial Hegemon	
Domestically Unconstrained: Royal Absolutism	
Spain's Response: Managing Hegemonic Decline	
Conclusion	
6. CONCLUSION: PAX AMERICANA OR THE END OF THE AMERICAN CENTURY?	216
Summary	
Success and Failure: Managing Decline	
Regional versus Global Hegemony: Rise and Decline of the United States	
The United States and the Soviet Union during the Cold War: "Different Strokes for Different Folks"	
Coming Decades	
APPENDIX	251

BIBLIOGRAPHY 254

LIST OF TABLES

Table

1. Case Studies	27
2. Outcomes	63
3. Union of Arms	193

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PUBLICATIONS AND PRESENTATIONS

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ABSTRACT OF THE DISSERTATION

Managing Hegemonic Decline:
Dilemmas of Strategy and Finance

by

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The grand strategy of a declining hegemon is to remain in the ranks of the great powers as long as possible. As a great power, the erstwhile hegemon can continue to shape the rules of the game in order to safeguard its existing security and commercial interests. Encountering different emerging contenders for regional hegemony in disparate parts of its formal and/or informal empire, the dilemma for the declining hegemon is to restore the balance between its military capability and global commitments while protecting its fiscal strength and its national security. A security strategy which favors either fiscal or security interests over the other will accelerate the hegemon's decline from the great power ranks.

While scholars tend to focus on geostrategic and domestic constraints on foreign policy adaptability, I argue that a hegemon's foreign commercial policy will shape and

constrain its range of security options for restoring the balance. In particular, ranging from liberal to imperial, the nature of a hegemon's foreign commercial policy will include or exclude certain security strategies among its range of foreign policy options.

How a hegemon manages its decline will affect how long it can remain in the ranks of the great powers. At issue is the hegemon's rate of decline. In the short run, both liberal and imperial hegemonies can select from alternative security strategies which can either accelerate or slow their rate of descent. However, in the long run, due to differences in the nature of the foreign commercial policies, a liberal hegemon can select a security strategy which will ensure that it remains a key player in the great power game longer than if it was an imperial hegemon. The rationale is that a liberal hegemon can select a security strategy which will safeguard both its economic strength and its national security, slowing its rate of decline. For an imperial hegemon, it can only select from a range of security strategies that either will erode its economic staying power or undermine its national security interests, accelerating its fall from the ranks of the great powers relative to a liberal hegemon.

CHAPTER 1

INTRODUCTION

The goal of a declining hegemon's grand strategy involves remaining a key player in the great power game as long as possible. Since hierarchy among states in the international system connotes different degrees of influence, in at least remaining in the ranks of the great powers, the declining hegemon can continue to shape the rules of the game in order to protect its existing security and commercial interests. Confronted with different encroaching contenders for regional hegemony in disparate parts of its formal and informal empire, the declining hegemon faces the dilemma of how to restore the balance between its military capability and global commitments without undermining its fiscal strength or eroding its national security interests.¹ In selecting a security strategy which favors either fiscal or security concerns over the other, the hegemon risks accelerating its fall from the ranks of the great powers to a second rate power. Ranging from liberal to imperial, a hegemon's foreign commercial policy will shape and constrain its range of alternative security strategies for managing decline. In the short run, both liberal and imperial hegemon can select from alternative security strategies which will accelerate or decelerate their rate of decline. However, in the long run, while decline is inevitable, only a liberal hegemon can select a security strategy which will safeguard both

¹ Harold and Margaret Sprout termed this condition the "dilemma of rising demands and insufficient resources" (1963, 1968).

its political economy and its national security interests, thus keeping that state in the ranks of the great powers longer than as an imperial hegemon.

In the United States there is currently a debate among scholars and policy-makers on how to narrow the growing gap between America's military capabilities and its global commitments (simply compare the contradictory goals of the Pentagon's 1992 Defense Planning Guidance for 1994-99 and Under-Secretary of State Peter Tarnoffs' 1993 statement on U.S. global leadership; *New York Times*, 8 March 1992; *New York Times*, 4 June 1993).² However, the dilemma that the United States faces in the coming decades in restoring this balance is neither unique nor unprecedented. Previous hegemonies such as Greece, Rome, Venice, the Arab Caliphate, the Dutch Empire, Spain, the Ottoman Empire, the Manchu Dynasty, Britain, and the Soviet Union faced a similar predicament. In particular, Spain during the Thirty Years' War, and Britain in the decades prior to World War I, and prior to World War II, faced emerging contenders for regional leadership on disparate fronts and in different parts of their empire. Like the United States, these declining hegemonies had a number of alternative foreign policy options for restoring the balance between their military (and economic) capabilities and global commitments. Facing similar international pressures (and in the British cases similar domestic pressures as well), this dissertation examines how American, Spanish, and British decision-makers managed their decline and why they selected different security strategies (not why these hegemonies declined, which has been discussed in great detail elsewhere, nor how to escape from decline).³ In particular, I examine periods in which

² The lack of consensus over the direction of American foreign policy is reflected in three related debates: (1) whether the United States should reduce, maintain, or expand its commitments in Europe (NATO), and/or Asia, (2) whether the Third World or the periphery "matters" for American security, and (3) when the United States should intervene in local conflicts.

³ See the articles in Cipolla (1970); also see Gilpin (1981); Olson (1982).

the distribution of power shifts from hegemonic to multipolar in order to answer, how and based on what factors do declining hegemons rank or prioritize their global commitments and strategic interests?; how do statesmen in a declining hegemon identify whether an emerging contender for regional hegemony is a potential ally (and acceptable regional successor) or a future adversary?; why do some power shifts due to differential rates of growth among rising and declining states result in preventive/preemptive war and others do not?; and finally, how do declining hegemons reconcile between the dangers associated with excessive and prolonged defense spending and the need to protect their global interests from preemptive attacks (i.e., to maximize economic growth or current military strength)?

One shortcoming in the existing literature on hegemonic decline is that scholars tend to over-simplify the hegemon's dilemma in balancing capabilities and interests by examining the hegemon's position in a single region or time period. This "globalist" framework is based on the assumption that there are only two major states in the international system, the declining hegemon and the rising challenger (for more detail, see below). However, in most cases, had the declining hegemon confronted only a single emerging contender, it could have concentrated its resources from different parts of its empire, overwhelming the challenger's. Instead, I develop a regionally differentiated framework of world politics which maintains that the declining hegemon is likely to confront different emerging contenders for regional hegemony, rising at different rates, and challenging the hegemon's leadership in disparate parts of its empire. The more extensive its empire, the greater the number of rising contenders it is likely to confront. In over-simplifying the hegemon's predicament, as the globalists do, it is difficult to understand the dilemma that the hegemon faces in restoring the balance between its capabilities and commitments.

When shifts from a hegemonic to a multipolar distribution of power occur, the dilemma for a declining hegemon is how to restore the balance between its capabilities and global commitments while safeguarding its fiscal strength and its national security interests. A security strategy which favors either financial or security interests over the other will accelerate the hegemon's fall from the ranks of the great powers. In particular, the dilemma for the declining hegemon in restoring this balance is three-fold. First, a security strategy that involves prolonged increases in the rate of peacetime defense spending in order to keep pace with the combined military buildup of several rising contenders (and to prepare for preventive wars if necessary) will divert resources from domestic investment, limit the scope of future economic growth, and ultimately weaken the productive strength of the declining state to construct a modern military. As well, sustained military spending in excess of available resources will drain the financial reserves that the declining power will need to extract in the event of protracted war. Second, a security strategy that maintains the hegemon's global commitments without increasing its rate of defense spending risks leaving it vulnerable to preemptive attacks by encroaching contenders. A disequilibrium between the hegemon's military capability and its global commitments might tempt rising states to challenge the declining state's regional leadership. Finally, a security strategy that involves abandoning its empire in order to lower the costs of hegemony means that the hegemon risks strengthening the war-making capacity of a rising revisionist challenger since the latter might capture the economic and military assets in the locale, eroding the declining state's national security objectives. Thus, in managing its decline, the hegemon must consider both the fiscal and security implications of its security strategy.

The failure of a declining hegemon to recognize the dilemma of balancing capabilities and commitments can be fatal. For instance, Spain under Philip IV,

Napoleonic France, and the Soviet Union restored the balance between capabilities and commitments by increasing their military capability. In particular, they increased their rate of resource extraction in order to prepare and fight preventive wars against several emerging contenders for regional hegemony simultaneously.⁴ However, excessive and sustained increases in the rate of military spending exhausted Spain, France, and the Soviet Union's economic base of power (capital and labor), and ultimately their ability to construct and maintain a modern military force (Spain declared bankruptcy in 1647; France's downfall was even more rapid than its rise; and the Soviet Union imploded). Rome also failed to heed the dilemma of balancing capabilities and commitments. Facing emerging challengers on different fronts, Rome appeased the Visigoths in 382 in order to lower the costs of hegemony. In particular, Rome allowed the Visigoths to settle as allies in northern Thrace along the Danube. However, the Visigoths proved to be revisionist challengers (using the settlement to strengthen their position without the fear of a preventive strike from Rome), and from 406 to 410, swept through the Balkans, Gaul, and Spain, finally sacking Rome in 410 (Ferrill 1986; Luttwak 1976). The United States' experience proves no exception to this dilemma. The Pentagon's 1992 Defense Planning Guidance for 1994-99 calls on the United States to "convince potential competitors that they need not aspire to a greater role or pursue a more aggressive posture to protect their legitimate interests." However, in discouraging Japan and/or a United Europe from playing a greater role in bearing the burden of regional hegemony, the United States risks undermining its economic staying power by sustained military spending.

⁴ On France, see Kaiser (1990); Dehio (1962). On Spain, see Chapter 5, on the Soviet Union, see Chapter 6.

What factors affect how a hegemon manages its decline? Scholars tend to focus on geostrategic concerns or domestic constraints (economic or political) on foreign policy flexibility in order to explain how a declining hegemon restores the balance between its capabilities and commitments (see literature review below). I argue that a hegemon's foreign commercial policy will shape and constrain its range of security strategies for managing decline.⁵ A hegemon's foreign economic policy (as opposed to its domestic trade policy) can range from liberal to imperial and reflects whether the hegemon will impose an open door or closed door trade policy on its overseas formal and/or informal empire and any regions it comes to dominate. The nature of a liberal or imperial hegemon's international commercial policy will include or exclude certain security strategies among its foreign policy alternatives, affecting its range of security strategies for restoring the balance. Thus, liberal and imperial hegemons will select from a different array of foreign policy strategies.

How a hegemon manages its decline matters; which strategy a hegemon selects to restore the balance can accelerate or decelerate its rate of decline from the ranks of the great powers. At issue is the hegemon's rate of decline, affecting how long it can remain a key player in the great power game. A declining hegemon's grand strategy is to remain in the great power ranks as long as possible. As a great power, the former hegemon can continue to advance an international system which favors its existing security and commercial interests. In falling from the ranks of the great power to a second tier power, the hegemon's influence will also decline. As a second-rate state, the erstwhile hegemon

⁵ For the political economy literature, foreign commercial policy is the dependent variable, and scholars focus on the role of domestic interest groups, sectoral politics, relative abundance, and relative size to explain why states select liberal or protectionist policies. I use foreign commercial policy as an independent variable to explain how states manage their decline.

will have limited influence over the rules of the game, relying on the remaining great powers to protect its national interests.

In the short run, declining hegemonies have a strategic choice.⁶ Both liberal and imperial hegemonies can select security strategies which will accelerate or decelerate their rate of decline from the great power club. The goal of the declining hegemon is to select the security strategy which will decelerate its rate of decline over its alternative options. A security strategy which accelerates its decline (over an alternative option), is a suboptimal choice. However, in the long run, due to differences in the nature of their foreign commercial policies, a liberal hegemon can select a security strategy which will ensure that it can remain a player in the great power game longer than if it were an imperial hegemon.⁷ The rationale is that a foreign policy that favors either economic or security concerns to the exclusion of the other will hasten the hegemon's fall from the ranks of the great powers. Only a liberal hegemon can select a foreign policy strategy that will safeguard both its economic strength and its national security objectives; consequently, only a liberal hegemon can remain in the ranks of the great powers the longest.⁸ For an imperial hegemon, even though it is often aware of the dangers of its foreign policy options, it can only select from a range of security strategies that will erode its economic staying power or undermine its national security interests, accelerating its

⁶ On strategic choice, see Stein (1990).

⁷ In the long term, hegemonies also have strategic choice. A hegemon can select an imperial or liberal commercial policy, which will affect its range of security strategies. In this dissertation, I focus on factors which affect why a hegemon selects one security strategy over another, not why a hegemon selects one foreign commercial policy over another. The rationale is that I am interested in explaining the effect that the choice of an international commercial policy has on the hegemon's foreign policy. For this reason, a hegemon's foreign commercial policy is treated as exogenous.

⁸ This involves selecting the security strategy which will allow the declining hegemon to remain in the ranks of the great powers longer than its alternative options and selecting the foreign commercial policy which will ensure that it remains in the ranks of the great powers longer than its alternative commercial policy. In doing so, the hegemon will remain in the ranks of the great powers as long as possible for that hegemon.

fall from the ranks of the great powers to a second tier power in relation to a liberal hegemon. However, this requires that the liberal hegemon select its optimal security strategy. An imperial hegemon which selects its optimal security strategy can remain in the ranks of the great powers as long as if it was a liberal hegemon which selects a suboptimal strategy.

Chapter Overview

The remaining part of Chapter 1 examines three competing perspectives on hegemonic decline. These approaches vary in terms of whether and why imbalances occur between capabilities and commitments, and how a declining hegemon will respond to this imbalance. For realists, managing decline is not an issue since a declining hegemon will always maintain a balance between its capabilities and global commitments. Operating in a frictionless environment, the declining hegemon will increase its rate of resource extraction or reduce its commitments as necessary. For globalists, managing decline is also not an issue since a hegemon's decline will occur rapidly, globally, and simultaneously. The rationale is that differential rates of growth will result in a major war between the rising and declining states, concluding in the hegemon's complete loss of global leadership to the emerging challenger. Finally, domestic politics arguments maintain that domestic constraints will result in an imbalance between the hegemon's capabilities and commitments. These scholars conclude that only a domestically unconstrained hegemon can manage its decline.

Chapter 2 discusses the effect of a hegemon's foreign commercial policy on how it restores the balance between capabilities and commitments, and how long it can remain in the ranks of the great powers. To be clear, I examine the effect that a hegemon's foreign commercial policy has on how it manages its decline. I do not focus on why a

hegemon selects one foreign commercial policy over another, but on the impact that this choice has on its foreign policy. Consequently, in my explanation, a hegemon's foreign commercial policy is treated as exogenous.

The first section of Chapter 2 develops a regionally differentiated framework of world politics. In contrast to the globalist approach, I argue that the international system is not a single unit, but composed of multiple regions or spheres of formal and informal influence.⁹ Based on this framework, a hegemon will decline at different rates in disparate parts of its formal and informal empire and is likely to confront different rising contenders for regional leadership in these locales. The consequence of this regional framework is that the hegemon's loss of leadership over one locale rarely translates into a global loss of leadership to an emerging contender, implying that the hegemon's rate of decline from the ranks of the great powers can occur gradually and smoothly over time. The challenge for the hegemon is to restore the balance between its capabilities and commitments without undermining its fiscal strength or eroding its national security interests.

The second section develops a number of hypotheses on how hegemons will manage their decline. Declining from undisputed leader over the locale to confronting emerging competitors for regional leadership, the hegemon has three alternative foreign policy strategies for restoring the balance between its capabilities and global commitments. These strategies are, increase resource extraction for defense spending through borrowing, taxation, burden-sharing and/or state-led industrial growth; devolve of regional leadership to a rising supporter or a local surrogate power; reach accommodation with some or all of the rising states. These strategies entail either

⁹ I define a hegemon as a state which simultaneously dominates several regions of the globe.

increasing its military capability or reducing the cost the political, economic, and military costs associated with regional hegemony.

The final section discusses the effect that a hegemon's foreign commercial policy can have on how it restores the balance and how long it can remain in the ranks of the great powers. First, a hegemon's foreign commercial policy will shape and constrain its range of security strategies for managing decline. The nature of an imperial hegemon's foreign commercial policy will restrict its range of security strategies to either a policy of extraction or accommodation (depending on its domestic flexibility), while a liberal hegemon's foreign commercial policy will include the option of devolution (and either accommodation or extraction depending on its domestic flexibility). Second, in the long run, a hegemon's foreign commercial policy will affect how long it can remain in the ranks of the great powers. In managing its decline, a hegemon must consider both the fiscal and security implications of how it restores the balance between its capabilities and its commitments. Favoring either fiscal strength or national security interests will accelerate the hegemon's fall from the ranks of the great powers. For an imperial hegemon, it can only select from a range of security strategies which will either undermine its fiscal strength or erode its national security, accelerating its rate of decline into the ranks of the second-tier states. In contrast, a liberal hegemon can select a security strategy which will safeguard both its fiscal strength and its national security, slowing its rate of decline and allowing it to remain in the ranks of the great powers longer than if it was an imperial hegemon.

Chapters 4, 5, and 6, examine three case studies of hegemonic decline. Chapter 3 examines Britain in the three decades prior to World War I (1889-1912). By the turn of the century, Britain faced an emerging United States, Germany, Russia, France, and Japan in disparate parts of its formal and informal empire, including the Far East, Central

Asia, the Americas, and Britain's homewaters. Domestically constrained liberal Britain restored the balance between its capabilities and commitments by devolving regional hegemony in order to lower the costs of hegemony. In devolving leadership over the Americas to a rising United States, ceding leadership over the northeast Pacific to an emerging Japan, and the Eastern Mediterranean to France, Britain was able to protect its remaining commitments in Central Asia and its homewaters without eroding its fiscal strength or undermining its national security. In the long run, Britain was able to manage its decline, remaining a player in the great power game.

Chapter 4 examines Britain in the inter-war period (1932-1939). During the 1930s, Britain confronted a rising Germany on the Continent, an emerging Italy in the Mediterranean, and a rising Japan in the Far East. As a domestically constrained imperial hegemon, Britain restored the balance between its capabilities and commitments by reaching an accommodation with each of the emerging challengers in order to lower the costs of leadership to a level that it could afford. However, in the long run, in accommodating several rising imperial challengers, Britain undermined its national security, contributing to its fall from the ranks of the great powers.

Chapter 5 examines Spain during the reign of Philip IV and his count-duce, Olivares (1621-1648). Spain confronted a rising France, England, and the United Provinces (Netherlands), in different parts of its empire including the Spanish Netherlands, the Americas, Africa, Asia, Italy, and northern Germany, as well as assaults by the Turks. Domestically unconstrained imperial Spain restored the balance between its capabilities and commitments by increasing its rate of societal resource extraction in order to augment its military capability. However, in the long run, excessive and prolonged military spending undermined Spain's (Castile's) fiscal strength and ultimately its military power, contributing to its fall from the rankings of the great powers.

Chapter 6 examines the United States and the Soviet Union during the Cold War and the implications for the United States in the coming decades. During the Cold War, the United States and the Soviet Union faced different emerging contenders on disparate fronts, including each other. In encountering a similar international environment, why did Soviet and American leaders select different security strategies to restore the balance? Ironically, while the Soviet Union collapsed, I maintain that the Soviet Union was more successful in managing its decline than the United States. The rationale is that the Soviet Union chose its best alternative security strategy, ensuring that it remained in the ranks of the great powers longer than any of its alternative security options (however, in the long run, this strategy of extraction eroded its economic strength and ultimately its ability to finance a modern military). In contrast, the United States selected a sub-optimal security strategy that accelerated its rate of decline in relation to its alternative options. Part of this discussion examines how the United States prioritized its global commitments and asks why during the Cold War, the United States built up Germany and Japan, accelerating their rate of ascent (in contrast to the tenets of realism), but was unwilling to devolve regional hegemony to these contenders in order to lower the costs of hegemony and restore the balance. Finally, I conclude with a discussion of the lessons for the United States in the coming decades and the importance of resisting domestic calls to adopt a protectionist or imperial foreign commercial policy.

Previous Research

This section examines three arguments which address the issue of managing hegemonic decline. I have framed these arguments in the context of hegemonic decline and have culled from them how each approach suggests that the hegemon will correct imbalances between its military capabilities and global commitments. These perspectives

are distinguished by their emphasis on regionalism or globalism, the influence of domestic and international constraints on foreign policy adaptability, and the ability of a hegemon to manage its decline.

Realism

For realists, managing decline is not an issue since a declining hegemon will always maintain a balance between its military capabilities and global commitments. Based on the assumption that the hegemon is a unitary actor (i.e., free from domestic economic and political constraints) and that the state is the central actor in world politics, realists argue that neither domestic politics nor international institutions will restrict or constrain the hegemon from restoring the balance. As a rational actor, realists assume that the declining hegemon will restore the balance between its capabilities and commitments by selecting a strategy that maximizes its national security interests and objectives, no matter what the economic cost. Consequently, operating in a frictionless environment, the hegemon can increase its rate of resource extraction for military spending in preparation for a preventive war or reduce its global commitments as necessary.¹⁰

In reducing its global commitments, realists argue that a declining power will differentiate across regions, standing firm in regions of strategic value and retrenching in regions of lesser strategic worth. The declining hegemon will prioritize its commitments based on which regions contain the most important assets and will identify which rising contenders are the most threatening based on the relative power of the emerging states. A region is considered valuable if its loss will shift the global balance of power to the rising

¹⁰ According to Waltz (1979) states will balance through internal means in a bipolar world and external means in a multipolar world.

state. Consequently, according to realists, the declining hegemon should retain the bulk of its global commitments, trimming them only in the periphery. The underlying assumptions are two-fold. First, the declining hegemon should stand firm in strategic locales because the loss of a vital region could tip the global balance against the declining hegemon. In fact, the declining hegemon should stand firm in the locale even if the emerging contender is an ally. The rationale is that since today's ally might be tomorrow's enemy, the hegemon must discourage the rising state(s) from developing its own defense capabilities or seeking regional hegemony. Second, the declining hegemon should retrench in the periphery since losses (by the hegemon) or gains (by rising challengers) in the Third World will not upset the global balance of power. Thus, according to realism, the declining hegemon will trim its global obligations by retreating only from less valuable locales in the periphery, never from strategic regions in the center.

For instance, writing shortly after World War II and in response to an emerging Soviet Union, George Kennan (1951) and Walter Lippmann (1943) argued that not all regions of the world were equally vital to American security. According to Kennan, only five centers of industrial and military power in the world were vital to American national security (the United States, Great Britain, Germany and central Europe, the Soviet Union, and Japan). Since only one region was in hostile hands, Kennan's policy of selective containment was intended to ensure that none of the other regions fell into Soviet control. The rationale was that only by conquering some or all of these vital power centers could the Soviet Union (or any other emerging counter, including America's allies) tip the balance of power in its favor. In contrast, Kennan objected to the notion that the United States had to resist communism wherever it appeared (i.e., a strategy of global containment). He argued that there was no need to contain the Soviets in the Third World

since even substantial Soviet conquest would have little impact on the global balance of power. Instead, the Third World offered little strategic value for the great powers and diverted scarce national resources from the main theaters of operation.

Stephen Walt (1989) and Stephen Van Evera (1989) contend that American vital interests have not substantially changed over the last five decades. The only addition to the list of strategic regions is preserving Western access to oil in the Persian Gulf. According to Walt's calculation, Western Europe is the largest "prize," producing roughly 22 percent of the gross world product, and the Far East the second largest, producing 12.5 percent. The entire Third World produces less than 20 percent of gross world product, scattered over more than 100 countries; all of Africa has an aggregate GNP lower than Britain (Walt 1989, 18). Samuel Huntington (1991) adds that even in the post-cold war era, the United States can not allow any single state to dominate either Europe or Asia, since this would tip the balance of power against the United States. He argues that the threat of the Soviet Union merely masked the conflicting interests among western democratic states. Consequently, to ensure no single state dominates the Eurasian landmass, Huntington recommends that the United States limit German power in the new Europe, restrain Japan by continuing the U.S.-Japanese military alliance, maintain its military posture in East Asia, and secure the Persian Gulf and Central American regions (1991, 13).

Globalism

For globalists, managing decline is also not an issue.¹¹ However, in contrast to realists, globalists treat a hegemon's decline as an undifferentiated event. Either as a

¹¹ I have clustered power transition theory, hegemonic transition, long cycle theory, under the general rubric of globalism. Long cycle theory accounts for the regular cycles of global stability and hegemonic war, with each cycle lasting roughly 100 years. Since 1500, there have been 5 such cycles of

result of peaceful transition or more likely hegemonic war, this approach maintains that a hegemon's decline (and its rise) will occur globally, rapidly, and simultaneously across its formal and/or informal empire.¹² The outcome is that the declining hegemon will lose global leadership to the rising contender in a single instance (again, peacefully or as a result of hegemonic war).

According to the globalist argument, a hegemon will structure the international system to advance its own interests (and as a by-product, the presence of a single dominant actor will promote international stability because it will establish and enforce a set of norms and rules which govern the international system). However, the benefits of hegemony attract competitors for global leadership. For Organski (1968) and Kugler (1980) the challenger comes from the ranks of the rapidly industrializing states which are powerful yet dissatisfied with the current system. For Modelski (1987) and Thompson (1980), the challenger is a territorial state.¹³ In both instances, since a contender is likely to restructure the international order to benefit its own interests, often to the detriment of the hegemon's interests, the declining state rarely peacefully relinquishes hegemony.

For globalists, differential rates of growth (rapid industrialization, demographic growth) allow a rising state to encroach on the hegemon's leadership position.¹⁴

stability and conflict. As part of the long cycle model, Modelski and Thompson (1988) contend that historically the hegemonic state has held a superiority in sea power, and more recently air and space (the hegemonic leaders have been Portugal, the Netherlands, Britain for two cycles, and the United States). The rationale is that leadership requires global reach in order to manage the international system and to protect long distance trade. In the past this could only be achieved through sea power.

¹² Organski (1968, 1980) contends that a declining hegemon can respond in several ways to an emerging challenger. These include appeasing a challenger and delaying a challengers industrialization. However, according to Organski the most common outcome is a hegemonic war between the rising and declining states.

¹³ For long cycle theorists, the challenger comes from the ranks of the territorial states. Also, see Doran and Parsons (1980).

¹⁴ Gilpin (1981) and Kennedy (1987) strengthen Organski's original model by explaining why a hegemon cannot indefinitely sustain its hegemonic position.

According to Gilpin (1981) and Kennedy (1987), although the hegemon reaps the benefits from its dominant position, domestic and international costs will contribute to the hegemon's relative decline. Internally, the rising cost of military technology and its diffusion, the growth in the demand for consumption goods and government spending within the hegemon, and the rise in the service sector contribute to a slow down in the hegemon's relative economic growth and industrial development. Externally, the hegemon single-handedly bears the high cost of providing the public goods of an open international system and freedom of the seas. However, in the long term, prolonged and excessive military spending will divert resources from "wealth creating" domestic investment, eroding the hegemon's productive strength and ultimately its ability to finance a modern military. In contrast, the emerging challenger has few global commitments and lower defense burdens, allowing it to allocate a much larger share of its wealth towards domestic investment and economic growth.¹⁵ As the rising state encroaches, there is additional pressure for the hegemon to defend its global commitments, forcing it to extract additional resources, accelerating its relative decline.

According to Gilpin (1981), the international system will remain stable as long as no emerging state believes that the benefits of challenging the hegemon and changing the system's structure exceed the costs of doing so. However, from the perspective of an emerging challenger, as the hegemon declines in relative power, so does the cost of challenging the leader for the hegemonic position. As differential rates of growth narrow the gap between the rising and declining power, the rising contender will launch a

¹⁵ For instance, in 1905, in a report on The Defense of Canada, it was noted that in comparison to Britain, an emerging United States had few global burdens, allowing it to concentrate its forces on defense of the homeland. The report states that "If we accept the Philippines and Cuba (the loss of either of which she would scarcely feel), she [the U.S.] has not distant possessions to be defended. This happy lack of external causes for preoccupation has enabled the United States to concentrate her warships upon her own shores, where (in war time) they would find their proper occupation in defending the shores of the Mother Land" (PRO, ADM 1/7807).

preemptive strike against the dominant power, fearing that the hegemon will attack (i.e., preventive war) and push it down the power trajectory.¹⁶ For Gilpin, hegemonic war brings the international system into balance with the actual distribution of power, since the most powerful state is once again the leader of the international order. Consequently, for globalists, a hegemon cannot manage its decline. The rationale is two-fold. First, the hegemon's defeat entails the complete transfer of global leadership to the victorious challenger. Second, the hegemon's loss of global leadership will occur rapidly, not over time or in territorial pieces. Thus, for globalists, the hegemon's fall from world leader to a second-rate regional power will occur globally and rapidly, leaving it little room to manage or affect its rate of decline.

Domestic Constraints

Finally, domestic politics arguments suggest that domestic political and economic constraints can prevent a hegemon from managing its decline.¹⁷ In particular, domestic politics will prevent the declining hegemon from either increasing its rate of societal resources extraction for defense spending or reducing its global commitments in order to restore the balance between capabilities and commitments. Domestic constraints include regime type, state-society relations, and entrenched interest groups, institutions, and

¹⁶ Kim and Morrow (1992) maintain that a risk averse challenger will strike prior to the power transition while a risk acceptant challenger will wait. Like power transition theory, long cycle theory posits that global leadership will be transferred from the declining state to a rising state. Yet, a crucial difference between the two models is the question of succession. According to Modelski and Thompson, the declining naval power will peacefully transfer leadership over the international system to a rising maritime power (the Netherlands transferred leadership to Britain, Britain transferred leadership to the United States). Goldstein (1988) offers a slight twist to the long cycle argument. He holds that more severe wars are likely to occur during the upswing phase of the long cycle instead of during the phase of hegemonic decline. His rationale is that economic expansion triggers competition among the great powers for scarce resources and war becomes one means to secure them. A final point, there is no reason that the declining hegemon cannot capitalize on its dominant position to launch a preventive strike against any rising challenger before it poses a threat

¹⁷ On domestic political constraints resulting in a state of underextension, see Stein (1993).

images of leaders. These scholars suggest that only a domestically unconstrained hegemon can manage its decline.

Domestic politics arguments highlight at least three broad domestic constraints on a declining hegemon's ability to restore the balance between capabilities and commitments. First a declining hegemon's regime type can affect its foreign policy adaptability. Richard Haas (1988), Celeste Wallander (1992), and David Lake (1992) differ on whether authoritarian regimes or democratic states are more domestically constrained in their ability to extract societal resources. Haass and Wallander suggest that a declining authoritarian regime can extract more societal resources in order to increase its military spending than a democratic state. Their rationale is that authoritarian regimes lack organized opposition (or the opposition has been reduced to total submission) and have weak institutional structures. Consequently, authoritarian states can often "pursue policies abroad for prolonged periods at the expense of the domestic society and the economy alike (Haass 1988, 415)" In contrast, David Lake argues that democratic states can extract more domestic resources than authoritarian regimes.¹⁸ Lake's rationale is three-fold. First, he argues that democracies possess greater national wealth. Second, Lake argues that greater societal support will allow a democracy to extract a larger relative share of resources for any given level of national wealth than an authoritarian regime. Finally, Lake argues that in a conflict with an autocracy, the possibility of the state's defeat allows democratic leaders to extract greater levels of

¹⁸ One possible solution to this debate on whether democracies or autocracies can extract greater resources is to distinguish between a state's extractive capacity and its allocative capacity. For an authoritarian regime, the lack of legitimacy will increase society's opposition, constraining the state's ability to extract societal resources. However, the absence of access to the political process will mean that state leaders will face little opposition in allocating a higher percentage of collected revenue to military spending. For a democracy, greater legitimacy and the threat of conquest by an authoritarian regime will allow state leaders to extract higher levels of domestic resources. However, access to the political process will mean that domestic opposition can block any attempt to increase the allocation of revenue to military spending.

resources. Thus, a declining hegemon's regime type can affect its ability to increase its rate of military spending.

Second domestic politics arguments suggest that state-society relations can restrict a declining hegemon from increasing its rate of resource extraction for military spending in order to restore the balance between capabilities and commitments. According to Michael Barnett (1992) and Jack Levy (1991), whether a state can extract additional societal resources is a product of the state's capacity to penetrate society and the regime's domestic legitimacy. For Barnett, states that are viewed as legitimate by their societies and/or which are relatively autonomous from dominant societal actors will be able to increase the rate of resource extraction for defense spending. Legitimacy is derived from societal participation in governance, suggesting that a democracy will be able to extract greater societal resources. In terms of autonomy, states with access to alternative sources of financial means can increase defense spending without the support of society. Alternative financial resources include state-run industry, foreign loans, and exogenous sources of wealth, such as the Spanish King's right to a share of the gold discovered in the New World (or more recently, oil).¹⁹ The higher the political cost of extracting societal resources, the more the state is constrained by society, and the more likely state leaders will pursue an alternative strategy to acquire resources.

Third, domestic politics arguments maintain that entrenched interest groups, domestic institutions, and the ideas and beliefs of state leaders can restrict a declining hegemon's foreign policy adaptability. My revision of Jack Snyder's (1991) framework for over-expansion suggests that vested interest groups can delay or prevent a declining power from reducing its global commitments. Jack Snyder's model is based on an

¹⁹ For instance, rentier states such as some of the oil producing states in the Middle East.

advanced version of the interest group model.²⁰ By forming a coalition, parochial interest groups with an interest in retaining the empire can pool their resources to muster societal support for their policies. Parochial groups can do so by appealing to society through strategic "myths" of security through retention of the empire. The combination of log-rolling among parochial groups with a vested interests in retaining the empire and strategic myths which have become accepted standards by the wider population (see Kupchan below), will make it increasingly difficult (and politically costly) for leaders to retrench from parts of the empire. One implication of this argument is that there is an incentive for pressure groups with regional interests to become entrenched in the political process of a hegemon while the state is expanding in order to influence the hegemon's foreign policy in the later period of decline and retrenchment.²¹

Similarly, David D'Lugo and Ronald Rogowski (1993) argue that the autonomy of domestic institutions can affect the state's ability to extract additional domestic resources. D'Lugo and Rogowski maintain that during the Anglo-German Naval race (1909-12), Britain extracted a greater share of societal resources for naval spending than Germany. Their rationale is that Britain's constitutional system was more flexible. In Britain, the

²⁰ A more simple version maintains that overextraction and overexpansion is the result of narrow interest groups which are able to capture or hijack the state to advance their selfish interests. In these instances, the state is merely the agent of powerful interest groups. For example, Hobson (1938) and Lenin (1939) maintain that imperialism is the result of monopoly capitalist seeking to export surplus capital to thwart economic decline. The military is enlisted to protect their overseas commitments. Accordingly, while the cost of defending the empire is borne by society as a whole, the benefits accrue to a select elite. Scholars often argue that another group interested in expansion is the military. Seeking increased military spending, both inter-service rivalry and military industrial complex can contribute to over-expansion, see Posen (1984).

²¹ For instance, in the case of Britain, until 1858, British dominions in India were governed through the decree of the East India Company. However, at the end of the mutiny in India, the East India charter was revoked. The India Office became the new governing agency in Britain and the Secretary of State for India was added to the Cabinet. A cabinet position granted the Secretary of State for India access to the inner circle and the prime minister. Once more, India underwrote all of its own administrative costs, granting the India Office considerable independence from the Treasury, see Davis and Huttenback (1988). Accordingly, in selecting where to retrench, the India Office's superior strength and entrenched position in the decision making process ensured that Britain was slow in retreating from central Asia.

Treasury had the power to levy both direct taxes and to borrow in order to bridge any shortfall in defense spending. In contrast, after German unification in 1871, as dictated by Germany's constitution, much of the power to tax remained in the hands of the states, rather than the federal Reich. The consequence was that a weak German Treasury was unable to secure a larger share of revenue for bigger defense budgets.²²

Finally, Joseph Lepgold (1990), Aaron Friedberg (1988), and Charles Kupchan (1994) maintain that entrenched ideas and beliefs of state leaders can prevent a declining state from reducing global commitments or increasing military spending in order to restore the balance. According to Joseph Lepgold, despite the United States' relative decline since the 1960s, there has been little revision in America's original pledge to NATO. Lepgold argues that American leaders have been slow to reduce global commitments for fear of damaging America's reputation and credibility to defend its remaining obligations. Similarly, according to Friedberg, in the face of new and old threats to Great Britain's global interests (1895-1905), British leaders were unwilling to revise embedded beliefs about the dangers of increased government expenditure on defense. The tradition of laissez faire government led many decision makers to believe that Britain could not increase government expenditure and raise taxes without damaging its economy (incorrectly according to Friedberg). It was widely accepted by decision-makers that the proper solution for continued growth and economic prosperity was a reduction in government expenditure, and particularly in defense spending.²³

²² See Ferguson (1994).

²³ According to Friedberg (1988), Britain's leaders came to the incorrect conclusion that the economy could not sustain increased government spending. While Friedberg argues that increased military spending would have given a boost to Britain's sagging economy, it is unlikely that Britain could have borne the formidable and constantly increasing burden of matching the combined defense spending of a rapidly industrializing U.S., Germany, Japan, and Russia. Failure to match the strength of these emerging states, while seeking to maintain its vast foreign commitments, would have reduced its ability to defend its global interests, leaving it weak and vulnerable to attack everywhere.

Finally, Charles Kupchan maintains that embedded strategic culture can prevent a declining state from reducing its overseas commitments. According to Kupchan, a state which is declining in relative military position and which is highly vulnerable to attack will pursue an overly competitive strategy in the periphery to demonstrate its resolve to defend its interests and an overly cooperative strategy in the core. As part of this strategy, decision makers propagate beliefs about the strategic value of empire to gain domestic support for defending the periphery. This propaganda leads to the formation of a "strategic culture" which eventually becomes embedded in both the state and society. In subsequent periods, when decision-makers seek to reorient the state's foreign policy and concentrate the state's resources in the core, this strategic culture will prevent retrenchment from its overseas empire. The disequilibrium between the preference for retrenchment and the embedded strategic culture of retaining the empire will raise the political cost of a policy of retreat to an unacceptable level for state managers.

In summary, domestic politics arguments maintain that domestic constraints will result in a state of over-extension (i.e., commitments exceed capabilities). These scholars argue that regime-type, state society relations, and/or entrenched interest groups, institutions, and ideas can restrict a hegemon's ability to correct imbalances in its capabilities and commitments by preventing it from either increasing its military spending or reducing its overseas obligations. Thus, they suggest that only a domestically unconstrained hegemon can restore the balance between capabilities and commitments.

These three perspectives on decline (realism, globalism, domestic politics) are distinguished by their emphasis on regionalism or globalism, and the influence of domestic constraints. As discussed in detail in Chapter 2, in terms of regionalism versus globalism, only a regionally differentiated perspective can be the basis of managing

decline. One problem with the globalists perspective is the assumption that there are only two states in the international system, the declining hegemon and the rising contender, and concomitantly, that the hegemon's decline will occur globally and rapidly. This perspective greatly oversimplifies the hegemon's predicament. Instead, the declining hegemon is likely to confront different emerging challengers which rise at different rates and challenge the hegemon's leadership in disparate parts of its empire. The more geographically extensive the hegemon's empire, the greater the number of rising challengers it is likely to confront. The outcome of this "regionally differentiated framework of world politics" is that the loss of hegemony over one locale rarely translates into a global loss of hegemony to a single emerging contender. Instead, in confronting different contenders on disparate fronts, depending upon the nature of the hegemon's foreign commercial policy, it can differentiate among emerging contenders, selecting a security strategy which will retard its rate of decline. Thus, rather than declining rapidly, globally, and simultaneously, a hegemon can slow its rate of descent, lengthening its tenure as a great power.

Second, how realists restore the balance and how they prioritize global commitments can accelerate the hegemon's fall from the great powers. For realists, the hegemon will restore the balance by increasing military spending or reducing global commitments with little concern for finances. However, in favoring national security over fiscal strength, the hegemon risks undermining its future military capability. In particular, excessive and prolonged extraction to keep pace with the combined military buildup of several emerging challengers will erode the hegemon's productive base and ultimately its ability to construct and maintain a modern military. Similarly, with little concern for costs, realists suggest that a declining hegemon will prioritize its commitments based on the region's strategic value, trimming its commitments only in

less strategic locales.²⁴ However, in standing firm in the face of an emerging ally, even in a strategic locale, the hegemon risks undermining its fiscal strength due to prolonged defense spending. Thus, a declining hegemon must consider both the security and fiscal ramifications of any security strategy or risk accelerating its decline from the great powers.

Finally, the absence of domestic constraints is not a necessary condition for managing decline. In fact, domestic constraints can restrain a hegemon from excessive and sustained peacetime defense expenditure, protecting its future military capacity. For instance, Britain's Exchequer and even Castile's Cortes (before the 1620s) rejected a strategy of ever-increasing military spending, recognizing that fiscal strength was another leg of defense.

Selection of Cases

I have selected cases based on a number of criteria. First, I have selected historical cases of hegemons which had extensive global commitments and which encountered rising contenders for leadership in different parts of their formal and/or informal empire during peace-time and war-time, rather than focusing solely on the latter. Consequently, each hegemon was faced with the dilemma of how to restore the balance between capabilities and global commitments. Within each case, the selected time-frame reflects the period in which the hegemon declined from undisputed leader to confronting emerging competitors for leadership. This period is characterized by a change in the distribution of power from hegemonic to multipolar. For instance, in the three cases I have selected (Spain, 1621-1648; Britain, 1889-1912; Britain 1932-1939), the beginning date marks the period in which the declining hegemon's leadership is first challenged.

²⁴ However, in contrast to the globalists, realists do adopt a differentiated view of decline.

For Spain, 1621 marks the end of the Twelve Years Truce and the preparation for preventive war against the Netherlands, for Britain, 1889 marks the enactment of the Naval Defence Act in response to an emerging France and Russia, and finally for Britain, 1932, marks the end of the Ten Year Rule and the beginning of limited rearmament. These periods often occur well before the complete collapse of the hegemon's empire. In adopting a regionally differentiated framework of world politics, each case study consists of sub-cases which examine how the declining hegemon responded in the specific region. The number of sub-cases will vary based on the extensiveness of the hegemon's empire and the number of rising contenders it confronts.

Second, I have selected cases in which the declining hegemon pursued its best short run strategy. A hegemon's best short run strategy is defined as the security strategy that will decelerate its rate of decline from the ranks of the great powers to a second rate power relative to its alternative security strategies.²⁵ The rationale is that hegemons which pursued their best short term strategy are the only states in the running to manage their decline. Third, I have selected cases with variance in the hegemon's commercial policy and domestic constraints (see table 1). These cases are, domestically constrained liberal Britain (1889-1912), domestically constrained imperial Britain (1932-1939), and domestically unconstrained imperial Spain (1621-1640). I have excluded a case of a domestically unconstrained liberal hegemon because I would expect it to pursue the same foreign policy strategy as a domestically constrained liberal hegemon. The British cases are especially attractive because they examine a single state across different time periods, holding domestic and international pressures constant (among other possible variables), while varying foreign commercial policy.

²⁵ There are debates in the literature on international relations over how to measure power and which facets matter in order to determine which states are in fact great powers and which are not.

Table 1.--Case Studies

Declining Hegemon	F.C.P*	Domestic Flexibility	Emerging Contenders	Security Strategy
Spain (1621-1648)	Imperial	Unconstrained	Britain, France, Ottoman Empire, Netherlands, Sweden	Extraction
Britain (1889-1912)	Liberal	Constrained	U.S., Japan, France, Russia, Germany	Devolution
Britain (1932-1939)	Imperial	Constrained	United States, Italy, Germany, Japan	Accommodation

* Foreign Commercial Policy

I excluded cases in which the hegemon lost its empire in a single instance. Under such conditions, the declining power was not confronted with the dilemma of balancing its resources and its commitments. For this reason, a declining hegemon such as Napoleonic France was rejected because its vast empire was virtually dismantled by the end of the Napoleonic Wars (Napoleon's downfall was more rapid than his rise). I have also excluded cases in which the hegemon's empire was protected or defended by another great power. Again, under this condition, the hegemon will not have to make crucial decisions about balancing resources and interests. For this reason, I excluded the Ottoman Empire (or the Sick Man of Europe), because by the 19th century, Britain defended the Ottoman Empire against dismemberment by Russia and France (known as the Eastern Question).

Definition: Decline

Hegemonic decline can broadly be divided into direct and indirect sources. Direct sources of decline are often attributed to economic and political mismanagement. They include entrenched economic interests groups, a decay in morals and the loss of moral virtues, poor leadership, rigid social structure, corruption, and economic mismanagement.²⁶ In these instances mismanagement directly contributes to the hegemon's demise. For instance, the decline of the Ottoman Empire is often attributed to poor leadership. After a wave of fratricide, the sons of the Sultan were kept in the palace in separate quarters called kages (cage), and succession was to go automatically to the oldest living son. Yet, he remained isolated from politics for the bulk of his life until his time to rule. This system ensured that no sultan from the seventeenth century forward would have any knowledge of or training in government affairs until he came to power. It is often noted that after 1566, thirteen incompetent sultans ruled in succession.

Indirect sources of decline will require that the hegemon adjust its foreign policy to its new environment.²⁷ Environmental shifts include the advent of new technology which makes current products obsolete (mainly military, such as Britain's Dreadnought of 1906), new forms of transportation and communication (for instance, some attribute the decline of Venice and the Ottoman Empire to shifts in trade routes), and demographic

²⁶ For instance, Olson (1982) argues that vested interest groups or "distributional coalitions" reduce economic efficiency and constrain economic growth. Gilpin (1981) and Ibn Khaldun (1967), emphasize the corrupting influence of economic prosperity (especially rising public consumption). On the negative effect of Britain's rigid social structure, see Barnett (1972). On Rome's economic decline, see Bernardi (1970), on its moral decay, see MacMullen, 1988, on the moral weakening of the ruling classes, see Eisenstadt (1963).

²⁷ See the organizational literature on decline, Whetton (1987, 1980); Zammuto and Cameron (1985); Weitzel and Jonsson 1989).

growth.²⁸ Even changes in the organization of the state (i.e., the bureaucratization of France in the 1790s) will contribute to uneven rates of growth, forcing other states to adjust or suffer decline.²⁹ In this instance decline is a result of the inability or unwillingness of a state's leaders to adjust to the external shock, and not due to domestic mismanagement.³⁰

A hegemon can fail to adjust its foreign policy to a change in its environment for two reasons. First, the hegemon might not be able to adjust its foreign policy for domestic economic or political reasons. Under this condition, domestic barriers, such as insufficient economic resources, entrenched interest groups, or state managers will restrict the hegemon's foreign policy adaptability. For example, as discussed in greater detail below, in the case of Britain during the inter-war period, the Treasury Department successfully blocked the state's attempt to rearm (i.e., prevented it from mobilizing additional domestic resources) and thus prevented it from adjusting its foreign policy to its declining global position. Second, a great power might not be able to adjust to environmental shocks for external reasons. In this instance, external barriers will prevent the state from adjusting its foreign policy. For instance, a declining great power might be unable to find an alliance partner to balance against a challenger.

²⁸ It is often argued that latecomers have an advantage in that they can adopt newer technological innovations while earlier investors must wait to recoup initial investment, see Chase-Dunn (1982); Gerschenkron (1962).

²⁹ Keohane notes that powerful "countries can postpone adjustment; and the stronger they are, the longer it can be postponed . . . but it merely postpones the inevitable, making it more difficult to deal with in the future" (1982, 70).

³⁰ One consequence of an external shock is that it encourages sameness and duplication (i.e., follow the leader) among the great powers. Since states are competing with each other, if one state introduces a change that will give it an advantage or make it stronger than the rest, the others must duplicate it in order to keep pace. Any state which fails to do so will fall behind the states that do adapt, see Stein (1990, 115-116).

There exists a fundamental difference between these two sources of decline. While domestic mismanagement directly contributes to the demise of the great power, external shifts will only indirectly contribute to its decline. In the latter case, decline is the result of internal and external barriers which prevent or restrict the declining hegemon from adapting its foreign policy to a shift in its environment.

CHAPTER 2

DILEMMAS OF STRATEGY AND FINANCE

Fiscal strength and national security are inextricably linked. Yet scholars often consider either domestic financial concerns or national security interests alone. In this chapter I examine how hegemonies manage their decline. In particular, I examine periods in which the distribution of power is shifting from hegemonic to multipolar. Facing rising contenders on disparate fronts, the grand strategy of a declining hegemon is to remain in the great power game as long as possible for that hegemon or to slow its inevitable decline into the ranks of the second tier states. The hegemon's rationale in remaining in the great power club is that there is a hierarchy among states in the international system. In remaining a great power, the erstwhile hegemon can continue to influence the rules of the game by which international politics is played in order to protect its existing commercial and security interests. However, as a second-tier state, the erstwhile hegemon's influence will also decline, leaving it dependent on the remaining great powers to protect its national interests.

In facing emerging contenders on different fronts, the dilemma for a declining hegemon is how to restore the balance between its military capabilities and its global interests while protecting its economic staying power and its national security objectives. In choosing a security strategy which favors either fiscal or security interests over the other, the hegemon risks accelerating its decline from the ranks of the great powers. In particular, the predicament for the hegemon is that maintaining its global commitments

without increasing its rate of defense spending will weaken the hegemon's relative military power, tempting rising states to challenge its leadership, while prolonged increases in societal resource extraction to keep pace with the military spending of several rising contenders will erode the hegemon's fiscal strength (i.e., productive base) and ultimately its military capability. In abandoning its empire, the declining hegemon risks undermining its national security by strengthening the war-making capacity of a future rival. Thus, to slow its rate of decline from the great power club, the hegemon must select a security strategy which protects both its political economy and national security interests.

The import of this work is that it highlights the linkages between economic and security policies. First, the nature of a hegemon's foreign commercial policy will affect how it restores the balance between its capabilities and commitments. Ranging from liberal to imperial, a hegemon's foreign economic policy reflects whether the hegemon will impose an open door or closed door trade policy on its overseas formal and/or informal empire and any regions it comes to dominate. The nature of a liberal or imperial hegemon's international commercial policy will include or exclude certain security strategies among its foreign policy options. Consequently, liberal and imperial hegemons will select from a different range of security strategies for managing decline.

Second, the nature of a hegemon's foreign commercial policy will affect how long it can remain in the ranks of the great powers. In the short term, both liberal and imperial hegemons can select from a range of security strategies which will accelerate or decelerate their rate of decline. However, in the long run, a liberal hegemon can select a security strategy that will ensure that it remains in the ranks of the great powers longer than if it was an imperial hegemon. The rationale is that a security strategy which favors either economic or security concerns to the exclusion of the other will accelerate the

hegemon's fall from the ranks of the great powers. Although often aware of the dangers, imperial hegemonies can only select from a range of security strategies that will erode either its economic staying power or undermine its national security interests. In particular, imperial states will fall from the ranks of the great powers due to either excessive defense spending, accommodating an incompatible rising challenger, or insufficient military capability to defend its global commitments. In contrast, liberal hegemonies can select a foreign policy strategy that will safeguard both its economic strength and its national security interests, lengthening its tenure as a key player in the great power game.

This chapter challenges the existing literature on decline in three ways (see Chapter 1 for a detailed review of this literature). First, realists maintain that geostrategic concerns are the primary factor in shaping how a declining hegemon will restore the balance between its capabilities and commitments. In contrast, I argue that a declining hegemon must consider both the political economy and security ramifications of its grand strategy or risk accelerating its rate of decline. Second, globalists maintain that a hegemon's fall from the ranks of the great power's will occur rapidly, globally, and simultaneously. In contrast, I argue that this view over-simplifies the hegemon's dilemma. Instead, the hegemon will decline at different rates in disparate parts of its formal and informal empire, and is likely to confront different rising contenders for regional leadership in these locales. Depending on the nature of the hegemon's foreign commercial policy, it can differentiate among emerging contenders, selecting a security strategy which will slow its rate of decline. Finally, domestic politics arguments suggest that only a domestically unconstrained hegemon can manage its decline. However, domestic constraints can restrain a hegemon from excessive and sustained peacetime defense spending, safeguarding its future military capacity.

This chapter is organized as follows. The first section discusses the dilemma of balancing capabilities and global commitments in greater detail. In contrast to the globalist view of decline, the second section develops a regionally differentiated framework of world politics. One implication of this framework is that it is possible for a hegemon to retard its rate of decline. The final section develops a number of hypotheses on how hegemons manage their decline.

The Dilemma of Balancing Capabilities and Global Commitments

The grand strategy of a declining hegemon which is facing emerging contenders for regional hegemony in disparate parts of its empire is concerned with restoring the balance between its capabilities and commitments while safeguarding its fiscal strength and national security interests in peacetime and wartime.³¹ The declining hegemon's predicament is how to balance its military capabilities and global commitments without excessive defense spending, which will erode its economic staying power and future military capacity, and without accommodating a rising revisionist challenger, which will threaten its national security interests. As Walter Lippmann notes "Foreign policy consists in bringing into balance, with a comfortable surplus in reserve, the nation's commitments and the nation's power" (1943, 9).³²

The dilemma for a hegemon in balancing its military capabilities and its global commitments is three-fold. First, if a hegemon maintains its global commitments without increasing its rate of domestic resource extraction for military spending in order to protect

³¹ On definitions of grand strategy, see Posen (1984, 13-14); Kennedy (1991, 1-3); Rosecrance and Stein (1993, 4).

³² Also, see, Huntington 1987/88. Arthur Stein claims that "A Great Power is overextended when it extends commitments that it cannot support because of insufficient capability" (1993, 99). According to Paul Kennedy, "grand strategy is about the balancing of ends and means, both in peacetime and in wartime (Kennedy 1991, 4)."

its fiscal strength (see below), it risks eroding its national security interests. The reasoning is that its military capabilities will be insufficient to protect its foreign interests, leaving it vulnerable to preemptive attacks everywhere. In allocating too little to defense, the declining hegemon will lack the military capability to deter rising challengers and, in the event that deterrence fails, the capability to defend its extensive global interests (i.e., preventive war). A disequilibrium between the declining power's military capability and its global commitments is especially dangerous because it might tempt rising states to challenge the declining hegemon's leadership. As Robert Gilpin warns, as the gap between a hegemon's capabilities and its global commitments widens, a rising contender's expected benefits in challenging the declining power will begin to exceed the expected costs of doing so (1981, 187).

Second, if the declining hegemon abandons its empire in order to lower the costs of hegemony, it risks undermining its own national security objectives by enhancing a rising challenger's war-making capability. The danger of global retreat is that a rising revisionist challenger will capture the economic and military assets of the regions which will add to its material power, strengthening its military capability. Second, a revisionist challenger can impose a new regional order over any locale which it comes to dominate, to the detriment of the declining hegemon's commercial interests. One outcome is that the declining hegemon may lose access to its traditional markets, investments and raw materials in the locale, which will have a negative effect on its future prosperity and fiscal strength, especially if the declining power is highly dependent on trade with the region.³³

³³ While often emphasizing the liabilities of colonies, scholars ignore the positive security externalities of empire (O'Brien 1988; Kennedy 1989). For instance, Moscow's retreat from its global interests, and especially from Eastern Europe, has denied Russia influence over events in strategic regions which could threaten its national security.

Finally, if the declining hegemon balances its capabilities and commitments by increasing its rate of resource extraction for military spending in order to protect its national security (in preparation for preventive wars against several rising challengers), it risks undermining its fiscal strength and ultimately its military capability. Robert Gilpin (1981) and Paul Kennedy (1987) warn that excessive peacetime defense expenditure to keep pace with the military spending of several rapidly rising contenders will divert resources from domestic investment, limit the scope of future economic growth, and eventually weaken the productive strength of the declining hegemon to construct and then maintain a modern military force.³⁴ In contrast, the rising challengers have few global commitments and lower defense burdens, allowing them to allocate a larger percentage of their resources towards domestic investment. As the challengers encroach, there is even greater pressure for the hegemon to extract additional resources, further contributing to its relative economic decline. Second, sustained military spending beyond the capacity of the economy will drain the hegemon's financial reserves (i.e., its war chest) which it will need to extract in the event of a prolonged war.³⁵ Finally, in increasing the rate of military spending, state leaders might confront growing societal opposition to higher taxation and possibly even a taxpayer revolution.³⁶

³⁴ Also, see Melman 1974. Generally, there is a three step argument which links military spending and economic decline. First, military spending to defend global commitments diverts resources from "wealth creating" activity such as domestic investment, R&D (commercial, not military), education, the infrastructure, equipment and factories, and the like (as will non-military government consumption such as entitlement programs and private consumption). Second, a shift in resources away from productive investment slows the expansion of the existing stock of capital and national wealth available for investment, and impedes the rate at which technology and innovation spread throughout the economy. Finally, in constraining reinvestment, innovation, and production, military spending reduces the state's long term productive capacity which precipitates economic decline.

³⁵ On the danger of budget deficits, see Thurow (1985).

³⁶ On the guns versus butter debate, see Mintz and Huang (1991).

There are two criticisms of this argument linking increased resource extraction and economic decline.³⁷ First, in some instances military spending can stimulate economic growth (Kupchan 1989). Defense spending can be used as a counter-cyclical macro-economic government tool to stimulate demand and reduce unemployment, especially when the economy is operating below full employment or when there is excess capacity. For instance, it was military spending during World War II, not Roosevelt's New Deal programs, which got the United States out of the Great Depression (Rosecrance 1990b). Similarly, defense spending during the Korean war pulled the U.S. out of the 1949 recession. Likewise, Aaron Friedberg maintains that at the turn of the nineteenth century, Britain should have pursued a policy of higher military spending in order to energize its faltering economy, rather than a reduction in military spending (1988).

In response, Kennedy's and Gilpin's arguments suggest a concern primarily with excessive and protracted military spending in peacetime and over a period of several decades if not longer, not with short term emergency spending or counter-cyclical military spending. Kennedy defines excessive military spending as more than 10 percent over the long term, and as little as 5 percent when the state is structurally weak (Kennedy 1987, 609, n. 18).³⁸ While both will concede that short term military spending can be productive, and neither suggest that defense spending is unnecessary, their argument is that excessive and sustained defense spending will contribute to the hegemon's economic demise.

³⁷ Chan warns that another problem with this argument is the long time lag make it difficult to ascertain whether military spending is the primary cause of economic decline (1985). For a critical assessment of the link between military burdens and economic growth, see Rasler and Thompson (1991, 1988); Thompson (1991); and Kupchan (1989).

³⁸ On this point, see Gilpin (1981). On the right, some argue that the U.S. policy of "peace through strength" forced the Soviet Union into an arms race which exacerbated Soviet economic decline.

A second and more compelling criticism of the defense spending versus economic growth argument is that while defense spending does crowd-out investment, so does non-defense government spending and private consumption (see Friedberg 1989a, b).³⁹ Among the developed countries, both non-defense government spending and especially private consumption exceed government military spending as a percentage of gross domestic product. In the case of the United States, expansion in entitlement programs (Social Security and Medicare) rather than increases in defense spending, have become the primary source of increased government spending. However, excessive and sustained defense spending will eventually crowd-out investment, contributing to slower economic growth. The more resources are devoted to defense, the less will be available for non-defense government spending, public consumption, and private investment. Significant and prolonged increases in the level of defense spending will require either a reduction in government spending, in private consumption, or in investment (or deficit spending and in extreme cases, insolvency, as in the case of Spain in 1647). Thus, in encountering emerging contenders on different fronts, the dilemma for a declining hegemon is to restore the balance while protecting its fiscal strength and national security interests. In favoring either fiscal or security concerns, the hegemon risks accelerating its decline from the great power ranks.

A Regionally Differentiated Framework of World Politics

One shortcoming in the existing literature on hegemonic decline is that scholars tend to over-simplify the hegemon's dilemma in balancing its capabilities and commitments by examining its position in a single region or time period. In contrast to

³⁹ Finally, Friedberg contends that military spending alone did not cause America's decline and defense cuts alone will not cause dramatic improvements in its economic standing (1989a).

the globalists' perspective (but like the realists), I adopt a regionally differentiated framework of world politics.⁴⁰ This regional framework is based on the view that the international system is composed of multiple regions or spheres of influence. A hegemon is defined as a state which simultaneously dominates several regions of the globe, and which as a unit comprise its informal and/or formal empire (see Kaufman 1976; Keal 1983; Triska 1986). In this context, hegemony means that the state creates and enforces the "rules of the game" over each region it dominates.⁴¹ In contrast, globalists define hegemony as control of the international system by a single powerful state (Gilpin 1981, 31).

A regionally differentiated framework differs from the globalist approach in several important aspects.⁴² First, differential rates of industrial growth mean that contenders will rise at unequal rates across a declining hegemon's empire, with some contenders rising earlier and faster than others. Second, a hegemon is likely to confront different rising competitors for regional leadership on disparate fronts and in different parts of its empire. The loss-of-strength gradient and the differentiated nature of power (discussed below) increase the likelihood that a declining hegemon will encounter different emerging challengers in different regions. The more geographically extensive a hegemon's empire, the greater the number of rising contenders for regional leadership it

⁴⁰ For a discussion and an application of the literature on subsystems, see Binder (1958); Cantori and Spiegel (1969); Brown (1984); Brecher (1963); Zartman (1967); Noble (1984); Doran (1989).

⁴¹ Joshua Goldstein defines hegemony as being able "to dictate, or at least dominate, the rules and arrangements by which international relations, political and economic are conducted . . . Economic hegemony implies the ability to center the world economy around itself. Political hegemony means being able to dominate the world militarily" (1988, 281).

⁴² For an application of this perspective see Stein and Lobell (1997). We argue that the end of the Cold War will not have a uniform effect on the post-Cold War era. In regions which were isolated from the Cold War and regions on the periphery of this rivalry, there will be little change. However, in regions which were highly penetrated by the superpowers, future regional relations will depend upon whether superpower intervention in regional affairs increased or decreased regional conflict and whether or not this involvement left a lasting impression on the region.

can confront. Finally, a hegemon's leadership is likely to be challenged by rising contenders in different periods across these locales. This means that a declining hegemon will encounter challengers earlier in some regions than in others. Even the same rising competitor will often challenge the declining power's hegemony at different periods in disparate regions, not simultaneously everywhere.

The outcome of these three characteristics of the international system is that a hegemon's loss of leadership over one locale rarely translates into a loss of global leadership to the emerging challenger. Even if a hegemon encounters the same emerging challenger across regions, it is likely to cede (or lose) leadership region by region or in territorial pieces, rather than transfer leadership over the entire international system to the rising contender in a single instance. Consequently, depending upon the nature of the hegemon's foreign commercial policy, it can differentiate among emerging contenders, selecting a security strategy which will safeguard its political economy and its national security interests, retarding its rate of decline. Thus, rather than declining globally, rapidly, or simultaneously, a declining hegemon can slow its rate of descent, lengthening its tenure as a great power.

This differentiated framework of world politics more accurately captures how leadership is ceded than the globalist approach. For instance, the globalist approach maintains that a declining Britain transferred world leadership to a rising United States after the end of World War II. However, as early as the turn of the nineteenth century, Britain devolved leadership over the Americas to a rising United States and ceded leadership over the Pacific to an emerging Japan, while standing firm against the remaining emerging challengers in other parts of its empire (see Chapter 3). During and shortly after World War II, a declining Britain ceded leadership over regions such as the Pacific and the Middle East to the United States. Thus, not only did Britain devolve

leadership over different regions to the United States and at different points in time, but Britain also devolved regional hegemony to other rising contenders. Similarly, the advent of American hegemony was not global in nature and did not begin after World War II, but instead occurred first in the Americas around the turn of the century.

Similarly, some scholars argue that Japan is currently encroaching on United States leadership over the Far East. As one article notes, "Japan, rather than the United States is now the dominant economic player in Asia. Japan is the region's technology leader, its primary supplier of capital goods, its dominant exporter, and its largest foreign direct investor and foreign aid supplier" (Borras and others 1992).⁴³ However, even if the United States is currently in the process of devolving leadership over the Pacific Rim to Japan, the United States has not transferred global leadership to a rising Japan.⁴⁴ Once more, this does not preclude the United States from devolving hegemony to other emerging contenders.

Two forces increase the likelihood that a declining hegemon will encounter different emerging competitors for regional hegemony and that these states will vary

⁴³ Similarly, Crone notes that in the Far East, Japan has become a significant challenger in trade and direct foreign investment and the lead country in foreign aid (1993).

⁴⁴ On this point, it is worth noting that Japan played an active role in Latin America's debt management (Katada 1994). My perspective suggests that Japan is beginning to encroach on U.S. leadership over the Americas. However, it remains unclear whether the U.S. is willing to peacefully devolve leadership to Japan. U.S. actions in other issue areas demonstrate a reluctance to accommodate Japan. For instance, only in 1990 was Japan promoted to the long overdue second rank in voting power in the IMF, equal to Germany and below the U.S. In addition, while the U.S. has encouraged Germany to invest in eastern Europe, Washington has been concerned about Japan's heavy foreign aid and investment in the Pacific rim.

One possible outcome is that the U.S. will stand firm in the Far East. For instance, George Friedman and Meredith Lebard warn that "For the United States, fear of being forced out of the Pacific is extremely deep rooted concern . . . Declining influence in this region will be seen as an economic and political challenge to the United States . . . Rising Japanese economic influence in the region will inevitably translate into political influence and military presence . . . With the Soviets no longer an important factor, any increase in Japanese power in this region will be seen as a challenge, rather than a benefit, to the United States" (1991, 102).

across regions. These are the loss-of-strength gradient and the differentiated nature of power.

Loss-of-Strength Gradient

The loss-of-strength gradient holds that the effectiveness of military power declines in a linear fashion over space, reducing the ability of a state to project its power over long distances.⁴⁵ According to Kenneth Boulding, this occurs because long distances create organizational and command problems, damage military morale, encourage domestic dissension, and debilitate soldiers and their equipment (1963). For instance, in the 1904-05 Russo-Japanese War, Russia's inability to maintain long supply lines across Siberia (stretching several thousand miles) contributed to Japan's victory.

The loss-of-strength gradient is important for this regionally differentiated framework because it reduces the likelihood that a single state can achieve a truly global position (i.e., simultaneously dominating all regions of the international system). In reducing the ability of a state to project its power over long distances, the loss-of-strength gradient allows states to emerge in regions beyond the effective reach of the hegemon. This characteristic of power increases the likelihood that a declining hegemon will confront different emerging states across regions, especially on the fringes of its empire. Consequently, the more extensive the hegemon's empire, the greater the number of emerging contenders for regional leadership it is likely to confront.

Even today, in a world of intercontinental ballistic missiles and supersonic planes, distance continues to limit the ability of a superpower to project its power. Although the time it takes to move a large number of men and equipment over distances has been shortened, logistical problems still persist and modern technology has created new

⁴⁵ For a counter argument, see Wohlstetter (1968).

challenges. For instance, long range aircraft capable of transporting men and supplies also require a long landing strip. Observing the U.S. operation in Somalia, Colin Powell noted, "Logistically, it is enormously challenging. When you say to somebody, 'Take 28,000 troops and send them 7,500 miles or so away, and by the way, there's no potable water there, and there are no gas stations and there's only one or perhaps two C-141 capable airfields and the port facilities only hold one or two ships,' that is very demanding" (*Los Angeles Times*, 5 December 1992).

Differentiation of Power

The second factor which increases the chance that a declining hegemon will confront several rising contenders for leadership is the differentiated nature of power. Rarely does a single state have the necessary financial resources or manpower to dominate all categories of military power (i.e., land, sea, and air). Instead, a state will often favor one category of defense over the others. This characteristic of power reduces the likelihood that a single state can dominate all regions of the globe simultaneously. Instead, the differentiated nature of power limits the number of regions which the hegemon can control effectively.

The simplest differentiation in the nature of power is between continental and maritime powers. The advent of the railroad in the last 30 years of the nineteenth century greatly reduced the historic advantage that maritime powers had over land powers (Sprout 1952). The quick Prussian defeat of France demonstrated that railroads were a fast, cheap, and efficient means of land transportation. Up until this point, the most efficient means to move goods was through shipping, even if it required circuitous routes. In addition, the development of the railroad made it possible for land powers to have secure internal lines of communication and made such states less vulnerable to a naval blockade

(Mackinder 1904). For instance, as a land power, Russia's Czar Nicholas II wrote "the strongest fleet in the world can't prevent us from settling our scores with England precisely at her most vulnerable point [i.e., India]" (Friedberg 1988, 217). When the assistant to Britain's First Lord of the Admiralty was asked to determine what naval means existed to attack Russia, he responded "Russia's geographical position is such that she is very unassailable to a sea power with a small army" (Neilson 1991, 716).⁴⁶ The differentiated nature of military power makes it difficult for a naval power to dominate the hinterlands and for a continental power to dominate overseas territories.⁴⁷

In summary, scholars often over-simplify a hegemon's dilemma by focusing on its position in a single region or time period. In most cases, had the declining hegemon confronted a single emerging challenger it could have concentrated its resources from other parts of its empire, overwhelming the contender's. Instead, I argue that a hegemon is likely to confront different emerging contenders which rise at different rates and challenge the hegemon's leadership in disparate parts of its empire. The more extensive a hegemon's empire, the greater the number of potential threats. In over-simplifying the hegemon's predicament, it is difficult to understand the dilemma that it faces in balancing its military capabilities and global interests while protecting its long term fiscal strength and its national security interests.

⁴⁶ Kupchan notes that, "A war between Germany [a land power] and Great Britain [a naval power] would in some ways resemble a struggle between an elephant and a whale, in which each, although supreme in its own element, would find difficulty in bringing its strength to bear on its antagonist" (1994).

⁴⁷ For this reason, a rising land power is most likely to extend its interests in areas contiguous to its own territory.

Managing Hegemonic Decline

Foreign Commercial Policy: Liberal and Imperial

A hegemon's foreign economic policy, as opposed to its domestic trade policy, is the commercial policy it will impose on any region it dominates or comes to dominate. The difference is that the former pertains to access to foreign markets dominated by the hegemon and the latter to access to the hegemon's domestic market. A **liberal hegemon** is a technologically advanced and powerful state (militarily and economically) that will create and then maintain a liberal economic order in its formal and/or informal empire. A liberal economic policy will ensure equal access to all nations to the area's resources and markets, allowing for freer movement of goods and capital. Often having a highly competitive economy (in the past, the 'workshop of the world' or dominating new leading economic sectors), liberal hegemons will be enhanced by freer trade (as will liberal challengers, see discussion below).⁴⁸ The rationale is that commercially competitive liberal hegemons can compete with economically efficient rising contenders and gain or maintain the predominant share of wealth through the free interchange of goods, while any disruption in trade will harm its economy.

In contrast, an **imperial hegemon** is a powerful state which will impose an exclusive economic order in any region it dominates, preferring a commercial policy of economic self-sufficiency or economic autarky. Consequently, an imperial hegemon will shut out foreign commercial competition and investment, ensuring exclusive access to the

⁴⁸ Having a competitive economy does not guarantee that the hegemon will pursue a liberal foreign economic policy (another measurement is relative labor productivity, see Lake 1988). For instance, in the 1930s, Germany was economically advanced but pursued an imperial foreign economic policy. One explanation is the prominent role of the relatively inefficient landowners. For a discussion of advanced and backwards economies, see Krasner (1976); Brawley (1994); Rogowski (1989); Lake (1988).

markets and resources in its empire. Usually having a relatively uncompetitive economy, imperial hegemons will have a disadvantage in open door competition (as will imperial challengers, see below).⁴⁹ Robert Gilpin notes that "hegemony without efficiency tends to move toward imperial-type economies" (1981, 129). Unable to compete with more efficient liberal states, imperial states will impose a closed door regional trading order. In fact, according to Lake, imperial leaders have a tendency to impose optimum tariffs (with a large domestic economy and by excluding more efficient producers, imperial hegemons can promote increasing returns industries in their exclusive spheres; Lake 1988, 47; Conybeare 1988). Imperial powers will pursue a protectionist policy unless coerced by liberal states since an open regional economy will undermine its hegemonic position.

It is important to stress three points about liberal and imperial hegemons. First, a hegemon's domestic political system and its international economic policy do not need to correspond. It is possible to have a politically liberal, commercially imperial hegemon, as well as a politically autocratic, commercially liberal hegemon. Second, a declining hegemon's international economic orientation can change over time, moving towards a liberal or imperial policy. Third, a hegemon's foreign commercial policy may differ from its domestic trade policy. Consequently, a state that is protectionist at home might impose an open door policy on regions it dominates (the reverse is also possible).

In shifting from a hegemonic to a multipolar distribution of power, declining liberal and imperial leaders will confront either emerging liberal challengers, imperial challengers, or some mix of these emerging contenders, rising at different rates and in

⁴⁹ An uncompetitive economy does not necessarily mean that the hegemon will pursue an imperial economic policy.

disparate parts of its empire.⁵⁰ A rising **liberal challenger** is a state that has a preference for a liberal regional economy. Reflecting the classical liberal view of trade, a liberal challenger prefers an open door economic order in any region it dominates since "it offers the best chance of obtaining the goals it has in mind."⁵¹ In particular, the liberal challenger will maximize its welfare under a liberal commercial arrangement. A rising **imperial challenger** is a state that will seek to create its own mercantilist position in the region in order to advance its interests. Consequently, it will establish its own exclusive commercial order in any locale which it dominates, whether that locale is currently an open or closed door regional order. Thus, a regional trading system will be quite different under liberal and imperial leadership.

Rising liberal and imperial contenders might engage in preemptive wars in order to open-up or close-off a region, respectively. Based on the power transition literature, as differential rates of growth narrow the gap between rising and declining states, rising liberal contenders will be tempted to launch preemptive strikes against imperial

⁵⁰ One can use a simple signaling game to explain how, in a world of incomplete information, a declining leader can identify whether a rising contender is a supporter or a challenger. If a declining leader has perfect or full information about each rising contender, it can readily determine a rising state's type (according to Kreps, type refers to a any information that is not common knowledge to all players; 1990, 213). Under this condition there is little doubt about how to identify whether an emerging state is a potential regional successor or a future adversary.

However, in the real world it is necessary to relax the assumption of complete information (Bueno de Mesquita and Lalman 1992; Stein 1990, 1983; Jervis 1970). For a declining hegemon, just as an individual who prefers to fight a wimp instead of a bully can observe what others have for breakfast in order to gain insight into their type (wimp if he/she eats quiche and bully if he/she has beer; see Kreps 1990; and Cho and Kreps 1987), certain traits of a rising power will signal its type. Although a declining power can look at a number of traits in order to assess a rising state's type, the central trait I focus on is a rising state's foreign commercial policy.

In terms of the payoff structure for the declining and rising states, the declining liberal hegemon gets its most preferred outcome if it correctly identifies the emerging contender, standing firm against an imperial challenger and devolving leadership to a liberal contender. The declining liberal hegemon gets its least preferred outcome if it stands firm against a liberal contender and/or devolves leadership to an imperial challenger. A challenger gets its second best outcome if it does not fight the declining leader (i.e., the leader peacefully retrenches) and its best outcome if it does not have to disguise or deceive its type to the declining leader in order to avoid a fight (due to possible domestic costs). For an application to International Relations theory, see Alt, Calvert, and Humes (1988); Iida (1993); Morrow (1989); Powell (1987); and Stein (1990).

⁵¹ Organski distinguishes between satisfied and dissatisfied rising powers (1968, 366).

hegemons, while imperial challengers will target both declining liberal and imperial hegemons. The rationale is that the rising contenders will fear that the declining hegemon is about to launch a preventive war, which will push the challenger down its power curve. Rising liberal contenders will find it easier to cooperate in concert against an imperial hegemon in order to impose an open door trading order in the locale. More than a temporary marriage of convenience, liberal contenders will mutually benefit under a liberal commercial arrangement. In contrast, imperial challengers will have difficulty creating stable alliances. The reasoning is that an imperial challenger is a potential threat to rising and declining states (liberal and imperial) since it will seek exclusive control over any locale it comes to dominate.

Czarist Russia and Napoleonic France exemplify imperial challengers. According to Walter LaFeber, the Cold-War between the United States and the Soviet Union had its origins in the rivalry between a rising liberal and imperial challenger. In particular, "[The Russians] after annexing land in Asia, tried to control it tightly by closing the markets to foreign businessmen with whom they could not compete. This highlighted the problem between the two countries in the 1890s, The United States believed its prosperity increasingly required an "open door" to trade in China's rich province of Manchuria, but the Russians were determined to colonize and close off parts of Manchuria" (LaFeber 1991a, 2).⁵² Similarly, Napoleonic France posed a threat to Britain's regional trade order. Napoleon's Continental System (Berlin Decree of 1806) upset the existing regional trading order by outlawing the importation of British goods to the Continent with the intention of expanding French economic control of Europe, while weakening Britain's

⁵² Similarly, according to Fox, "The tension of the Cold War can be understood at least in part as an extension of the land-water dichotomy that first emerged in seventeenth-century Europe: to the east, the vast land-based territorial state of the Soviet Union is heir to the administrative-military tradition, while across the Atlantic to the west, the United States reveals its origins and membership in the oceanic trading community" (1991, 2).

economic power.⁵³ In particular, Napoleon intended to give French industry a Continental monopoly, while bankrupting Britain by cutting off its markets for exports. For Britain, Continental trade was vital to its economic health. In commenting on Napoleon's exclusive Continental System, Gilpin notes that, "at issue in the clash between industrial Great Britain and Napoleonic France were two fundamentally opposed systems for organizing the world's economy" (1981, 134).

A declining liberal hegemon will differentiate among emerging imperial and liberal contenders. It will view rising imperial challengers as a threat to its economic strength and national security interests.⁵⁴ First, in carving-out an exclusive sphere of influence in the area or in partitioning the region, an imperial challenger will deny the liberal hegemon access to its markets, investments, and raw materials in the locale. In particular, in seeking exclusive commercial rights, it will exclude the hegemon's more efficient traders and investors from the area's markets. The loss of access will undermine the hegemon's economic strength, especially if it is highly dependent upon trade with the region. Second, ceding regional leadership to an imperial challenger will strengthen the challenger's potential war-making capacity, eroding the declining hegemon's national security interests.⁵⁵ Consequently, the declining liberal hegemon will oppose territorial aggrandizement by an imperial challenger for several reasons.

⁵³ See Fox (1991, 93); Kaiser (1990, 250-3).

⁵⁴ Traditionally, it has been argued that maritime great powers tend to be trading states while continental powers tend to be territorial states. Based on this premise, Modelski argues that hegemonic wars will occur between declining naval powers and rising continental powers. The outcome is the defeat of the continental power and the transition of world leadership peacefully to a rising naval power. See Modelski and Thompson (1988).

⁵⁵ Rivals are unlikely to trade for fear that economic gains will be converted into military power, see Gowa (1994); on the inverse relationship between levels of trade and conflict, see Polachek (1980); Mansfield (1994).

In contrast, a declining liberal hegemon will view rising liberal contenders for leadership as supporters of its existing liberal regional economy. The rationale is that committed to the principles of a liberal economic order, the rising liberal state will not alter significantly the existing open door commercial order in the locale. Under the leadership of a liberal contender, the declining hegemon will retain access to its markets, investments, and resources in the locale, without strengthening the war-making capacity of a future rival and without bearing any of the costs associated with regional hegemony (the hegemon will free-ride on the new regional leader). In fact, the declining hegemonic leader is likely to assist in the rise of liberal contenders (accelerating their rate of ascent), hastening its own retreat from the locale, in order to reduce the costs of hegemony. For instance, Rosecrance and Taw note that "Dutch capital largely financed British commercial and industrial growth at the end of the seventeenth and the beginning of the eighteenth century. Similarly, British investment provided an essential stimulus to the growth of the United States both before and after the Civil War" (1990, 190). Around the turn of the century, Britain contributed to German industrial development, and after World War II, the United States encouraged Japan and Germany's rise. Strategically, a rising liberal contender will seek leadership over the locale from the declining liberal hegemon sooner rather than later, reducing the risk that the erstwhile hegemon will move in the direction of an imperial foreign policy and thus a rival.

However, Stephen Rock (1989b) and Mark Brawley (1994) challenge the concept of peaceful transition among certain liberal states. According to Rock, peace is most likely to "break-out" among states which are heterogeneous in their economic activity and tension is most likely to escalate among states which are homogeneous in their economic activity. Conflict is likely among homogeneous states, even if they are liberal states, because they will compete with one another in home and overseas markets. Similarly,

according to Brawley, a capital abundant declining liberal leader and a capital abundant liberal contender are natural economic rivals because they will produce and/or export similar goods and services.

In contrast, a declining imperial hegemon will not differentiate among emerging contenders, but will view all rising states (liberal and imperial), as a threat to its national interests. The rationale is that no successor will continue to maintain the imperial hegemon's privileged commercial position in the locale. For a declining imperial hegemon, an emerging liberal contender will alter the status quo by imposing a liberal economic policy, allowing access to its exclusive sphere. Unable to compete with more efficient liberal producers, the declining hegemon will lose its market share to the rising liberal contender. In contrast, a rising imperial challenger will replace the imperial hegemon's existing regional order with its own exclusive order, blocking the hegemon's future access to its interests in the locale. Thus, the loss of access will undermine the imperial hegemon's fiscal strength by denying it a market for its goods and will erode its national security by enhancing the war-making capacity of a future rival.

Alternative Security Strategies to Balance Capabilities and Global Commitments: Extraction, Devolution, and Accommodation

In facing rising contenders on disparate fronts, a hegemon's existing rate of resource extraction for military spending is unlikely to be sufficient to defend its extensive global interests. Failure to restore the balance between the declining leader's military capabilities and its global commitments will tempt rising contenders to challenge its leadership. As Robert Gilpin warns, as the gap between a great power's capabilities and its global commitments widens, a rising contender's expected benefits in challenging the great power will begin to exceed the expected costs of doing so (1981). Declining from undisputed leader to confronting emerging competitors for regional leadership,

liberal and imperial hegemons have a number of alternative security strategies for restoring the balance between their capabilities and global commitments.⁵⁶ These strategies include, increase resource extraction for defense spending through borrowing, taxation, burden-sharing and/or state-led industrial growth; devolve regional leadership to a rising supporter or a local surrogate power; accommodate with some or all of the rising states. Each of these strategies has its attractions and its dangers.

Domestic Resource Extraction

The first strategy for a hegemon to balance its capabilities and global interests is to extract or mobilize additional domestic resources in order to increase its military capability (which includes both defense and foreign-policy outlays).⁵⁷ In increasing its rate of resource extraction, the hegemon will have sufficient capability to defend against challenges in disparate parts of its empire and on different fronts. A military buildup can deter an emerging contender from challenging the hegemon, and in the event that deterrence fails, prepare for a preventive war, destroying or weakening the rising competitor while the military advantage is still with the declining power (a preventive strike is a war initiated by the declining hegemon while it is relatively more powerful than a rising contender in order to avoid a war later under less favorable conditions, whereas a preemptive attack is under taken by the rising challenger because it believes that attack from the hegemon is imminent; Levy 1984, 90). However, as discussed below, there are inherent dangers associated with a strategy of extraction.

⁵⁶ For a discussion of strategies for managing decline, see Gilpin (1981, 186-210); Levy (1987); Huntington (1987/88). Also, see the literature on the trade-offs between internal arms buildup and external alliance formation as a means of balancing, Morrow (1993); Most and Siverson (1987); and Altfeld (1984).

⁵⁷ For Waltz, this constitutes internal balancing (1979). Mastanduno, Lake, and Ikenberry differentiate between resource mobilization and extraction (1989). They maintain that mobilization is wealth creation while extraction is the consumption of wealth.

A hegemon has a number of alternative means to increase its rate of resource extraction. First, additional domestic resources can be extracted through domestic taxation and borrowing. Other strategies to acquire additional resources include extracting revenue from other states in the empire (i.e., burden-sharing) and territorial conquest to grab or steal wealthy regions. Second, domestic reforms can be implemented to create greater efficiency in the means of extracting or using existing resources.⁵⁸ For instance, in the first century B.C., Rome nearly collapsed due to the fighting among governors seeking to enrich themselves, contributing to chaos in the periphery. Emperor Augustus implemented a number of administrative reforms which recentralized the bureaucracy, giving it greater control over both money and arms (the wealthy province of Egypt became a possession of the emperor; Starr 1982).⁵⁹ To stem the European onrush, a declining Ottoman Empire adopted a series of domestic reforms, borrowing Europe's military technology and seeking to consolidate power in Istanbul (this era of reform is known as the Tanzimat).

Third, the state can strike a bargain with society, exchanging greater resource extraction for more social rights and benefits (Levi 1988; Lamborn 1991). In doing so, the state can defuse societal opposition to increased resource extraction. For instance, the 1905-10 pension and welfare reforms in Britain were intended to offset the massive increases in extraction during the Boer War (Lamborn 1983, 130). Leaders have also extended suffrage in order to increase the rate of extraction for defense. Finally, to increase its capabilities, in the long term, the state might be able to generate additional

⁵⁸ Some argue that Soviet domestic reforms went too far and are responsible for the dissolution of the empire and its absolute decline in power. On French bureaucratic reforms in the 18th century, see Boshier (1970).

⁵⁹ According to Douglas North, the British Crown implemented more efficient capitalist property rights to generate additional revenue for war (1981).

resources, especially if the immediate military threat is not too great. The state can promote greater industrial productivity or industrial revitalization through macro-economic tools, which will raise societal wealth and increase the base from which the state can extract resources. At the extreme, through state-led development, the government can encourage industrial growth and restructure the economy (Trimberger 1978). This strategy of resource mobilization is highlighted by the Meiji Restoration in Japan and Stalin's Five Year Plans in the Soviet Union.

Accommodation

A second security strategy to restore the balance is a policy of accommodation. A strategy of accommodation involves concessions and compromises by both the rising and declining states and usually takes the form of arms limitation and arms control agreements. A declining hegemon will seek accommodation with some or all of the rising contenders in order to slow down the emerging states' rate of ascent (militarily and economically) and to reduce the costs associated with hegemony.⁶⁰ While such agreements are difficult to reach, both rising and declining states have an incentive to strike a deal. In offering concessions, the declining hegemon's intention is two-fold. First, the hegemon intends to increase its immediate security by slowing down the challenger's rate of military buildup and/or limiting the type of weapon systems without the costs of a preventive war (negotiations might even generate divisions in the other's society, slowing down the momentum of its procurements). A declining hegemon will

⁶⁰ I avoid using the term appeasement because it has a negative connotation. It is often used to mean unilateral concessions and the "cowardly surrender under the threat of force." Historically, Britain used a strategy of appeasement to balance its capabilities and commitments. Kennedy defines it as "the policy of settling international (or, for that matter, domestic) quarrels by admitting and satisfying grievances through rational negotiation and compromise, thereby avoiding the resort to an armed conflict which would be expensive, blood, and possibly very dangerous" (1983, 16). Also, on British appeasement, see Schroeder (1976b); Watt (1965a); Walker (1980); Coughlan (1972); Richardson (1988).

also be more secure if it can eliminate certain offensive weapons (especially if offense is or is thought to be relatively easy, allowing states to expand at low cost, while defense dominance will make conquest more costly; Jervis 1978) or channel the arms race away from areas of weakness or towards areas of strength. Second, the hegemon can safeguard its economic staying power by reducing the demands on its resources to a level that it can readily afford. By limiting a rising contender's military buildup (especially by avoiding a costly arms-race), the hegemon might be able to maintain its regional military superiority without significantly increasing its military expenditure. At the very least, a strategy of accommodation might buy time for the declining hegemon to rearm at a more moderate pace or slow down the rising state's rate of industrialization.

For the rising contender(s), its incentive to accept these concessions is that it can satisfy some of its demands without the fear of a preventive strike from the declining hegemon. An emerging challenger will seek to avoid a preventive war while it is vulnerable to attack because it will be pushed down its power trajectory. In fact, a rising state might concede to such an agreement in order to buildup its military without the fear of attack (and with the intention of cheating on the accord once it is no longer vulnerable). The more the rising challenger fears that the hegemon will launch a preventive strike, the more the contender is likely to strike a deal with the declining state (and the more of its demands it is willing to concede in the agreement).⁶¹ An emerging state's demands might include recognition of special interests in the locale, treaty revision, and/or limited military buildup.

The kind of concessions most acceptable to the declining hegemon are those that impede the further increase in the military power of the rising contender(s). The most

⁶¹ Consequently, a declining hegemon can increase its bargaining power if it appears willing and capable of launching a preventive strike.

common forms of accommodation are arms limitation agreements and settlement of regional differences. First, through arms limitation and arms control agreements, the declining hegemon can channel a military buildup away from its strengths. For instance, historically Britain viewed naval supremacy in battleships as necessary to protect its extensive sea-lanes of communication (in fact, Britain maintained a Two-Power Standard, meaning that its navy would be larger than the next two navies combined). To discourage German battleship construction, in 1935 London negotiated a naval agreement with Germany which allowed Berlin to buildup its fleet to no larger than 35 percent the size of the British surface fleet. For Germany, this meant that it could increase its fleet without the fear of a preventive strike, and for Britain it assured adequate defense at home, while providing for a sufficient naval force to be sent to Singapore in the event of war with Japan in the western Pacific. Second, through an arms limitation agreement, the declining hegemon can limit the military spending of the rising contenders to levels that the hegemon can afford. In the long run, the declining power might even reduce its rate of military spending. For instance, the Washington Naval Agreement (1922) reduced the likelihood of a costly and unrestricted naval race between Britain, the United States, and Japan. More recently, the SALT treaties reduced the chance of a costly arms race between the United States and the Soviet Union. Third, through negotiations and discussions, the rising and declining states can reduce the risk of a costly war over the locale. For instance, in 1904, Britain settled a number of colonial disputes with France and in 1907, Britain reached a similar settlement with Russia. More recently, Nixon's opening to China reduced the potential threats to American interests in the Far East (Huntington 1987/88). In reducing the risk of war or the likelihood of a costly arms race, diplomacy can lighten the unbearable burden of preparation for war against several major enemies in disparate parts of its empire.

Devolution of Regional Hegemony

Finally, a hegemon can pursue a strategy of devolution of regional hegemony in order to restore the balance between capabilities and commitments. A strategy of devolution entails ceding leadership over a region to an emerging state or a regional surrogate power. The hegemon's intent is to reduce its international commitments and associated costs to a level that it can sustain without significantly increasing its rate of resource extraction. The hegemon can concentrate the freed-up resources in its remaining commitments, further reducing its defense spending, while investing the peace dividend at home. In devolving hegemony, the successor and not the declining hegemon, will bear the political, economic, and military costs of regional governance. Consequently, the declining hegemon might assist the rising state, accelerating the contender's rate of ascent in order to hasten its own retrenchment from the locale. This strategy is continuous, meaning that the amount of responsibility and the rate at which it is transferred will vary across regions. The transfer of leadership can be informal such as Britain's transfer of leadership over the Americas to the United States around the turn of the century, or formal, such as Britain's 1912 Naval Agreement which ceded leadership over the Eastern Mediterranean to France.

In addition to devolving hegemony to an emerging liberal contender, the declining hegemon can lower the costs of hegemony by building up a regional surrogate. A regional surrogate is a state that is not powerful enough on its own to dominate the locale. In creating and maintaining the regional surrogate, the great power will continue to have leverage over the surrogate's behavior. Mark Gasiorowski defines surrogacy as "a mutually beneficial, security oriented relationship between the governments of two

countries that differ greatly in size, wealth, and power" (1991).⁶² However, the declining hegemon must provide substantial assistance to the surrogate. This strategy is exemplified by the Nixon Doctrine, which entailed building Iran and South Vietnam to police U.S. interests in the Persian Gulf and Southeast Asia, respectively, and the bolstering of Israel in the Middle East (Osgood 1973; Organski 1990).

There are a number of important differences among these security strategies for redressing the discrepancy between resources and commitments. First, these strategies restore the balance in different ways. A strategy of extraction restores the balance by increasing military capability. In contrast, working from the other side of the equation, accommodation and devolution restore the balance by lowering the costs of hegemony. In the case of accommodation, this is done by slowing the military buildup of the emerging contenders through concessions and compromises. The declining hegemon does not cede regional leadership, but maintains its global commitments and the associated costs, albeit at a lower level. In the case of devolution, the declining hegemon lowers the costs of hegemony by reducing its global commitments, ceding regional hegemony to an emerging contender or regional surrogate. In devolving leadership, the declining state no longer bears any of the costs of regional hegemony in the locale.

Second, these foreign policy strategies encompass different responses to encroaching contenders. In increasing its rate of resource extraction, a declining hegemon's intention is to strengthen its immediate military capability in order to deter emerging contenders from challenging its hegemonic position, and to prepare for preventive war in the event that deterrence fails. In contrast, accommodation is intended to slow down the rising states' rate of ascent, but without the costs of a military buildup. Finally, in the case of a strategy of devolution, there is no notion of preparing for war or

⁶² On Rome's use of client states, see Luttwak (1976).

even slowing down a rising state's ascent. In fact, in contrast to a strategy of extraction, the declining hegemon might buildup the emerging power, accelerating its rate of ascent. The hegemon's intent is to hasten the contender's ability to perform the responsibilities associated with regional hegemony, allowing the declining hegemon to retreat from the locale sooner.

Balancing Capabilities and Commitments: The Dilemma of Strategy and Finance

The grand strategy of a declining hegemon is concerned with remaining in the ranks of the great powers as long as possible. As a great power, the declining hegemon can continue to shape the rules of the game in order to protect its existing commercial and security interests. Facing emerging contenders in disparate parts of its empire, one factor which will shape how the hegemon can restore the balance and how long it can remain in the ranks of the great powers is its foreign commercial policy. In particular, while in the short term both liberal and imperial hegemons can select from a range of security strategies which will accelerate or decelerate their rate of decline, in the long run, a liberal hegemon can retain its great power position longer than if it was an imperial hegemon. However, this requires that the liberal hegemon select its optimal security strategy.

Imperial Hegemon

The nature of an imperial hegemon's foreign commercial policy will restrict and constrain its range of policy options to either a strategy of accommodation or resource extraction (see Table 2). An imperial commercial policy will exclude the strategy of devolution because it will accelerate the hegemon's rate of decline over its alternative options. In particular, an imperial hegemon will not differentiate among challengers because both liberal and imperial contenders will pose a threat to its national interests. First, in devolving hegemony, the imperial hegemon will undermine its commercial

interests. The rationale is that an emerging liberal contender will replace the existing closed door order with an open door commercial arrangement, while an emerging imperial contender will replace it with its own exclusive order. Second, in devolving leadership, an imperial power will undermine its national security by strengthening the war-making capacity of a future rival. Thus, a declining imperial hegemon will eliminate a strategy of devolution from its range of foreign policy options.

Restricted to a strategy of accommodation or extraction, one factor which will influence an imperial hegemon's choice is its domestic flexibility. Domestic flexibility is a hegemon's ability to restore the balance by increasing its rate of resource extraction or reducing its global commitments. The presence of domestic economic or political constraints will exclude a strategy of societal resource extraction. Economic constraints include insufficient economic or material resources (i.e., commitments exceed available domestic resources), while political constraints include barriers to domestic resource extraction or retrenchment by societal actors or state fiscal managers (even if the hegemon has sufficient economic resources; for a complete discussion, see Chapter 1). For a constrained hegemon, a preventive strike to weaken or destroy any of the rising contenders is especially dangerous because the hegemon will lack the economic resources in the event a costly and protracted war ensues, and will lack the military capability to defend its remaining commitments if challenged in other locales or on other fronts simultaneously (unless the hegemon can build a reputation of harsh retaliation cheaply).

Facing numerous emerging challengers on different fronts and unable to reduce its global commitments, a **domestically unconstrained imperial hegemon's** best short run strategy to restore the balance between its capabilities and commitments is to increase its military capability in order to outpace the military buildup of the emerging contenders over its alternative option of accommodation. In increasing its rate of military spending,

the declining hegemon will have sufficient military capability to deter challenges, and in the event that deterrence fails, to launch a preventive war while the challengers are still too weak to mount a serious threat (in contrast to the globalist literature, based on a differentiated framework of world politics, the declining hegemon might have to fight several preventive wars in different parts of its empire, possibly simultaneously). If increased extraction or even a costly preventive war can discourage other would-be contenders (in the same locale, in other parts of the hegemon's empire, or future challenges), then a strategy of extraction is a cost-effective investment, especially if the hegemon can create a reputation for retaliation.⁶³ Under this condition the hegemon will rarely need to resort to a costly preventive war.

The failure of a domestically unconstrained imperial hegemon to increase its defense spending while maintaining its global commitments will endanger the declining hegemon's immediate national security interests. A disequilibrium between the declining power's military capability and its global commitments is especially dangerous because this imbalance will tempt rising states to challenge the declining hegemon's leadership. Alternatively, since both liberal and imperial contenders will pose a threat, the declining imperial hegemon cannot concentrate or redistribute its existing military forces without weakening its position in the locale (which will tempt rising states to capitalize on its temporary vulnerability). Finally, there are political costs for leaders in the declining hegemon if the state is caught unprepared for war. Under this condition the political elite will be accused of leaving the empire exposed to external challenge.

While ensuring that the unconstrained imperial hegemon remains in the great power game longer than its alternative options, in the long term, indiscriminate and

⁶³ See the literature on the chain-store paradox, Selten (1978); Fudenberg and Tirole (1991); von Hohenbalke and West (1986); Milgrom (1982); Rosenthal (1981).

prolonged societal extraction in preparation for war against several different emerging contenders (especially during peacetime) will undermine the hegemon's economic base for future military spending, accelerating its fall from the ranks of the great powers. In the long term, even a preventive war is unlikely to deter emerging liberal and imperial challengers permanently, forcing the hegemon into an upward spiral of ever-increasing extraction (in fact, liberal challengers pose a greater threat because of their greater ability to collude). First, as Gilpin (1981) and Kennedy (1987) warn, excessive and sustained peacetime military expenditure will divert resources from domestic investment, limit future economic growth, and erode the economic base of the declining hegemon to construct and maintain a modern military force. In particular, too heavy of a burden on the economy cannot be borne indefinitely without ruining the declining state's future capacity to create a modern military. For instance, in the case of imperial Spain, prolonged levels of domestic resource extraction contributed to Castile's lag in growth industries of the period such as textiles, metallurgy, and shipbuilding. The consequence of deindustrialization was that Spain could not keep pace with the combined naval construction of three emerging contenders, Madrid could not afford to supply enough horses for its army of Flanders. More recently, some argue that America's policy of "peace through strength" forced the U.S.S.R. into an arms race, undermining its productive strength, the source of its military power in the long run. At the extreme, in 1916, Germany embarked on the "Hindenburg Program" which entailed converting almost the whole of the German industrial system to munitions production. The result was the short term increase in production at the price of making certain that the German wartime economy would collapse in a few years, undermining its ability to field a large military force (Barnett 1976, 13).

Second, prolonged defense spending in peacetime will drain the country's war chest, which it will need to mobilize during wartime. For instance, Britain's leaders viewed England's fiscal strength and economic stability as "fourth arm of defence" on which the other three arms (and traditionally Britain's allies) depended. Britain's Exchequer feared that excessive taxation and/or borrowing during peacetime would drain its war chest, leaving little room for expansion during wartime (Peden 1979a; Shay 1977; Parker 1975). Finally, excessive taxation might provoke social unrest and domestic instability, especially if certain groups feel they have been unfairly targeted or if there is a decline in the country's standard of living. Louis XVI's attempt to levy higher taxes contributed to the French Revolution, Philip IV's attempt to increase taxes in Catalonia and Portugal resulted in a revolt (1640), and the strain of excessive extraction during World War I contributed to revolution in Russia (1917) and Germany (1919).

Table 2.--Outcomes

Hegemon	Security Strategy	Outcome
Constrained Imperial	Accommodation -concessions/compromises -slow military/economic ascent emerging contenders	fiscal strength > national security
Unconstrained Imperial	Extraction > Accommodation -outpace military buildup emerging contenders -prepare for preventive wars	national security > fiscal strength
Constrained Liberal	Devolution > Accommodation -retrench, liberal contenders -standfirm, imperial contenders	safeguard fiscal strength & national security
Unconstrained Liberal	Devolution > Extraction > Accommodation -retrench, liberal contenders -standfirm, imperial contenders	safeguard fiscal strength & national security

Facing numerous emerging challengers on different fronts and unable to reduce its global commitments or increase its rate of societal resource extraction, a **domestically constrained imperial hegemon's** only strategy to redress the balance between its capabilities and commitments is to lower its costs of hegemony by a foreign policy of accommodation.⁶⁴ The more domestically constrained an imperial leader, the more it is willing to reach an accommodation with a potentially hostile rising challenger. For an overextended state that cannot reduce its foreign obligations or increase its fiscal and military capability, there are several benefits of a strategy of accommodation. First, through concessions and compromises, a strategy of accommodation will slow-down the rising states' ascent and lower their military buildup, allowing the constrained hegemon to reduce the immediate demands on its military and economic resources to a level that it can afford with its existing rate of resource extraction. By convincing some/all of the rising contenders to reduce their military spending (and preventing a costly arms race), the declining hegemon can lighten the unbearable burden of preparing for a preventive war against several different rising challengers, husbanding its economic power in the event of a protracted conflict. If war never comes, then the hegemon will not undermine its economy with excessive and prolonged military spending. As one author summarizes in the case of Britain, "the balance struck between defensive strength and economic stability in 1937-1939 at least allowed Britain to survive the initial Nazi onslaught, and to have the financial credit to draw upon the considerable resources of the Empire and

⁶⁴ The declining hegemon might also rely on cheaper forms of power in order to lower its costs such as nuclear weapons in the modern era. On intertemporal issues, especially the choice between short term and long term interests, see Stein (1990).

Commonwealth during the war" (Peden 1984, 26). At the minimum, accommodation might postpone a showdown until more favorable circumstances prevail.

Second, accommodation can enhance the declining hegemon's immediate security by slowing down the challenger's rate of military buildup, eliminating destabilizing and offensive weapons, or directing an arms race away from the hegemon's weaknesses or towards its strength, without the costs and risks of a preventive war. In either case, concessions will delay the rising state's ability to launch a preemptive strike, allowing the constrained hegemon time to prepare for a preventive war at the moderate pace dictated by domestic economic and/or political constraints. Third, a strong economy and a large war chest might deter rising contenders from challenging the declining power's regional leadership. For instance, during the interwar period, Prime Minister Chamberlain believed that Britain's fiscal strength meant that it possessed superior war potential relative to Germany, Japan and Italy. Consequently, these challengers would be deterred from attacking since any conflict would become a protracted war, which Britain would likely win.⁶⁵

While increasing its immediate security and safeguarding its fiscal strength, in the long run, in accommodating some or all of the rising challengers, a domestically constrained imperial hegemon will erode its national security interests. First, decision-makers in emerging liberal and imperial contenders are unlikely to accept a permanent position of inferiority in the locale. The rationale is that both liberal and imperial contenders prefer a different commercial arrangement than the existing regional order. In the long term, since accommodation is unlikely to achieve their final objective, rising states will see preemptive war as inevitable. Elites in rising powers will see the passage

⁶⁵ Consequently, Chamberlain's goal was to prevent defeat by a knock-out air strike. By insuring that Britain could not lose a quick war and would win a prolonged conflict, the emerging challengers would be deterred from attacking. For more detail, see Chapter 3.

of time as working against them since the longer the declining state can avert conflict, the more time it has to prepare for war, becoming an even more formidable opponent. Consequently, an emerging contender's rationale for moderating its behavior and agreeing to such an accord is to buildup its capability in preparation for a preemptive war, without the fear of a preventive attack (i.e., during its window of vulnerability). As the emerging contenders encroach on the declining hegemon, they are likely to cheat or repudiate any agreement that condemns them to a permanent junior position in the locale. Less maliciously, a state might interpret an agreement as suited to its own interests. In either case, the outcome is that once the agreement (formal or informal) between the rising and declining states breaks down, or some or all of the rising states cheat on the accord or repudiate it, the declining hegemon will have insufficient capabilities to defend its imperial commitments, leaving it weak, vulnerable, and exposed to preemptive attack across its empire.

Second, accommodation might signal the declining leader's growing weakness and undermine its external appearance of strength. Prestige can deter contenders from challenging the hegemon's regional leadership, while perceived weakness will embolden the challengers, making them more aggressive in their desire to expand. Accommodation might even encourage other rising states to challenge its leadership position or damage the declining power's credibility and reputation to defend its remaining foreign commitments (Huth 1988). Thus, while increasing the declining hegemon's immediate security without extracting significant additional resources, a strategy of accommodation risks undermining the hegemon's long term national security interests. More generally, the problem for a declining imperial hegemon (constrained and unconstrained) is that it can only select from a range of security strategies that will either erode its political economy or its national security. In the long run, in favoring fiscal or security concerns

over the other, the hegemon will accelerate its decline from the ranks of the great powers to a second rate regional power.

Liberal Hegemon

The nature of a liberal hegemon's commercial policy will include the foreign policy strategy of devolution of regional hegemony. In the short run, a **liberal hegemon's** best security strategy for restoring the balance between its capabilities and commitments is to lower the costs of hegemony by devolving regional leadership over its alternative options of accommodation or extraction (depending on its domestic flexibility).⁶⁶ In contrast to imperial hegemons, due to the nature of its foreign commercial policy, a declining liberal hegemon can differentiate between liberal and imperial contenders, viewing only imperial contenders as a threat to its national security objectives and commercial interests. For this reason, the declining hegemon can devolve leadership to rising liberal contenders while standing firm in regions with rising imperial challengers (and going to war if necessary) without eroding its fiscal strength or national security interests. In devolving leadership to liberal contenders, the declining hegemon will retain access to its traditional markets, investments, and sources of raw materials in the locale without the burden of any of the economic, political, and military costs associated with regional hegemony. These costs will be borne by the new regional successor. Consequently, instead of retarding the ascent of rising contenders as realism would suggest, the liberal hegemon can assist emerging liberal contenders, accelerating their rate of ascent, in order to hasten its own retreat from the locale, further lowering its

⁶⁶ Similar to Friedberg's argument (1988), Nye argues that retrenchment can weaken a great power's global position. Nye states that, "policies of retrenchment are premature, and, ironically, they could produce the very weakening of American power they are suppose to avert" (1990, 4). Haas makes a similar argument (1988).

costs. The declining hegemon can either redistribute the freed-up resources to other regions (with imperial challengers), further reducing its defense costs, or invest this peace dividend at home in order to promote economic growth (however, if the peace dividend is used simply to increase government spending on entitlement programs it will not contribute to long term economic growth).⁶⁷

In the long run, in devolving regional leadership, the liberal hegemon can protect its fiscal strength and its national security interests, remaining in the ranks of the great powers longer than as an imperial hegemon. First, in devolving leadership the declining hegemon will safeguard its economic staying power. By concentrating the freed-up resources in its remaining commitments, the declining hegemon will not need to increase significantly its rate of resource extraction for military spending in order to match a challenger's buildup (and actually may be able to reduce its defense budget). In the long term, the hegemon will have the economic base to create and maintain a modern military, and to fight a preventive war if necessary. For this reason, Britain's Exchequer maintained England's fiscal strength was the third leg of defense.

Second, in devolving regional leadership to a rising liberal challenger, the declining liberal hegemon will safeguard its national security interests.⁶⁸ Once the new liberal successor assumes hegemony, it will not use its military capability to close-off the locale or capture any of the erstwhile liberal hegemon's remaining commitments. Consequently, the liberal hegemon might assist in the buildup of an emerging liberal contender, accelerating the rate of its retreat from the locale in order to lower the costs of

⁶⁷ On this point, see Friedberg (1991).

⁶⁸ See Solingen's (1994) distinction between liberalizing and inward looking coalitions, or Rosecrance's trading state (1994, 1986). On the concept of the Manchester Liberals, see Blainey (1988, 18-34). It should be clear, my emphasis is on shared commercial liberalism between the rising and declining states, not political liberalism, see Doyle (1983, 1986b); Schweller (1992).

hegemony. In fact, failure to devolve hegemony to a liberal contender, even in a strategic locale, means that the declining liberal hegemon risks undermining its economic staying power by prolonging excessive defense spending. While in the long run, there is always the risk that a liberal successor will revert to an imperial hegemon, this risk must be weighed against the dangers associated with the alternative strategies of extraction and accommodation.

In devolving hegemony, a declining liberal hegemon will protect its fiscal and security interests, remaining in the ranks of the great powers as long as possible for the hegemon. First, in the short term, in selecting a security strategy of devolution the liberal hegemon will decelerate its rate of decline over its alternative security strategies of extraction or accommodation (as discussed above, extraction will erode its long term productive strength, while accommodation will undermine its national security interests). Second, in the long term, in selecting a liberal foreign commercial policy, it will decelerate its decline over its alternative commercial policy. Thus, as a liberal hegemon, the declining power will ensure that it has greater economic and military capability to continue to influence the rules of the game in order to protect its existing national interests. However, an imperial hegemon which selects its optimal strategy can remain in the ranks of the great powers as long as if it was a liberal hegemon which selects a suboptimal strategy.

A declining liberal hegemon that faces only emerging imperial challengers will suffer the same long run fate as a declining imperial leader. Unable to devolve regional leadership, depending upon its domestic flexibility, it can either increase its rate of resource extraction or pursue a strategy of accommodation. Consequently, this liberal hegemon will either erode its fiscal strength or its national security, accelerating its decline from the ranks of the great powers. One implication is that a liberal hegemon has

an incentive to assist in the rise of liberal contenders and to encourage the spread of commercial liberalism in order to ensure that it can devolve leadership to liberal contenders.

A foreign policy of devolution contradicts the expectations of realism. In retrenching in regions with liberal states and standing firm in regions with imperial challengers, the declining liberal hegemon is likely to retreat from some highly strategic regions while standing firm in less valuable locales. In contrast, according to the realist strategy of devolution, as a hegemon declines, concerned that the challenger will accumulate power dwarfing its own military capabilities, the declining state will retrench only in areas of lesser strategic worth. The rationale is, (1) "loss" of a valuable locale can tip the delicate balance of global power against the declining hegemon and ultimately threaten its survival (by allowing the rising state to assemble greater economic and military capacity than the declining state), and (2) retrenchment from less vital regions will have little if any impact on the global balance. Consequently, for realists, irrespective of costs, the declining hegemon should only trim its commitments in peripheral regions.

The problem with the realist strategy for disengagement is that it risks accelerating the hegemon's fall from the ranks of the great powers. While realists recognize the importance of industrial capacity as a component of potential military capability, they ignore the fiscal consequence of balancing capabilities and commitments for the declining hegemon. In particular, failure to devolve leadership to a liberal contender in a strategic locale means that the liberal hegemon risks undermining its economic staying power by prolonging excessive defense expenditures (consequently, contrary to realism, a declining liberal hegemon might assist in the rise of liberal contenders, even in strategic locales, in order to hasten its retreat from the locale, further

lowering the cost of hegemony). In eroding its fiscal strength, the hegemon will undermine its productive strength and ultimately its ability to create and maintain a modern military force, reducing its influence over the international system.

In summary, the goal of a declining hegemon is to stave-off falling into the ranks of the second-tier powers as long as possible. As a great power, the declining hegemon can continue to influence the international system in order to advance its existing commercial and security interests. Facing emerging contenders for regional hegemony, a declining hegemon's foreign commercial policy will shape how it restores this balance and how long it can remain in the ranks of the great powers. While in the short term, both liberal and imperial hegemonies can select from a range of strategies which will accelerate or decelerate their rate of decline, in the long run, a liberal hegemon can select a security strategy which will allow it to remain in the great power ranks longer than as an imperial hegemon.⁶⁹ The rationale for these outcomes is that only a liberal hegemon can select a strategy of devolution, safeguarding its fiscal strength and its national security. In contrast, imperial hegemonies can only select from a range of options which will either erode their fiscal or security interests; they cannot find an equilibrium strategy. The consequence is that only a liberal hegemon might remain in the ranks of the great powers as long as possible for the given state. In particular, a hegemon risks accelerating its decline from the ranks of the great powers in two ways, (1) in the short term, in selecting a suboptimal security strategy and (2) in the long term in selecting a suboptimal foreign commercial policy. Consequently, a declining imperial hegemon which selects its optimal security strategy can remain in the ranks of the great powers as long as if it was a liberal hegemon which selects a suboptimal strategy. However, only a liberal

⁶⁹ Once more, a liberal hegemon which adopts an imperial commercial policy will accelerate its rates of decline over remaining a liberal hegemon, while an imperial hegemon which adopts a liberal foreign commercial policy will decelerate its rate of decline in relation to remaining an imperial hegemon.

hegemon which selects a strategy of devolution can remain in the ranks of the great powers as long as possible for the given state.

However, some scholars argue that a declining hegemon might select to jump into the ranks of the second-tier powers. The hegemon will give-up its great power standing and the associated responsibilities because the costs are not worth the benefits (Jervis 1993). Yet, as a second rate power, the erstwhile hegemon will have limited influence, leaving it dependent on the remaining great powers to protect its national interests.

Conclusion

The import of this work is that it highlights the relationship between economic and security policies. In shifting from a hegemonic to a multipolar distribution of power, the goal of a declining hegemon is to remain in the ranks of the great powers as long as possible. As a great power, the former hegemon can continue to create an international environment which advances and protects its existing commercial and security interests. In falling from the ranks of the great powers to a second rate power, the erstwhile hegemon's influence in the international system will also decline, becoming regional or even local in nature. As a second tier power, the former hegemon's influence will be limited, relying on the remaining great powers to protect its national interests.

In the short term, facing emerging contenders on disparate fronts, declining hegemon's have a strategic choice in how to restore the balance between capability and commitments. Both imperial and liberal hegemon's can select security strategies which will accelerate or decelerate their rate of decline. For instance, an unconstrained imperial hegemon which selects devolution or accommodation will accelerate its rate of decline over its alternative strategy of extraction, while a constrained imperial hegemon which chooses devolution will accelerate its rate of decline over its foreign policy options of

accommodation (conversely, in selecting their optimal strategies, these hegemons will lengthen their tenure as great powers). Similarly, a declining liberal hegemon will accelerate its rate of decline in selecting either a strategy of extraction or accommodation over a policy of devolution (again, in selecting a strategy of devolution, the hegemon will lengthen its tenure as a great power). Thus, only a declining liberal hegemon can remain in the ranks of the great powers as long as possible in relation to its alternative options.

In the long run, while decline from the ranks of the great power is inevitable, a declining liberal hegemon can remain a key player in the great power game longer than if it was an imperial hegemon. The reason is that in selecting how to balance its capabilities and commitments, decision-makers must consider both the financial and security ramifications of a foreign policy strategy. Favoring either economic or security concerns will hasten the hegemon's fall from the leading states to a second rate regional power. However, only a liberal hegemon can select a foreign policy strategy of devolution which will safeguard both its fiscal power and its national security interests. In remaining in the ranks of the great powers, the declining liberal hegemon will continue to be able to shape and influence the nature of the international system. Yet, a liberal hegemon must devolve hegemony to rising liberal contenders, even in strategic locales, or risk undermining its fiscal strength. In contrast, although aware of the dangers of its foreign policy alternatives, an imperial hegemon can only select from a range of strategies which will undermine either its long term fiscal strength or erode its national security interests, contributing to its fall from the ranks of the great powers to a second rate power.

The implication for policy makers in a declining liberal hegemon is that they should resist domestic pressure to adopt a protectionist economic policy. In losing market shares to foreign competition, some domestic producers will call for sweeping protectionism under the assumption that this strategy will slow down or reverse the

hegemon's rate of decline. However, an imperial commercial policy will restrict the hegemon's range of security options for managing its decline to either a strategy of increased resource extraction or accommodation, accelerating its fall from the ranks of the great powers in the long run. In contrast, a liberal commercial policy will mean that the hegemon can manage its decline by devolving regional hegemony, lengthening its tenure as a key player in the great power game in relation to imperial hegemons.

CHAPTER 3

THE NEW COURSE IN BRITAIN'S FOREIGN POLICY: DEVOLUTION OF REGIONAL HEGEMONY (1889-1912)

In the sixty or so years after the Napoleonic wars, Britain came to dominate many of the regions of the globe. These spheres of formal and informal influence included the Far East, especially China; central Asia, including the "Jewel in the Crown," India, and the buffer territories of Persia and the Gulf, Afghanistan, and Tibet; the Mediterranean (the Straits of Gibraltar and the Turkish Straits); southern and eastern Africa; Central and Latin America. Finally, while not dominating Europe, Britain was also the historic balancer on the Continent. To defend its far-flung interests, Britain's Royal Navy commanded the high seas as well as most of the strategic sea-lanes of communication. As Admiral Fischer gloated, "five keys lock up the world. Singapore. The Cape. Alexandria. Gibraltar. Dover. These five keys belong to England, and the five great fleets of England will hold those keys!" Britain's naval supremacy was supported by an extensive global network of coaling and cable stations and naval bases.

However, by the last decade of the nineteenth century, both new and old contenders for regional hegemony, including the United States, Russia, France, Germany, and Japan, were ascending, at different rates and in disparate parts of Britain's formal and informal empire. First, most of these emerging states were encroaching on, and in some

instances, surpassing, Britain's industrial lead. Second, the weakening and disintegration of a number of historic empires encouraged a "scramble for empire" in or near many of Britain's traditional spheres of influence. Finally, many of these rising states more than doubled their warship tonnage in the three decades before World War I (Germany actually tripled its navy), challenging Britain's traditional naval supremacy.⁷⁰ Even more threatening, a combination of these navies would soon outnumber the Royal Navy.

In encountering these ever-more powerful rising competitors, the dilemma for Britain's decision-makers was how to restore the balance between its military capability and its global interests, while at the same time protecting its fiscal strength and its national security interests. Britain's existing foreign policy called for Splendid Isolation. However, defending its global interests with its existing Two-Power Standard was dangerous because the naval construction in the United States, Germany, Japan, France and Russia meant that Britain's military capabilities would gradually become insufficient to protect its extensive empire (the Two-Power Standard called for Britain to maintain a fleet equal in size to the combined fleets of the next two largest navies). Britain's increasing vulnerability might tempt the emerging states to launch a preemptive attack, challenging Britain for regional hegemony. However, to keep pace with the naval construction of several rapidly-industrializing competitors would require Britain to constantly revise its Two-Power Standard. The danger of upwardly revising its Two-Power Standard to a three- or even a four-power standard was that excessive and sustained peacetime defense spending to protect its global interests would undermine

⁷⁰ Not only was the size of the navies increasing, so was the cost of defense. During this period, naval ships underwent a fundamental revolution in size, armor, guns, and speed. In 1905, First Sea Lord, Admiral Sir John Fisher's introduced the *Dreadnought*, which was faster, highly maneuverable, all big gun ship. Its introduction made earlier capital warships obsolete. The increase in the thickness of armored hulls, the size of ships, and heavier gun mountings greatly increased the cost of a battleship (see Kennedy 1991, 227-228; Sumida 1989, 20). The rapid revolution in technology meant that ships rapidly became out of date (Marder 1940, 123)

Britain's fiscal strength and eventually, Britain's military power. Finally, global retreat from its empire was dangerous because abandonment of strategic regions might add to the war-making capacity of future rivals, undermining Britain's national security interests.

Despite these challenges, Britain was able to manage its decline, remaining a key player in the great power game for another half-century. The nature of Britain's foreign commercial policy contributed to its success. As a declining commercially liberal hegemon, Britain was able to select a foreign policy strategy that safeguarded both its economic staying power and its national security interests. This chapter examines how Britain managed its decline and why this strategy was successful. The first section discusses the competitors which Britain encountered, rising at different rates and challenging its hegemony in disparate parts of its empire. The second and third sections focus on two debates that ensued among Britain's decision-makers over how restore a balance between the nation's military capability and global commitments. The final section discusses why Britain's leaders selected a foreign policy strategy of regional devolution of leadership over the alternative strategy of resource extraction and accommodation, and why this strategy succeeded.

The Emerging Contenders for Regional Hegemony: A Regionally Differentiated Framework of World Politics

Scholars who examine Britain's geo-strategic environment in the three decades prior to World War I often focus on England's position in a single region, The Americas, Europe, Central Asia, or the Far East. Having the largest navy in the world, had Britain confronted a single emerging contender, it could have concentrated its fleet from other parts of its empire, overwhelming the emerging challenger's. However, during this period, Britain confronted an emerging Germany, Japan, United States, Russia, and France, rising at different rates and in disparate parts of its empire. In over-simplifying

Britain's predicament, it is difficult to understand the dilemma that London faced in balancing capabilities and commitments while preserving its fiscal strength and national security interests.

First, Britain confronted disparate rising contenders for regional leadership across its empire.⁷¹ In the three decades before World War I, Britain faced intense industrial and naval competition from an emerging United States in Latin America, and especially in Central America; an emerging Japan, Russia, United States, Germany, and France in the Far East and Pacific; a rising Russia in Central Asia; a rising Russia, France, and Germany in the Middle East; an emerging France and Italy in the Mediterranean; and a growing France and Germany in Africa. Finally, although not in a hegemonic position in Europe, Britain also faced a rapidly rising Germany on the European continent.

Second, differential rates of industrial growth meant that contenders for regional leadership encroached at different rates across Britain's empire, with some states rising earlier and faster than others. The United States was the first power to surpass Britain in a number of key industrial sectors such as steel production, coal consumption, and energy use (Kennedy 1987; Hobsbawm 1987). In 1890, an emerging United States produced more steel than Britain (and by 1913 more steel than the rest of the great powers combined) and by 1900 the United States surpassed Britain in relative shares of world manufacturing. By 1900, Germany was the second power to eclipse Britain in a number of industrial sectors. While remaining a relatively backward power, Russia underwent rapid industrialization in the first decade of the twentieth century. Finally, although Japan did not enter the ranks of the great powers until after World War I, it greatly increased its industrial and military power during this period.

⁷¹ This section is based in part on: Barnett (1972); Marder (1961); Kennedy (1976); Taylor (1971); Holborn (1966); Beloff (1970); Neilson (1991); Mowat (1968b); French (1982).

Finally, Britain's regional leadership was challenged by rising contenders at different periods across these locales. In some cases, even the same rising contender challenged Britain's hegemony at different periods in different regions. As early as the 1870s, Russia began to pose a threat to Britain's interests in Central Asia, mainly India, and in the buffer states of Persia and Afghanistan (Yap 1987). In the mid-1880s, Britain confronted France in both Africa and southern China. By the early 1890s, and especially after the conclusion of the Franco-Russian alliance in 1894, both France and Russia began to encroach on Britain's naval supremacy in the Mediterranean, virtually forcing Britain to abandon its historic defense of the Turkish Straits for Alexandria. The scramble for empire in China did not begin in earnest until after the Sino-Japanese war in 1894-95 when Germany, Russia, and France carved out sections of the collapsing empire. Around the same time, the United States and Britain had a number of disputes in North and Central America, as America was attempting to exert greater control over events in its backyard. Finally, in Britain's homewaters, Germany did not become a major naval challenger until 1904.

The Americas: The United States

At the turn of the century, the United States was the primary rising power in the Western Hemisphere (Healy 1988; Poitras 1990; Pletcher 1984; Kurth 1982).⁷² With the close of the American frontier in the 1890s and the ascendancy of American industry, the United States began to focus its efforts on external expansion (economic, political, and military) in the Americas, one of Britain's more valuable spheres of influence. Highly dependent upon the import of raw materials and food, 20-25 percent of Britain's trade was

⁷² There is an extensive amount written on Anglo-American relations at the turn of the century. See for instance, Neale (1966); Campbell (1960); Allen (1954); Anderson (1981); Bourne (1967); Perkins (1968); Gelber (1938).

with central and Latin America (Doyle 1986a, 268; Platt 1972). In 1898, in its first major expansion outside of North America, the United States captured Cuba, Puerto Rico, and the Philippines from Spain (invoking the Monroe Doctrine, which pledged the United States to defend Central and South America against European expansion) and annexed Hawaii.

Britain's concern over an emerging United States in the Americas was two-fold (Bourne 1967; Barnett 1972; LaFeber 1963). First, Britain feared that the United States might invade Canada (Sarty 1990). Canada's long border with the United States was virtually indefensible.⁷³ In a land war, the United States would have shorter lines of communication, while supplies from Britain would require several months to arrive. Second, British leaders were concerned that a rising United States could threaten England's future access to its valuable trade with Central and Latin America. A large percentage of Britain's raw materials and food was imported from this region.

One of the most significant disputes between the United States and Britain was over the building of an isthmian canal in central America in the 1890s (either through Panama or Nicaragua; Grenville 1955).⁷⁴ In the Clayton-Bulwer Treaty of 1850, the United States and Britain agreed that neither state would build an isthmian canal exclusive of the other, nor limit the navigation rights of other powers in such a canal nor fortify it. However, near the turn of the century, American leaders began to push for a revision of the Clayton-Bulwer Treaty which would allow the United States to construct and defend an Isthmian Canal unilaterally. Britain's admiralty warned that an American-

⁷³ British leaders offered two strategies to defend Canada. First, the Crown could offset an American invasion of Canada by invoking a naval blockade, Britain's traditional tool of compellence, which would bring American cities to their knees. However, as in the case of Russia, the construction of an extensive railroad network (financed largely by British capital) reduced America's vulnerability to a prolonged naval blockade. Second, Britain could bombard American coastal cities.

⁷⁴ Other differences included the Alaskan and Canadian Yukon boundary dispute, the Venezuela border dispute with British Guinea (1895), and the Atlantic fishery.

controlled isthmian canal would allow the United States to quickly concentrate its Pacific and Atlantic Fleets, granting the United States maritime supremacy in the Western Hemisphere, and forcing Britain to buildup its Caribbean and Atlantic fleets.⁷⁵

The Far East: Russia, Japan, France, Germany

The Americas was only one of several spheres where Britain had to devote its resources. In the last decade of the nineteenth century, Britain came under heavy pressure to protect its commercial and political interests in the Far East from an emerging Japan, Germany, France and especially Russia (Nish 1966, 1977; Lowe and Dockrill 1972b; Monger 1962; Langer 1951). The cause of this "Scramble for China" was the internal decay of the Manchu Dynasty. Britain feared that the partition of China by these encroaching states would endanger its Open Door policy.

Japan's easy victory over China's larger army and navy in 1894-95 demonstrated the weakness of the Manchu Dynasty, inviting a scramble for special concessions, leases, and exclusive spheres of influence in China among the emerging great powers. In 1896, Russia made the first move, securing rights to construct the Chinese Eastern railway across Manchuria, linking it to Vladivostok and its Trans-Siberian railway. In 1898, Germany acquired a naval base at Kiaochow for its newly formed Far Eastern squadron and extensive concessions in the Shantung Peninsula. Soon after, Russia persuaded China to lease the Liaotung Peninsula on the approach to Peking and Port Arthur (which Russia intended to use as an ice-free naval base for its expanding Far Eastern squadron).

⁷⁵ As one Admiralty memorandum stated "Without intruding on the political aspect of this question, - I would only remark that the construction of a successful canal through Central America would give an enormous advantage to the United States in future competition with England in trade with the Western coasts of America, and with China, Japan; and that I cannot therefore understand why Great Britain would be "desirous" of seeing it completed" (ADM 1/7550A).

In response, France acquired a naval base at Kwangchow-wan.⁷⁶ In 1900, Russia used the Boxer Revolt to make further inroads into China by occupying the entirety of Manchuria. In 1902, Russia agreed to evacuate its troops in stages by 1903; however, in 1903, Russia delayed its evacuation, seeking greater concessions from China (Seton-Watson 1967).

There were three residual effects of this scramble for China on Britain. First, the number and tonnage of warships in the region increased drastically. By 1901, there were a total of 12 non-British battleships in the region and more were under construction, Russia had five battleships and was building another three, France had one, and Japan had six and was building another battleship (Monger 1963). More threatening, the Dual Alliance would shortly thereafter outnumber Britain's Far Eastern squadron by five battleships. Second, as a land-power, Russia's new Trans-Siberian and Chinese Eastern railways would allow Russia to project its military power deep into the region, with little opposition from Britain's navy. Finally, in response to the encroachment of Russia, France, and Germany, and in the aftermath of the Triple Intervention, Japan sought to carve-out Korea as part of its sphere of influence (Nish 1966; Iriye 1989; Beasley 1987).⁷⁷

⁷⁶ Earlier, France sought to use its position in Siam, which was nestled between the French in Indochina and the British in Burma, as a jumping off point for the creation of a greater Indochina.

⁷⁷ In the aftermath of the Sino-Japanese war (1894-95), the Treaty of Shimonoseki called for China to recognize the independence of Korea (in the Chinese view, Korea was a vassal state of China, but Chinese authority was limited in practice), to cede to Japan the territories of Taiwan and the Pescadores islands, and to cede control over the Liaotung peninsula. However, to prevent these acquisitions by Japan, the Triple Intervention, consisting of Germany, Russia, and France, forced Japan to retreat from most of its demands on China.

Mediterranean: France, Russia, Germany

Since the opening of the Suez Canal in 1869, the Mediterranean served as Britain's primary commercial and military route to India and the Far East. Consequently, the bulk of Britain's navy was stationed in the strategic waters of the Mediterranean at Gibraltar and Malta, not in its homewaters. Beginning in the early 1890s and especially after the Franco-Russian Dual Alliance (1894), France and Russia's combined fleet threatened Britain's naval supremacy in the Mediterranean.

In the western Mediterranean, the death of Sultan Mulai Hassan in 1894 led to a scramble for Morocco, especially by France and Germany. Already in control of Algeria and Tunisia, France sought to complete its domination over North Africa by pursuing a policy of "peaceful penetration" into Morocco (Williamson 1969). However, Britain sought to preserve Morocco's independence for fear that if France came to occupy the Moroccan coastline, it could challenge Britain's passage through the Straits of Gibraltar.

In the eastern Mediterranean, Britain sought to preserve the sovereignty of the "Sick Man of Europe," the Ottoman Empire, against German and Russian partition (Brown 1984). Britain's traditional role in the region had been as protector of the Turkish Empire and defender of the Turkish Straits from Russian expansion. However, by 1890, Britain lost undisputed command of the eastern Mediterranean to Russia's Black Sea squadron. Fearing that Britain would not be able to defend Constantinople and the entrance to the Turkish Straits against a determined Russian invasion, by 1892, the Admiralty and the War Office called for abandoning Constantinople for Alexandria (in the event of war with Russia, France was unlikely to remain neutral; instead, the two countries would combine forces to eliminate Britain's Mediterranean fleet; Beloff 1987; Marder 1940).

Africa: France, Germany

Beginning in the 1890s, France and Germany steadily encroached on Britain's position in West and East Africa (Langer 1935; Louis 1971). In West Africa, France undertook a concerted effort to unify its scattered holdings straddling the Sahara into a single empire, stretching from the Congo to the Mediterranean. The danger of French expansion in Africa was heightened by the French Colonial Army's disregard for orders from Paris, especially in French Sudan.

In addition to West Africa, France challenged England's presence in Egypt and the Upper Nile (the Sudan). In 1896, France failed to gain German and Russian support in ending English occupation of Egypt (England had promised to evacuate Egypt once order had been restored). In the same year, France's Jean Baptiste Marchand led 130 soldiers to set claim to the Upper Nile, which would allow Paris to threaten Egypt's welfare. As one diplomat noted, "whatever Power holds the Upper Nile valley must by the mere force of its geographic situation, dominate Egypt" (Porter 1975, 162).

Central Asia: Russia

For Britain, India was the Jewel in the Crown. Lord Curzon wrote that "As long as we rule India we are the greatest power in the world. If we lose it we shall drop straight to a third rate power." In many ways, the British empire was a result of the need to protect the approach to India. Britain's dominance over the Mediterranean (Straits of Gibraltar, Malta) and the Suez Canal (Egypt), the Persian Gulf, Afghanistan, Tibet, Persia, southern Africa (the Cape, and east Africa) and even the Far East (Singapore and Burma) was linked to India's defense. Since this route was flanked by Russian power, the "Great Game" between Britain and Russia stretched from the Ottoman Empire to the Far

East, with Russia encroaching on the buffer states of Afghanistan, Persia, and Tibet (Gillard 1977; Mahajan 1982).

Britain did not intend to defend India on Indian soil, but in Afghanistan. As a result, Russia's annexation of Merv near the Afghan border in 1884, the conflict with Afghanistan in Panjdeh (even closer to the frontier) in 1885, and the possible encroachment on Herat, Afghanistan, was seen as a direct challenge to India (Kazemzadeh 1968). As a land-power, Russia's commencement in 1901 of construction of the Tashkent-to-Orenberg railway heightened Britain's fears of a Russian invasion of India even more. This line put the Russian railheads within 400 miles of Kabul, causing the British government in India to revise upwards the troop levels it would need to defend India against a Russian invasion.

Homewaters: Germany

As a late entrant in the colonial race, the German Reichstag approved Germany's First Naval Law in 1898 and two years later, the Second Naval Law of 1900 (Kennedy 1980). Britain's initial concern over German naval construction was that the Imperial Navy would tip the balance between Britain and the Dual Alliance. In the aftermath of the Triple Intervention and the Kruger telegram, there were new fears of the formation of a Continental Coalition against Britain. By 1904, Britain's admiralty argued that Germany would possess a battleship supremacy in the North Sea.⁷⁸

In summary, in contrast to the globalist perspective of decline, Britain's rate of decline was far from global, rapid, or simultaneous in nature. Had Britain confronted a

⁷⁸ Marder (1940) has found no evidence that the German threat caused any modification of British plans before 1904. He maintains that Britain's fleet distribution was a sign of changes in technology. New armored cruisers with greater speed, meant that ships did not need to be distributed widely across the globe. Modern telegraph systems meant that ships could be instantly signaled to steam towards a region.

single emerging contender, it could have concentrated its existing resources in the locale. Instead, in confronting an emerging United States, France, Russia, Germany, and Japan, which were rising at different rates and challenging its hegemony in disparate regions and at different points in time, Britain's leaders faced the impossible dilemma of balancing capabilities and commitments without eroding its economic strength or undermining its national security objectives.

Domestic Constraints on Britain's Foreign Policy Adaptability

Facing an emerging France, Russia, Japan, America, and Germany, one debate among Britain's policy elite focused on whether to restore the balance between its military capabilities and global commitments by increasing its rate of domestic resource extraction in order to increase its military capability.⁷⁹ The immediate cause of this debate was the failure of two large British naval construction programs (the Naval Defence Act and the Spencer Act) to deter the emerging contenders from challenging Britain's naval supremacy. The prospect of facing ever-increasing naval estimates to maintain Britain's command of the high seas and local naval supremacy in the Americas, the Pacific, the Mediterranean, and Britain's homewaters ignited a debate between the successive Chancellors of the Exchequer (the Treasury) and the navalists over Britain's ability to bear the increased government expenditure and taxation necessary for a three- or four-power naval standard. A lesser debate between the Conservative government and Liberal party focused on the capacity of particular groups to bear increased taxation. In the end, the Treasury Department's opposition to a strategy of ever-increasing resource extraction forced Britain to select an alternative foreign policy to manage its decline.

⁷⁹ For a detailed discussion of this domestic debate, see Friedberg (1988); Murray (1980); Emy (1972); Monger (1963); Kennedy (1976, 1981, 1983); Mallet (1913); Roseveare (1969); French (1982), Howard (1972); Steiner (1963); Boyce (1990); Sumida (1989).

Fiscal Orthodoxy and the Exchequer

The Treasury Department, as the watchdog over government finance, was responsible for striking a balance between the competing demands of government expenditure (civil and military) and maintaining the health of the economy.⁸⁰ In order to accomplish this goal, the Treasury was responsible for levying and creating new taxes as well as approving each department's annual budget estimate (see the Appendix for a discussion of the concept of Treasury Control). The intention of Treasury control over government expenditure was to ensure that a department's estimates were economical. As one Chancellor noted, "The function of the Chancellor of the Exchequer is to resist all demands for expenditure made by his colleagues, when he can no longer resist, to limit the concession to the barest point of acceptance" (Kynaston 1980).

The philosophy of the Treasury was steeped in the Gladstonian tradition of limited government expenditure on defense and social welfare, low taxation, minimal interference in the economy, and free trade. As part of this tradition, the Treasury and the military establishment accepted Britain's need to limit its military spending in peacetime. The rationale was that Britain's fiscal strength was a third leg of defense, upon which the other two legs (the army and the navy, and Britain's allies) would rely in the event of a prolonged conflict.⁸¹ Too much extraction in peacetime would divert resources from domestic investment, limit the scope of future economic growth, and ultimately undermine Britain's productive capacity to construct a modern military and to wage a

⁸⁰ Other advisers on government economic policy included the Bank of England and the City of London.

⁸¹ According to French, as the prospect of a continental war emerged, Britain would be the financial backer of the Triple Alliance (1982). A strong British economy would allow the allies to "sustain the burden of war while the enemy is rapidly consuming his resources."

prolonged war. In living beyond its means, the Treasury argued that Britain risked draining the financial war chest (its wealth and its international credit) which it would need to mobilize for war.

In peacetime, the Treasury's priority was to restore Britain's financial war chest by lowering direct taxes and repayment to the Sinking Fund.⁸² First, the Treasury's ability to levy direct taxes (taxes on income such as rent, profits, or wages) and indirect taxes (taxes on commodities such as alcohol, tea, and tobacco) meant that it could extract immense revenue on short notice. However, in peacetime, the Treasury opposed new or increased direct taxation for fear that it would leave little room for expansion during wartime. Low peacetime taxation translated into low civil and military expenditure. Second, in peacetime, the Treasury resumed repayment to the Sinking Fund (a debt repayment program). Debt repayment from previous wars to the Sinking Fund ensured that Britain could borrow large sums at relatively low interest rates during an emergency.⁸³ Each budget set aside a fixed amount for payments of the interest on past debt, and allocated a sum towards the Sinking-Fund for the redemption of the principal. The Treasury recognized that failure to meet past responsibilities would damage the nation's credit

⁸² According to E. W. Hamilton, "One of the principal reasons why there are such uneasiness and stagnation in the City is that the Government have been borrowers on so large a scale on account of the war and of the Transvaal after the war. The Money Market is suffering from a surfeit of Government stocks which in fact have never been properly digested. Digestion of these stocks, as also of other stocks of the gilt-edged order, like Municipal and Colonial Loans, must be a slow process; but, slow though the process may be, the difficulty would be surmounted in course of time, were further issues of a considerable amount not to be feared. Unfortunately, the Loan horizon is not clear" (T' 168/61).

⁸³ Permanent Under-Secretary of the Treasury, E.W. Hamilton warned that "I believe it is difficult to overrate the advantages which result from the maintenance of a considerable Sinking Fund. It not only gives great strength to our credit in times of peace, but it is an immense reserve in times of war. Indeed, the Sinking Fund constitutes our War Chest, and a War Chest administered in a much more scientific and much less wasteful manner than that of Germany. Its legitimate suspension in times of real emergency would enable us to raise, without any additions to taxation, over 200 millions. But in normal times to reduce seriously the amount devoted to redeem debt would, I believe, tell sensibly on our credit and on the financial position which we occupy in the eyes of the world; and any proposal which the Chancellor of the Exchequer might make in the direction of trenching upon the national Reserve Fund, opposed as such proposal would be to the best financial authorities, would be most difficult to defend" (PRO CAB 37/39/38).

rating, increasing the cost of borrowing during future crises. In protecting Britain's war chest, there was little room to increase its rate of resource extraction for military spending during peacetime.

Britain's income tax and high international credit rating meant that it had superior war potential over its continental neighbors (Emy 1972; D'Lugo and Rogowski 1993; Ferguson 1994; Kennedy 1983). First, Britain's Treasury had the power to levy and increase both direct taxes and indirect taxes, while most European governments could raise revenue only by indirect taxation. In the case of Germany, only state governments (not the Reich) could raise direct taxes. Consequently, much of Germany's spending on the navy during the Anglo-German naval rivalry had to be financed through loans. In France, public spending was financed by indirect taxes and stamp taxes, and a high level of borrowing, while in Russia, the government relied on revenues from taxes on consumption and railways, and on foreign capital. Second, Britain's management of public debt meant that the government could borrow large sums of money at relatively low interest rates. In contrast, the Continental states tended to borrow on the money-markets, even in peacetime, in order to cover the gap between expenditure and revenue. The result was a high national debt and higher interest rates. Thus, while the combined economic resources of Britain's neighbors were greater than its own, Britain's capacity to extract revenue was much greater than the continental powers' (Kennedy 1989; Ferguson 1994; Sumida 1989).

In summary, in peacetime, the rules of finance dictated that the Exchequer balance the nation's revenue and expenditure, restricting Britain's rate of domestic resource extraction for military and social spending. Since deficit spending was considered impossible over the long run, options to balance the budget included new or increased direct and/or indirect taxes, government borrowing, suspension of debt repayment to the

Sinking Fund, or a reduction in government expenditure for military and civil programs. Of these options, the last choice was the least problematic for the Treasury. Consequently, Britain was politically constrained, not economically constrained, in its ability to extract resources. The difference is that while Britain had a large war chest which it could have used to increase its military capability, domestic fiscal managers opposed a strategy of resource extraction during peacetime.

Domestic Politics (1889-1912)

The Naval Defence Act and The Spencer Act

Beginning in the late 1880s, both old and new contenders for regional leadership initiated naval construction programs, encroaching on Britain's traditional naval supremacy. Britain's initial response was to increase its rate of resource extraction for naval construction (Naval Defence Act and Spencer Act) in order to deter these rising competitors from challenging its regional hegemony. However, by the turn of the century Britain abandoned this strategy due to the Treasury Department's opposition to the prospect of ever-increasing rates of resource extraction for defense.

Up until 1888, France and Italy had the second and third largest navies in the world, and the Russian fleet was a negligible fourth. On good relations with Italy, this meant that Britain only had to ensure naval superiority over the French fleet. However, in 1888, both Russia and France launched concerted naval construction programs. More threatening, in 1891, the two powers agreed to an entente that stopped just short of a military alliance and in 1894, the two powers formed the Dual Alliance, a formal military alliance. The Admiralty projected that Britain's slim naval superiority over a combined Franco-Russian fleet in 1894 of five first-class battleships would fall in 1895-96 to mere

equality, drop behind in 1896-97 by two, and plummet by seven first-class battleships in 1897-98 (Marder 1940, 191).

Britain responded to this naval challenge by enacting the Naval Defence Act of 1889 and the Spencer Act of 1894. In the Naval Defence Act, the First Lord of the Admiralty, George Hamilton, formally called for Britain to maintain a Two-Power Standard or a navy "at least equal in strength" to the next two largest fleets. For Hamilton, the Two-Power Standard was based on modern battleships. The Naval Defence Act would bring Britain's fleet up to a Two-Power Standard by providing for the construction of 10 battleships, 42 cruisers and 18 torpedo-gunboats, over five years, at a cost of 21.5 million pounds (Ropp 1987).⁸⁴ In 1894, Britain followed the Naval Defence Act with the Spencer Act, which authorized construction of an additional 7 first-class battleships, 6 second-class cruisers, 36 destroyers to be completed by 1899, totaling 17.4 million pounds (Ropp 1987; Sumida 1989).⁸⁵

The intention of the enormous naval buildup under the Naval Defence Act and the Spencer Act was to deter current and future rising contenders from challenging Britain's traditional naval supremacy in Europe and elsewhere, and to prepare for a preventive war if necessary. The Admiralty argued that by demonstrating Britain's ability to out-build and out-spend France and Russia, Britain would not only discourage the naval aspirations

⁸⁴ In addition, the Imperial Defense Act of 1888 and the Barracks Act of 1890 provided for completion of the fortifications of the overseas coaling stations, primarily against Russia and additional coastal defenses in England, primarily against France (Ropp 1987).

⁸⁵ Britain was able to pay for the Naval Defence Act and the Spencer Act without substantial borrowing or increases in taxation. Spending increases were balanced by a reduction in the cost of servicing the National Debt (1889), an increase in the income tax, and an increase in death duties through a system of graduated rates. However, most importantly, economic prosperity which increased indirect tax receipts, gave way to budget surpluses, which traditionally were allocated to the reduction of the National Debt (Sumida 1989). In fact, in spite of the increased spending due to the Naval Defense Act and the Spencer Act, economic prosperity brought in so much revenue that Britain continued to run substantial yearly budget surpluses.

of these rising states, but would also deter any future naval challengers.⁸⁶ As Hamilton noted, "if there are any nations abroad who do wish to compete with us in naval armaments, the mere enunciation of this scheme will show to them the utter futility of their desire" (Sumida 1989, 15; Marder 1940, 204).⁸⁷ Similarly, the Spencer Act would "show once and for all that such competition was futile" (Marder 1940, 204). For this reason, the conservative members of Parliament argued that the program should be made public. Proponents rationalized that in deterring current and future naval challengers, these expensive naval programs would save money in the long run by allowing Britain to reduce its naval spending.

⁸⁶ Britain's response was analogous to the chain-store game. According to this game, a chain store which has many branches, will seek to discourage stores from entering its market and challenging its supremacy. In each round of the game, a challenger must decide whether to challenge the chainstore. The decision of the challenger depends upon its forecast of the chain store's likely response. If it believes that the chainstore will respond aggressively, and engage in a price war, the challenger should not seek to enter the market. If it expects the chainstore to accommodate, then the challenger should enter the market. The chain store reaps its highest return if a rival selects not to challenge the chain store's position, since it maintains its monopoly position in the region, however, a price war is not only costly for the challenger, but for the chainstore as well. As the equivalent of a chainstore, Britain sought to establish a reputation as a predator in order to deter current and future entrants from challenging its naval supremacy on the high seas, in the Americas, the Pacific, the Mediterranean, and Britain's homewaters. On entry deterrence, see Lobell (1993).

⁸⁷ The Naval Defence Act and the Spencer Act granted Britain two advantages over France and Russia. First, the large size of the program allowed Britain to build more ships than the combined building programs of both countries. Second, the Naval Defence Act allowed Britain to build ships faster than its neighbors. The Naval Defence Act departed from the existing budget process. Traditionally, a department submitted budget estimates for the following year and second, any unused portion was returned to the Treasury. For departments such as the Navy which had projects which required multiple years of funding, this meant that annually it had to request funding for the same project. In the case of naval construction, the middle years of construction are the most expensive, requiring an increase in the level of funding. Lack of funds often meant that naval construction was delayed and interruptions in construction raised the overall cost of a ship.

The Naval Defence Act provided a remedy to this problem. First, it provided funding for five years instead of single year. Second, it allowed for unexpended balances for naval construction from one year to be used in the next year. Underspending in the early years of construction would be applied to the more expensive middle years of construction, without requiring the Treasury's and Parliament's annual approval.

The Admiralty versus the Treasury

Instead of deterring the emerging contenders, the Naval Defence Act and the Spencer Act incited a costly arms race, overwhelming Britain's existing Two-Power Standard. In 1897, in response to Britain's military buildup, both France and Russia launched new naval construction programs. The German Naval Laws of 1898 and 1900, meant that Germany would shortly hold the balance between Britain and the Dual Alliance in the Atlantic, while Japan's rapid naval construction in the aftermath of the humiliating Triple Intervention meant that it would hold the naval balance in the Pacific. Finally, beginning in 1902, the United States launched a large battleship construction program.

For Britain's First Lord of the Admiralty, Earl Selborne (1900-05), the failure of the Naval Defence Act and the Spencer Act to deter the emerging powers from launching naval construction programs meant that the only foreign policy option was an upward revision of the Two-Power Standard to a three- or even a four-power standard. A revised naval standard would allow Britain to maintain its historic command of the high seas and its local naval supremacy in the Americas, the Mediterranean, the Far East, and Britain's homewaters. In September 1901, in a letter to the Colonial Secretary, Joseph Chamberlain, Selborne wrote that "In respect of naval expenditure it is quite certain that what has been and is being spent is barely sufficient to maintain our battle fleet in a position to cope successfully with France and Russia combined and to protect our commerce in a naval war" (Boyce 1990, 126). In support for Selborne, Joseph Chamberlain called for Britain to build five ships for "any three battleships built by an naval combination against this country" (Friedberg 1988, 155), while former MP Charles

Dilke called for "keeping up such a fleet as would make us safe against any probable combination" (Friedberg 1988, 156).

The Chancellor of the Exchequer, Sir Michael Hicks Beach (1895-1902), opposed an increase in the Two-Power Standard, arguing that Britain could not keep pace with the naval construction of three emerging states without undermining its fiscal strength. His rationale was that no more revenue could be extracted from an already overburdened populace and that Britain's financial problems would not end with the end of the costly fighting in South Africa. In a letter to Selborne in January, 1901, he warned that "I would never undertake the impossible task of building against more than two principal naval powers" (Boyce 1990, 107). In 1901, he warned that the steady increases in naval spending would lead "straight to financial ruin" (Sumida 1989, 23) and that the possibility of a tax being raised above the wartime level "could not be borne" (Monger 1963). With the increasing cost of the Boer War, Hicks Beach argued that, unless there was a fundamental change in Britain's foreign policy, Britain faced the choice of permanently increasing taxation, which would eventually weaken Britain's financial strength, or/of maintaining an insufficient army and navy, which would erode its national security (Monger, 1963).

Members of the services (navy, army), Conservatives such as Joseph Chamberlain, and members of the Liberal Party, countered that Britain could afford the rising naval and social expenditure (Liberals only supported the latter). Proponents of greater defense spending argued that it was impossible that "Britain was approaching the end of [its] resources" (Marder 1961, 10). Selborne argued that resources must be found for the Navy, since defeat at sea would be far more ruinous than any damage to the economy due to increased government expenditure. Others argued that it was well within Britain's financial capacity to increase government expenditure for the defense of the

empire (Murray 1980). Chamberlain's controversial scheme to pay for a three power standard was imperial preferences. Chamberlain maintained that Britain should replace its free trade system with a system of imperial preferences which would protect its industry from foreign competition and generate additional revenue to pay for the defense of the empire. Between 1903 and 1905, the Conservative party battled over the issue of tariff reform, splitting the party into three factions, giving way to the defeat of the Labor Party in 1905. Imperial preferences proved highly unpopular with the masses because it would increase the cost of cheap imported food (Porter 1983).

However, in January of 1901, Selborne also rejected the policy of achieving equality with the three largest navies, instead asking the Cabinet to approve the principle of basing its Two-Power Standard on France and Russia alone. He wrote that, "I propose to consider our position almost exclusively from its relative strength to that of France and Russia combined" (Monger 1963, 11). While momentarily retreating from this stance in 1902, Selborne admitted the impossibility of arming against the next three or four naval powers.⁸⁸ However, Selborne fully intended to maintain the Two-Power Standard. In 1903, he wrote to Hicks Beach's successor at the Treasury, Austin Chamberlain, that "it is perfectly impossible for me to let the standard of the Navy drop" (Boyce 1990, 161).

The Conservative government versus the Liberal Party

As part of this debate on Britain's taxable capacity, there was a lesser debate between the Conservative government and the Liberal party on the limits of tolerable taxation for particular groups of taxpayers. Not only did many Liberal politicians believe

⁸⁸ In 1902, Selborne wrote, "Since I wrote the two Memoranda for the Cabinet last autumn I have studied the naval policy of Germany more closely than I had previously done. The result of my study is that I am convinced that the great new German navy is being carefully built up from the point of view of a war with us" (CAB 37/63/142).

that Britain could afford greater government spending without straining its resources (for social welfare, not the military), they also argued that the bulk of increased taxation should be borne by the wealthy, not the middle classes. Liberals called for Britain to reduce or abolish indirect taxes and to increase direct taxation to meet higher levels of government expenditure for social programs. In addition to increases in direct taxation, they called for a graduation of income tax, the differentiation between earned and unearned incomes, and the taxation of land values, all directed at the wealthy.

The Conservative government rejected any graduation in direct taxation, tax on unearned incomes, and tax on land values to narrow the gap between resources and global interests. Britain's Conservative government derived much of its political support from the landed class and sought to protect its constituents against substantial new taxation. Hence, Conservative politicians argued that direct taxes should be kept as low as possible, instead preferring indirect taxation as the main source of revenue. Even Giffen, who argued that Britain could sustain higher level of government expenditure, called for increased indirect, rather than direct, taxation (Murray 1980). Until their defeat in 1906, the Conservatives rejected most attempts to increase or impose new direct taxes. Many in the Conservative party opposed increased military spending on the same grounds. An upward revision of the Two-Power Standard would require additional revenue and new or higher taxation in peacetime, which would result in the party's loss of political supporters.

Summary

In 1914, Austen Chamberlain declared that, "we are living too fast, we are moving too rapidly . . . we shall run upon the rocks" (Emy 1972, 127). Britain's increased defense spending was in part feasible because of the rapid growth in the economy and the fast increase in the volume of trade of the British empire. However, by 1900, the prospect of

facing ever-increasing estimates of naval outlays to maintain Britain's command of the high seas and local naval supremacy in the Americas, the Pacific, the Mediterranean, and Britain's homewaters ignited a heated debate over Britain's ability to bear the increased government expenditure and taxation. Domestically constrained by the Treasury Department, the opponents of a revised Two-Power Standard prevailed over the navalists, preventing Britain from balancing its capabilities and commitments by increasing its naval capabilities.⁸⁹ However, even advocates of increased military spending recognized the link between Britain's fiscal strength and its military power. In 1901, during the large increases in military spending due to the Boer War, Selborne noted that "Its [Britain's] Credit and its Navy seem to me to be the two main pillars on which the strength of this country rests, and each is essential to the other" (Cab 37/59, 118, p.2).

Britain: A Declining Liberal Hegemon

The nature of Great Britain's foreign commercial policy further shaped its range of security strategies for managing decline. As a declining liberal hegemon, Britain's foreign policy alternatives included the option of devolution of regional hegemony. Consequently, beginning in the late 1880s, with the increasing financial strain due to the

⁸⁹According to French (1982), despite the growth in aggregate spending, Britain did not significantly increase its defense spending. French maintains that in the period between 1905 and 1914, Britain had a two-fold policy towards Europe ("the strategy of business as usual"). First, it rejected the idea of sending an army to the continent and instead decided to assist its allies in defeating Germany through a naval blockade of its ports. Emphasizing the Royal Navy over the Army, the military plans before 1914 did not call for significant expansion of the army or the navy.

Second, as during the Napoleonic war, Britain saw its role in alliance as using its strong economy to supply its allies with the munitions necessary for waging a land war. Based on this logic, it was argued that Britain must not mobilize a large standing army because doing so would deprive it of its industrial manpower. This would allow Britain's allies to "sustain the burden of war while the enemy is rapidly consuming his resources" (French 1982, 34). Equipped with British made supplies, the French and Russian armies would fight the ground war. As J.A. Pease believed, "we could win through holding the sea, maintaining our credit, keeping our people employed and our industries going-by economic pressure, destroying Germany's trade, cutting off her supplies we would gradually secure victory" (French 1982, 35). The Cabinet did not revise this policy until 1915, when it created a continental-scale army to assist the French, requiring a full scale mobilization of economic and military resources.

naval race, the scramble for empire, the Boer War, and domestic pressures for increased social spending, Britain's policy elite began to debate whether Britain should continue its historic foreign policy of Splendid Isolation or abandon this policy in the search for allies in order to devolve regional hegemony.

The principle proponent of a continuation of the strategy of Splendid Isolation during this period was the Prime Minister and Foreign Secretary Lord Salisbury (Grenville 1964; Porter 1987). Britain's foreign policy of Splendid Isolation eschewed alliances, either permanent or transitory. Instead, Splendid Isolation called for Britain to maintain a 'free hand' in its policy choices and to pursue a self-reliant foreign policy. As Paul Kennedy notes, Splendid Isolation was based on the premise that "an independent Britain could look after herself in all corners of the world" (1991, 249).

By 1901, Salisbury's policy of Splendid Isolation came under attack from the Chancellor of the Exchequer, Sir Michael Hicks Beach, the new Foreign Secretary, Henry Lansdowne (1900-05, Lansdowne replaced Salisbury at the foreign office, but Salisbury remained prime minister), and the Colonial Secretary, Joseph Chamberlain. Lansdowne was alarmed by Britain's isolation and believed that Britain could only maintain its empire by alliances (Steiner 1959). Chamberlain spoke of Britain's weakness and its need for continental friends (Steiner 1963, 1977). In a letter to Hicks Beach in December 1900, even the First Lord of the Admiralty, Earl Selborne, argued that a formal alliance was the "only alternative to an ever-increasing Navy and ever-increasing Navy estimates" (Boyce 1990, 106).⁹⁰ Once Britain's leaders had warmed to the possibility of abandoning the foreign policy of Splendid Isolation, they still had to identify whether any rising

⁹⁰ As the Admiralty warned "Great Britain unaided can hardly expect to be able to maintain in the West Indies, the Pacific, and in the North American stations, squadrons sufficiently powerful to dominate those of the United States and at the same time to hold the command of the sea in home waters, the Mediterranean, and the Eastern seas, where it is essential that she should remain predominant" (PRO Cab 37/56/2).

powers were acceptable regional successors. As Paul Kennedy notes, "this [end of isolation] still left many painful decisions as to the regions and interests which would no longer justify full attention and limitless sacrifices" (1991, 249).

Rising Liberal and Imperial Contenders

After the Napoleonic Wars, and especially after the 1830s and 1840s, Britain pursued a freer trade policy both at home and abroad.⁹¹ As a declining liberal hegemon, Britain viewed rising imperial challengers as a threat to its economic strength and national security interests. The rationale was that territorial aggrandizement by an imperial challenger would destroy Britain's overseas markets. With considerable investment across its empire, Britain's ever-present concern was that a rising contender for regional hegemony would replace Britain's Open Door spheres of influence with its own closed door or exclusive sphere, blocking Britain's future access to its markets, investments, food supplies (imports made up 35-40 percent), and raw materials in the locale (the value of Britain's sea-borne trade was 1,200,000,000 pounds per annum).⁹² Highly dependent on foreign trade, the loss of access to its global markets would have a detrimental effect on Britain's wealth and balance of trade, both key components of Britain's war chest (and necessary to pay for a prolonged war). Also, in ceding regional leadership to an imperial challenger, Britain would strengthen the war-making capacity of a future rival, eroding its own national security.

In contrast, Britain viewed rising liberal contenders as supporters of its regional commercial arrangement. The rationale was that in favoring an open door regional order,

⁹¹ This is represented by the repeal of the Corn Laws, the navigation laws, and the gradual removal of tariffs.

⁹² For instance, in the case of China, LaFerber notes, "England had an immense stake in maintaining the open door, for she controlled 70 percent of China's trade" (1963, 316).

a rising liberal state would not dramatically alter the existing commercial order in the region. In fact, Britain assisted in the rise of several liberal supporters, accelerating their rate of ascent in order to hasten its own retreat from the locale, further lowering the cost of hegemony. For Britain, there were three advantages in devolving regional leadership to liberal supporters, Britain would retain access to its local interests without the cost of regional hegemony (Britain intended to free ride on the new regional hegemon); Britain would not strengthen the war-making capacity of a future rival; and Britain could defend its remaining interests without increasing its rate of resource extraction (by concentrating the freed-up resources in its remaining commitments).

United States

Britain identified the United States, Japan, and France as supporters of its free trade system, and Germany and Russia as challengers to its Open Door order. In the case of the United States, although protectionist at home, President William McKinley sought to ensure equal access for the U.S. to overseas commercial opportunities, especially in China. Presidents McKinley and Theodore Roosevelt, among others, were driven in part by the belief that foreign markets were necessary to relieve a glutted American economy and that the United States would stagnate if it failed to expand (the United States had just come out of a severe depression; Becker 1984). According to Williams, with the close of the American frontier in the 1890s, American leaders redirected their focus from continental expansion to the creation of a free trade empire (1972). However, some policy makers did call for the United States to shut the Open Door and join in partitioning the remaining undeveloped regions.

America's free trade outlook was actualized in the Open Door Notes, which became the basis of American foreign policy (LaFeber 1963; Williams 1972). In 1899,

McKinley and Secretary of State John Hay issued the first of two Open Door Notes, which supported Britain's Open Door policy in China. Hay distributed to Britain, France, Germany, and Russia a note calling on the major powers to declare equality of commercial treatment in their spheres of influence, with the Chinese government itself to operate tariffs equally across all the spheres, along with further limitation on preferential treatment within the spheres in order to keep trade open to all states. In particular, the Notes called upon the great powers to give formal guarantees of equal commercial access to both treaty and non-treaty ports, and assurance of uniform (non-discriminatory rates) harbor dues and railroad rates in their spheres. The preamble to the British note emphasized that the open door would help in maintaining the integrity of China (McCormick 1967).

Britain, France, and Germany agreed to adhere to the main points. Japan, which had not been approached in the first place presumably because it was not thought to have a 'sphere of interest,' asked to be invited, after which it promptly adhered to the declaration. Russia's ambiguous reply (refusal to sign but verbally consented) was interpreted by Hay as evidence of adherence although Russia's intentions were far from clear (Russia rebuffed part of the agreement on uniform railroad rates in China because Russia intended to use differential rates to pay for railroad construction).

In 1900, after the Boxer rebellion against Western penetration, Hay issued a second Note to prevent Britain, France, Russia, and/or Japan from using the uprising as an excuse to carve-up China. The states agreed to "Preserve Chinese territorial and administrative entity, protect all rights guaranteed to friendly powers by treaty and international law, and to safeguard for the world the principle of equal and impartial trade with all ports of the Chinese empire" (Clymer 1975). Hay asked for no formal replies

because he expected that "Russia was opposed to it, and would probably reject it" (McCormick 1967, 160).

The intention of U.S. support for Britain's Open Door policy in China was to keep the fabled "China Market" open for future rather than present American trade. American leaders believed that its economic strength and efficiency would allow it to dominate the region commercially (and eventually the world marketplace), as long as it remained open to all. American opposition to the partition of China by special concessions and exclusive spheres of influence drew it closer to Britain (and as discussed below, Japan) in opposing Russian ambitions in Manchuria, and French and German expansion in China. For Britain, the Open Door Notes signaled American support for the objectives of Britain's Open Door policy in China.

Japan

As a late developer, Japan favored initially an exclusive sphere of influence to protect its markets and investments from more competitive and efficient producers such as Britain and the United States.⁹³ However, while Japan had commercial ambitions in Manchuria and Korea, the Triple Intervention demonstrated that Tokyo could not compete with Russia, France, and Germany to acquire its own share of China's crumbling empire. Due to the subsequent scramble for China, and especially Russia's expansion in Manchuria and Korea and its attempt to dominate Peking, Japan feared it would be excluded from China, and that Korea would be occupied and subsequently closed off to Japanese trade and investment. Consequently, Japan supported Britain's Open Door

⁹³ Despite the rapid industrialization experienced under the Meiji era (1868-1912), a large percentage of the population remained in agriculture. In 1872, four-fifths were estimated to be engaged in agriculture, forestry and fishing. Although the numbers declined, in 1913 over three fifths remained in these sectors. In the 1890s, private factory output accounted for less than 6 percent of the total national product (10 percent if government factories are included).

policy in the Far East in order to prevent Russia and Germany from annexing Chinese territory.⁹⁴ Further Russian expansion pushed Japan into fully embracing the Anglo-American position of protecting China's territorial integrity and the continuation of the Open Door policy (Beasley 1981; Nish 1966; McKercher 1989). In 1899, Japan signed the American Open Door Notes. In 1900, during the Boxer revolt, Japan collaborated with the great powers to prevent a further partition of China by the imperial powers. In 1902, with the signing of the Anglo-Japanese alliance, Japan endorsed the Open Door policy in China again. The alliance committed both states to "maintaining the independence and territorial integrity" of China and Korea, and "securing equal opportunities in those countries for the commerce and industry of all nations" (Beasley 1987, 77).

France

Finally, Britain increasingly viewed France as a satisfied rising contender. France sought to reserve its colonial markets for itself and to use these markets to absorb gluts in products of metropolitan manufacture (Lebovics 1988; Ashley 1970; Fieldhouse 1971). The Méline Tariff of 1892 firmly established the policy of tariff assimilation (over the practice of imperial preference). France's colonial policy of economic assimilation called for the incorporation of its colonies into the metropolitan tariff - which meant the establishment of the French tariff on foreign imports into the colony, as well as a free exchange of goods between the colony and France (Clough 1939; Smith 1980).

⁹⁴ Japan's expansion in the Pacific during this period was primarily defensive in nature. In the case of Korea, due to its geographic proximity, the Army General Staff deemed control over the Korean peninsula as essential to the defense of Japan (Crowley 1974). Japan's goal was to deny control over Korea by any other power, since Korea was "a dagger pointed at the heart of Japan" (Duus 1976). As Gillard argues, "As rulers of an island power off the Asian mainland, Japanese leaders felt about Korea much what the British felt about Belgium" (1977, 162). Outside of Korea, Japan was anxious to gain control over the sea approaches to Japan, especially the Straits of Tsushima, and Taiwan and the Pescadores Islands to protect its southern flanks (Crowley 1974).

However, some colonial possessions, such as Morocco, remained 'non-assimilated' because of international agreements, like the 1904 Entente with Britain, which allowed London to maintain commercial freedom in parts of France's empire (such as Morocco).

Germany

While the United States and Japan, and to a lesser degree France, supported Britain's Open Door trade policy abroad, Germany sought to carve-out its own exclusive sphere of influence in the center of Europe (Fischer 1974, 1975). According to David Calleo (1978), Germany's economic expansion consisted of two sequential commercial phases, the first was an economically liberal, territorially satisfied Germany, counting on free trade both to supply its factories and to sell its products; the second was a mercantilist and imperialist Germany, seeking self-sufficiency, needing space commensurate with its growing production and population.

Beginning in 1897, Britain viewed Germany's global policy of *Weltpolitik* or world policy and its correlate, the continental policy of *Mitteleuropa*, as a threat to its open trading system (Calleo 1978; Geiss 1976; Dehio 1962; Hillgruber 1981; Holborn 1966).⁹⁵ *Weltpolitik* called for a more active foreign policy which included a search for new overseas markets and exclusive colonial possessions for markets and raw materials, a large North Sea fleet to protect its trade and to reflect its rising stature (*Risikoflotte* or risk fleet), continental expansion, and increased tariffs to make Germany more self-sufficient.⁹⁶ As part of this policy, several geo-political arguments were put-forth for greater German economic self-sufficiency, Germany needed to maintain a capable

⁹⁵ The chief architects of Germany's *Weltpolitik* were Chancellor von Bülow, Naval Secretary Alfred von Tirpitz, Minister of Finance Johannes Miquel, and Kaiser Wilhelm II.

⁹⁶ Kehr (1977) emphasizes the domestic element of *Weltpolitik*. He attributes it to three forces: agrarians, commercial and industrial bourgeoisie, and the industrial working class.

indigenous agriculture; growing German dependence on foreign foodstuff made Germany vulnerable to cutoffs in time of war (Ashley 1970); industrializing states would steadily consume their own raw materials, leaving little for export; Germany bordered two increasingly hostile neighbors (Russia and France), and could not rely on their exports (Calleo 1978); and Britain might damage German trade by imposing imperial preferences.

Of greater concern to Britain was Germany's continental policy of *Mitteleuropa*. As a late entrant in the race for colonies, there was extensive discussion in Germany that Central Europe was its natural territorial sphere in the world (despite Britain's eventual willingness to cede to it some colonies in Africa). *Mitteleuropa* was a mercantilist and expansionist plan which called for a closed central European economic system or customs union headed by Germany (Gilbert 1977; Schultz 1989).⁹⁷ This zollverein was intended to serve as a "United States of Europe" under German leadership, targeted at the three other great empires of Britain, the United States, and Russia (Kitchen 1979). Calleo points to Bismarck's bilateral alliance with Austria-Hungary in 1879 as the first step in creating a self-sufficient German dominated bloc in Central Europe (1978). As part of a larger mercantilist scheme, Leo von Caprivi, Bismarck's successor, sought to create a liberal European trading bloc (the New Course). According to Fischer, "Behind Caprivi's trade policy was the idea of closer tariff links in *Mitteleuropa* so as to keep out the British Empire, Russia, and above all the United States" (1975, 6).

By 1912, Germany aimed to become a world power by creating an empire which would consist of four parts (Fischer 1975), (1) permanent control of Belgium and direct

⁹⁷ Friedrich List called for the creation of a Prussian Customs Union which would include the whole Habsburg Empire. During the war, *Mitteleuropa* was expanded into the broader concept of Ostraum: Germany would now extend all the way through the Ukraine to the Caucasus and Georgia (Fischer 1975, 33-34, 46; Calleo 1978, 48; Hillgruber 1981, 38, 45).

annexation of the French iron areas in the west; (2) permanent control of the entire area between German and Russia in the east; (3) *Mitteleuropa*-the creation of a Central European Customs Union, dominated by Germany which would include the partners in the Quadruple Alliance and Holland and the Scandinavian countries, as well as defeated powers such as France; (4) *Mittelafrika* called for a German "belt" all the way across Africa. Other regions into which Germany would exert its influence included the Near East (the Baghdad Railway). However, only a secure position in central Europe could provide the economic base for Germany's global empire. Britain's fear was that Germany's foreign policy of *Mitteleuropa*, like Napoleon's Continental System, was directed at itself. Germany's exclusive *Mitteleuropa* policy would destroy Great Britain's extensive and profitable continental trade, threatening the economic base of its military power.⁹⁸

Russia

Russia's economic expansion also concerned Britain. As early as the 1840s, Britain perceived Russia as the most likely challenger to its free trade system (Brawley 1993; Seton-Watson 1967). Britain feared Russia's imperial expansion because it threatened its Open Door commercial policy in Asia. Russia's rejection of the American Open Door Notes further confirmed London's fears. In Britain, it was widely believed that "where the czar sets his Custom House he there proclaims the policy of 'Protectionism'" (Marder 1940, 238). Russia's Finance Minister, Count Witte, claimed openly his determination to "control the entire movement of international commerce in Pacific waters" (LaFeber 1963, 320). Domination was possible through Russia's

⁹⁸ In 1806, Napoleon banned the importation of British goods to the continent with the intention of expanding French economic control over Europe while weakening Britain's fiscal strength.

burgeoning railroad network in the Far East (Marks 1991). In 1887, Russia began to survey for a Trans-Siberian railway, inaugurating construction in 1891, and in 1896 Russia secured the right to construct the Chinese Eastern, which would link the Trans-Siberian Railroad to Vladivostok. Instead of following the more difficult but all-Russian route (along the Amur River), Russia annexed the northern part of Manchuria, allowing Russia to facilitate its penetration into Manchuria.

Britain feared that since Russia was a powerful country with a backwards economy, it would close off to foreign competition any region which it dominated (for instance, the Mendelejev Tariff of 1891 placed heavy duties on imported manufactured goods and on exported raw materials, allowing free entry to only fourteen products; Geyer 1987; Sontag 1968). As a relatively backward state, Russia had a disadvantage in Open Door competition with more efficient producers. According to Walter LaFeber, "[The Russians] after annexing land in Asia, tried to control it tightly by closing the markets to foreign businessmen with whom they could not compete" (1991a, 2). Consequently, Britain feared that Russia would exclude English economic interests from Manchuria, and that as Russia expanded it would eventually make China its vassal, threatening Britain's interests in other parts of China as well.

In summary, Britain confronted a mix of emerging liberal and imperial contenders for regional hegemony. The United States, Japan, and to a lesser extent France supported Britain's Open Door commercial policy. In contrast, imperial Germany and Russia sought to carve-out or partition-off exclusive spheres in Europe, central Asia, and the Pacific. In moving from a hegemonic to a multipolar distribution of power, Britain's dilemma was how to restore the balance between its capabilities and commitments while safeguarding its fiscal and security interests.

Britain's Response: Managing Hegemonic Decline

Alternative Strategies for Restoring the Balancing Capabilities and Commitments

Facing so many potential rivals, Britain's existing level of defense spending was inadequate to protect its global interests. As J.A.S. Grenville notes, "countries are not often faced with so many global changes and dangers in so short a time" (1964). Britain's policy makers debated several alternative strategies to redress the imbalance between its military capabilities and foreign policy goals without undermining its fiscal strength (especially its war chest) or threatening its national security interests. These strategies included increased domestic resource extraction, Splendid Isolation, and devolution of regional hegemony.

With the failure of the Naval Defence Act and the Spencer Act to deter the emerging contenders from constructing first class navies, a number of decision makers, especially the navalists, called for a strategy of increased **domestic resource extraction** in order to restore the balance by revising Britain's Two-Power Standard to a three- or even a four-power standard. It was argued that Britain could generate additional revenue through borrowing, levying new taxes or increasing direct and indirect levels of taxation, suspending debt repayments, seeking greater contributions from the dominions to defend the empire, or even imposing a preferential system of trade. Failure to increase Britain's military capability would tempt rising states to launch preemptive strikes. In response to claims that Britain could not afford an upwardly revised standard, Selborne countered that resources must be found for the Navy, since defeat at sea would be far more ruinous than any damage to the economy due to increased government expenditure. In adopting a three- or four-power standard, Britain could maintain its command of the high-seas as well as its local naval supremacy in the Far East, the Mediterranean, and the Americas.

Second, Prime Minister and Foreign Secretary Salisbury argued that Britain should return the balance by continuing to pursue the time honored policy of **Splendid Isolation** in order to reduce the number of potential threats to its interests and lower the costs of hegemony. Splendid Isolation called for no binding alliances in times of peace; instead, Salisbury believed in retaining a 'free hand' for Britain, which would allow for secret negotiations behind closed doors and for quiet and personal diplomacy. As Zara Steiner notes, "Salisbury preferred a continuation of his 'free hand' policy, making direct settlements with his country's rivals where he could and maintaining barriers against their further expansion when this was feasible" (1977, 24). However, the danger in accommodating some of the rising contenders was that if the agreement broke down or if a rising challenger cheated on the agreement, then Britain would have insufficient military capability to defend its imperial commitments.

Finally, as a declining liberal hegemon, Britain's range of security options for restoring the balance included the strategy of **devolution** of regional hegemony in order to lower its costs of hegemony. Successive Chancellors of the Exchequer, such as Hicks Beach, C.T. Ritchie, and Austin Chamberlain warned that the strain of ever-increasing defense spending could not be "borne" without greatly weakening Britain's economic health and ultimately its ability to afford military spending. Dominating several regions, Britain could balance its capabilities and commitments by devolving regional leadership to rising liberal supporters, while standing firm in locales with rising imperial supporters. The benefits of devolution were two-fold, (1) in redistributing its freed-up resources to other locales, Britain could defend its remaining obligations with its existing level of defense spending; and (2) in transferring leadership over the region to a liberal supporter, Britain would retain access to its traditional interests in the region without bearing the costs associated with hegemony. However, the danger of retreat, as former First Lord of

the Admiralty Reginald McKenna warned, is that "our colonies and our trade will depend not on British power, but on French goodwill" (Kennedy 1991, 259).

The New Course in Britain's Foreign Policy

Domestically constrained by the Treasury Department from increasing its rate of resource extraction, liberal Britain's most attractive strategy to manage its decline was a foreign policy of regional devolution over its alternative option of accommodation. Increased resource extraction for military spending was rejected because the Treasury opposed an upward revision of the Two-Power Standard to a three or four power standard as economically infeasible and the Conservative party opposed an increase in direct taxation to pay for the additional defense spending. Rejection of this foreign policy option was not a foregone conclusion. During the Anglo-German naval race (1909-1912), Britain increased its rate of resource extraction in order to outpace German construction. Alternatively, a continuation of Splendid Isolation was rejected because Britain's leaders recognized that in devolving leadership to the United States, Japan and France, Britain could retain access to its interests in the Americas and the Pacific, without bearing any of the financial, political, or military costs associated with regional hegemony.

In selecting a strategy of devolution, Britain restored the balance between its capabilities and commitments by reducing the costs of hegemony. First, in devolving leadership over the Americas to the United States, the northeast Pacific to Japan, and the eastern Mediterranean to France, and in some instances even building up these emerging liberal supporters in order to hasten its retreat, Britain no longer bore any of the costs of regional hegemony. Second, Britain concentrated the freed-up resources from these locales in its remaining commitments in its homewaters (against Germany) and in central Asia (against Russia), further reducing its defense spending.

A strategy of devolution safeguarded Britain's fiscal strength and its national security interests, ensuring that it had sufficient fiscal and military capability to continue to influence the great power game in order to protect its existing national interests. First, devolution of leadership to the United States, Japan, and France meant that Britain did not undermine its economic strength or drawdown its war chest by excessive and prolonged defense spending. Consequently, Britain had the resources to finance the allies' war against Germany. However, had Great Britain been unwilling to retrench from strategic locales such as the Americas, Britain would have risked undermining its fiscal strength by prolonging its defense spending. Second, Britain did not undermine its national security by devolving regional leadership to either imperial Germany or Russia, which risked accelerating its rate of decline by strengthening the war-making capacity of a future rival and by losing future access to Britain's commercial interests in Europe, central Asia, and the Pacific. Thus, in relation to its other foreign policy options, a strategy of devolution (and a liberal foreign commercial policy) ensured that Britain remained a great power as long as possible.

Devolving leadership to the United States, Japan, and France

In 1901, Britain ceded leadership over the Western Hemisphere to the United States with the signing of the Hay-Pauncefote Treaty.⁹⁹ As J.A.S. Grenville notes, "The signature of the Hay-Pauncefote Treaty in 1901 marked-and the British cabinet was in no doubt about this-the conscious British recognition of the eventual United States supremacy in the Western Hemisphere and thus entailed a fundamental change in the

⁹⁹ During this period, Britain transferred leadership over the Americas (Latin America, the Caribbean and North America, i.e., Canada), and especially the Caribbean, to the United States. This is demonstrated by the withdrawal of British forces from bases in the Caribbean Sea (Barbados, Trinidad, Bermuda, and Jamaica) and Canada (Halifax, Esquimalt, and the Great Lakes).

relations of the two countries" (1955 48; see also Bourne 1967; Wells 1968; Lowe and Dockrill 1972a). In 1902, Selborne urged Britain's Cabinet to drop the U.S. navy from the two power standard. And by 1903, Britain's Prime Minister, Arthur Balfour, openly proclaimed his support for the Monroe Doctrine, claiming that "The Monroe Doctrine has no enemies in this country that I know of. We welcome any increase of the influence of the United States of America upon the great Western hemisphere."¹⁰⁰ Thus, similar to Britain's decline, the advent of American hegemony was not global in nature, but instead occurred first in the Americas around the turn of the century.

Some scholars contend that Britain appeased a rising United States because of the latter's potential military capability (Kennedy 1983; Gilpin 1981; Rock 1989a; Lowe and Dockrill 1972a). Although Britain might not have been able to prevent the rise of the United States, it could have done much to slow its rate of industrial growth. Just as the United States sought to slow the speed of Soviet industrialization by "delaying tactics" such as embargoing Western goods to the East (Organski 1968), Britain could have slowed America's rate of industrial ascent through trade barriers and embargoes, especially by blocking the transfer of British capital. English capital was an essential component in the early development of American industry, especially the development of its vast railroad network. In 1899, British investors held about 2.5 billion in American stocks and bonds, roughly 75 percent of all American securities in foreign hands (Porter 1983). As a last option, Britain could have waged a preventive war against the United States while war was still feasible.

However, there was no reason for Britain to slow U.S. industrial growth or to launch a preventive war because, as Britain viewed the United States as an acceptable

¹⁰⁰ Under the Roosevelt Corollary, the U.S. undertook the role of "international police force" in cases of "wrongdoing or impotence."

liberal successor.¹⁰¹ For Britain, the U.S. Open Door Notes signaled its support for Britain's Open Door commercial policy. With an ever-increasing amount of British trade and investment concentrated in Latin America, U.S. domination of the sphere would allow Britain to continue to advance its commercial interests in the region without the cost of leadership. In fact, Britain assisted in the rise of the United States in order to hasten its own retreat from the Americas, allowing Great Britain to redeploy the Royal Navy to another locale (Rosecrance and Taw 1990).

Interestingly, Stephen Rock maintains that like German naval expansion, American naval expansion was directed at Britain (1988). By creating a "risk" fleet of sufficient size and because Britain would be unwilling to concentrate its fleet in the Americas on account of its rivalry with France, Russia, and Germany, the U.S. forced Britain into making a number of concessions. The problem with this argument is that the timing is wrong. Britain's departure from the Americas prompted the United States to increase the size of its fleet. No longer able to count on protection from the Royal Navy, the U.S. initiated a naval buildup beginning in 1902 (the lead time was roughly three years to build a battleship). American naval buildup did not begin in earnest until Theodore Roosevelt assumed office in 1901, and was further prompted by the Venezuelan crisis of 1902. Between 1902 and 1905, Congress authorized ten first-class battleships, four armored cruisers, and seventeen other vessels of various classes (Sprout 1944). By 1905 the U.S. had twelve modern battleships and was building another twelve. In 1907, after the introduction of the Dreadnought, which rendered all other American

¹⁰¹ The "special relationship" relationships between the U.S. and Britain tempered relations. A belief in the unity of Anglo-Saxon nationalism, based on a common language, history, and political ideology, contributed to Anglo-American goodwill. In Britain, key decision makers such as Joseph Chamberlain and Arthur Balfour discounted the danger posed by the United States (Rock 1988). Few members of Britain's government made similar pronouncements in favor of Germany. One solution to Britain's problems at the turn of the century was to admit America as an equal partner in the pax-Britannica (Lowe and Dockrill 1972a).

capital ships obsolete, Congress authorized construction of two dreadnoughts and two more the following year.

In addition to accommodating the U.S. in the Americas, in 1902, Britain devolved leadership over the Pacific to Japan (Nish 1966; Steiner 1959). The Anglo-Japanese alliance entrusted Japan with preservation of naval security in the northeast Pacific, while the British fleet continued to safeguard the sea routes to Australia and New Zealand and to protect British interests in Hong Kong and Singapore (Crowley 1974). During World War I, Curzon admitted that "I suppose it is not to be denied that our alliance with her [Japan], and the assistance of her naval forces, assured the complete safety of our possessions in the Pacific" (Barnett 1972, 252). For both Britain and Japan, devolution was mutually beneficial. Japan sought alliance with Britain in order to enhance its international reputation as an emerging power (especially to prevent a repetition of the Triple Intervention) and to provide security. Japan also needed British capital to develop its backward infrastructure and British support in order to reverse the "unequal treaties" which guaranteed extraterritoriality to resident Westerners and tied Japan's hands in such foreign economic policy matters as the autonomous use of tariff rates. Britain sought alliance with Japan as a tool to "control" a rising power which could otherwise evolve into another competitor in the Far East and to buildup Japan, especially its navy, in order to reduce its own commitments in the region.¹⁰²

For Britain, Japan was an acceptable regional successor. Japan's opposition to the partition of China and its support for Britain's Open Door policy in China meant that Britain could devolve regional leadership over the northeast Pacific to Japan and still

¹⁰² See Schroeder (1976a) on the use of alliances as tools of management and control. In a speech in March 1914, Churchill announced that the defense of the South Pacific would be undertaken by Japan.

retain access to its traditional interests in the locale.¹⁰³ In fact, Britain built up Japan's Imperial Navy, accelerating Tokyo's rate of ascent in order to hasten its own retreat from the Far East.¹⁰⁴ By entering into a naval alliance with Japan in 1902, Britain maintained a local naval supremacy over the Dual Alliance in the Far East, without mobilizing additional resources or reducing its naval stations in other regions.¹⁰⁵ For Selborne, an Anglo-Japanese alliance would release ships from the Far Eastern station, freeing-up resources which could be redistributed and concentrated in European waters. In 1905, the Anglo-Japanese treaty was expanded to include as a *casus belli* an attack by any one power on the "Asiatic possessions" of either Japan or Britain (the alliance was renewed again in 1911 for ten years). The extension of the treaty with Japan solved the problem of Britain's inability to defend India in the instance of a Russian invasion. As part of the renewal of the Anglo-Japanese alliance, Japan agreed to commit 100,000 troops to the defense of India. In response, Sir George Clarke commented that Britain would "pull off another great coup" by getting Japan to assume some responsibility for the defense of India (Neilson 1991, 717).

¹⁰³ In Japan there was disagreement between the faction led by Yamagata, which favored an alliance with Britain and the faction led by Ito, which felt that war could best be averted by arriving at some sort of understanding with Russia. The argument for alliance with Britain was that as a satisfied power, the alliance was more likely to last than with Russia, which was still pursuing its ambitions (Nish 1974).

¹⁰⁴ Many of Japan's larger naval ships were built in British shipyards (ships built for the Imperial Japanese Navy in 1901; Marder 1940):

Class	Where Built	# of Ships
Warships	Home	45
	Great Britain	47
	Elsewhere	32
Destroyers	Home	45
	Great Britain	16
	Elsewhere	5

¹⁰⁵ Unfortunately for Britain, Japan was expanding in Manchuria, a region which Britain had little interests but which the U.S. had considerable interests, putting the two countries on a collision course, with Britain in the middle (Barnett 1993).

Finally, Britain devolved leadership over the eastern Mediterranean to France. The Anglo-French entente of 1904 settled a number of colonial disputes, reducing the likelihood that a colonial conflict could erupt into war and facilitating the withdrawal of British and French troops from the periphery (Andrew 1968; Rolo 1969).¹⁰⁶ While France's trade policy was characterized by protection, Paris did fulfill its international agreement to allow Britain to maintain commercial freedom in parts of its empire such as Morocco. By the turn of the century, Britain increasingly viewed France as a rising satisfied power. In 1912, due to the rising German threat in Europe and Britain's view of France as a satisfied rising power, Winston Churchill, First Lord of the Navy, announced the Anglo-French naval agreement (Halpern 1971; Williamson 1969).¹⁰⁷ This naval agreement transferred leadership over the eastern Mediterranean to France, allowing Britain to concentrate its Mediterranean fleet in the North Sea and the upper reaches of the Channel.¹⁰⁸ Devolution meant that Britain could maintain its naval supremacy in its homewaters while ensuring its commercial and imperial interests in the Mediterranean. Nicholson, the Foreign Office Permanent Under Secretary called it the "cheapest, simplest and safest solution" (Kennedy 1991, 268).¹⁰⁹

¹⁰⁶Significant for Britain was France's respect for British strategic interests in the Mediterranean (Williamson 1967). Determined to prevent the fortification of the narrow eight-mile wide Straits of Gibraltar, Britain (and France) agreed to give weaker Spain control over the sector of the Moroccan coast adjacent to the Straits, not allowing any fortifications to be built.

¹⁰⁷ Due to the rising German land challenge, France underwent its own process of retreat from empire. Not only did it reach an agreement with Britain in 1904, but with Japan in 1902 and Siam in 1907. The purpose was to reduce threats to France's empire so that it could concentrate its troops in Europe. For this reason, France was unwilling to assume any of Britain's global responsibilities.

¹⁰⁸ In 1912, facing a rising Germany on the continent, Britain had four options (Neilson 1991): Reduce the margin in the North Sea, abandon the Mediterranean, build a new fleet for the Mediterranean, make naval arrangements with France and leave enough ships in the Mediterranean to give an undoubted superiority.

¹⁰⁹ For France, maintaining sea control in the Mediterranean was essential to ensuring the transport of troops from North Africa. This arrangement meant that France would have a local superiority over the combined Italian and Austrian fleets.

Standing firm against Russia and Germany

In devolving leadership to the United States and Japan, and to a lesser extent, France, Britain was able to concentrate its freed-up resources against a rising imperial Russia in Central Asia and an emerging imperial Germany in Britain's homewaters. Britain stood firm against an emerging Russia because London believed that the Czar would establish a new and exclusive regional order, to the detriment of Britain's local interests, over any region which Russia came to dominate. Even after the Anglo-Russian agreement in 1907, the General Staff in India thought largely in terms of the Russian menace (Lowe and Dockrill 1972b, 276). Russia's backward economy signaled that Russia would protect its market and any region it dominated because it could not compete with more efficient foreign imports. The danger, as LaFeber notes, is that "If Russia consolidated her power in the Far East, and her power would be immense after the completion of the Trans-Siberian railroad, she could close the open door at will" (1963, 322).

Finally, Britain stood firm in the face of an emerging Germany in its homewaters. Germany's foreign policy of *Weltpolitik* posed a threat to Britain's commercial interests. Commercially, Germany sought greater self-sufficiency in the form of a *Mitteleuropa* policy. The purpose of this foreign policy was to create a fourth empire, dominated by Germany, to compete with the Russian, British, and American empires. However, if Germany were to gain hegemony over Europe, Germany would threaten Britain's trade with the continent and ultimately its economic wealth. Just as Britain fought Napoleon's Continental System, it was destined to fight Germany's *Mitteleuropa*.

Safeguarding fiscal strength

In devolving hegemony, Britain was able to concentrate its freed-up resources in its remaining commitments, protecting its fiscal strength without eroding its national security by strengthening the war-making capacity of an emerging rival. In particular, a strategy of devolution meant that Britain could reduce its rate of resource extraction for defense spending, safeguarding its productive capacity and its war chest. Beginning in 1903, the Chancellor of the Exchequer, Austin Chamberlain (1903-05) imposed drastic reductions in military spending, especially naval construction and implemented reforms to increase the efficiency of existing expenditure. He noted that "In my opinion, they [reductions] must be sought in both the Army and Navy estimates. Neither alone will be sufficient; and however reluctant we may be to face the fact, the time has come when we must frankly admit that the financial resources of the United Kingdom are inadequate to do all that we should desire in the matter of Imperial defense" (CAB 37/70).

Chamberlain exacted concessions from Arnold-Forester, the Secretary of State for War, and Selborne for leaner defense budgets. In the case of the Army, in 1904-05 the army cost 31.6 million pounds and by 1905-06 this amount had been reduced to 29.1 million pounds and continued to decline until 1913 (Sumida 1989, Table 15; Dunlop 1938). Savings resulted from withdrawal of a number of colonial garrisons (West Indies, Bermuda, Canada), weakening British forces in Canada, and a cap on Britain's defense spending in India (Friedberg 1988; Wells 1968).¹¹⁰

¹¹⁰ During the 1890s, the army and the War Office were guided by the Stanhope memorandum (1891) which defined the Army's duties as: home defense, supplying replacements for overseas garrisons, and preparing two corps for operations in colonial areas. By 1903, this duty had been revised, the Navy could block any invasion threat, leaving the army to defend against a possible Russian invasion of India.

More drastically, beginning in 1904, Britain underwent a second round of reduction in naval spending (Marder 1940, 483-514). Lord Selborne and his First Sea Lord, John Fisher, reduced naval expenditures by creating a smaller and less expensive fleet and by scrapping obsolete ships. This savings was accomplished by implementing four reforms, creation of a nucleus crew system, the redistribution and further concentration of fleets in homewaters (which was aided by the telegraph and faster ships) to meet current needs (which had been going on since 1901), the decommissioning of ships of minimal fighting value, and the introduction of the all-big-gun battleship and battlecruiser.

Britain reduced the cost of hegemony by concentrating freed-up naval squadrons in its remaining commitments. The Pacific, South Atlantic, and the North America and West Indies squadrons were abolished. The Cape squadron was to take over the two latter stations and the West Coast of Africa. The Eastern fleet, with its center at Singapore, was to consist of the amalgamated squadrons of the Australian, China, and East Indies station. The Home fleet was renamed the Channel fleet, centered at Dover and increased to 12 battleships; the old Channel fleet was renamed the Atlantic fleet, based at Gibraltar and remained at 8 battleships; and the Mediterranean fleet based in Malta was reduced from 12 to 8 battleships. The Atlantic fleet could reinforce either the Channel or the Mediterranean fleet. The outcome of these reforms was that naval estimates declined every year from 1904-05 to 1909-10, falling from 41 million pounds in 1904-05 to a low of 32.7 million in 1907-08, not surpassing the 1904-05 level until 1910-11 (Sumida 1989, Table 3). Expenditures on battleships and cruisers fell from 10 million in 1904-05 to a low of 5.9 million in 1908-09, not reaching a new high until 1912-13.

In summary, in selecting a security strategy of devolution, Britain remained in the ranks of the great powers as long as possible (Neilson 1991). In particular, in the short run, devolution decelerated Britain's decline, ensuring that it remained in the great power ranks longer than its alternative choices of accommodation or extraction. In accommodating an emerging Russia or Germany, Britain risked eroding its immediate national security by strengthening the war-making capacity of a rival. Alternatively, in extracting resources to out-pace the combined military buildup of several emerging contenders, Britain risked undermining its productive strength and ultimately its military capability. In contrast, in devolving hegemony to an emerging United States, France, and Japan, Britain was able to reduce its rate of defense spending while strengthening its war-making capacity against an emerging imperial Germany and Russia by concentrating its freed-up resources in its homewaters and central Asia.

In the long term, the nature of Britain's liberal foreign commercial policy ensured that it remained in the ranks of the great powers longer than under an imperial commercial policy. As an imperial hegemon, Britain could only select from a range of strategies which either would erode its fiscal strength or its national security. In contrast, as a liberal hegemon, in devolving regional leadership to the United States, Japan, and France, while standing firm against imperial Germany and Russia, Britain safeguarded its economic staying power and its national security interests. First, by concentrating the freed-up resources from the Americas, the Pacific, and the Mediterranean against an emerging Russia in central Asia and against Germany in Britain's homewaters, Britain protected its fiscal strength by lowering its rate of resource extraction for military spending. Second, in devolving hegemony to liberal supporters, Britain protected its national security by not strengthening the war-making capacity of imperial Germany or Russia. However, had Britain been unwilling to devolve regional leadership in valuable

locales it would have risked undermining its fiscal strength by excessive defense expenditures. Thus, in safeguarding its political economy and its national security, Britain had sufficient economic and military capability to continue to influence the great power game in order to protect its national interests.

Conclusion

In the two decades prior to World War I, Britain was able to manage its decline, remaining a key player in the great power game until World War II. The nature of Britain's foreign economic policy contributed to its success. As a declining liberal hegemon, a foreign policy strategy of regional devolution was more attractive than the alternative strategies of upwardly revising its Two-Power Standard to a three- or four-power standard or continuing its policy of Splendid Isolation. In the short term, in devolving leadership to the United States, Japan, and France, Britain was able to restore the balance between its capabilities and commitments by reducing the costs of hegemony. In particular, Britain was able to retain access to its traditional interests in these locales without bearing any of the costs associated with regional hegemony. In the long run, in devolving regional hegemony Britain safeguarded its economic strength and national security; Britain did not erode its economic staying power as it would have done by increasing its rate of resource extraction or threaten its national security interests by accommodating imperial Germany or Russia.

In contrast, Aaron Friedberg argues that Britain should have increased its rate of domestic resource extraction for defense spending rather than devolving regional leadership (1988). His rationale is that Britain's leaders concluded incorrectly that the economy could not sustain increased government spending. However, it is unlikely that Britain could have borne the formidable and constantly increasing burden of matching the

defense spending of a rapidly industrializing United States, Germany, Japan, and Russia. Failure to match the strength of these emerging states, would have left Britain vulnerable to attack everywhere, while excessive and prolonged resource extraction would have undermined its economic strength. Thus, a strategy of prolonged extraction would have risked accelerating Britain's rate of decline over its chosen strategy of devolution, resulting in a corresponding reduction in Britain's influence in the great power game.

Britain's leaders also recognized the linkages between economic and security policies. Had Britain adopted the imperial preference system advocated by Joseph Chamberlain, it would have hastened Britain's fall from the ranks of the great powers rather than slowed down or reversed its rate of relative decline. As an imperial hegemon, Britain's foreign policy alternatives for managing decline would have been restricted to either a strategy of increased resource extraction or accommodation. While ensuring Britain's immediate security, extraction would have undermined Britain's economic strength, while accommodation would have eroded its national security interests. In the long run, these strategies would have resulted in Britain's fall from the ranks of the great powers due to either excessive defense spending, accommodating an incompatible rising challenger, or insufficient defense capability.

CHAPTER 4

BRITAIN'S FOREIGN POLICY OF ACCOMMODATION (1932-1939)

In the decade after World War I, Britain was once again the pre-eminent world power. Britain's empire included new regions in the former Ottoman Empire. Germany was disarmed under the Versailles Treaty and its navy was scuttled at Scapa Flow. Other potential contenders for regional leadership such as Italy and Japan were relatively quiescent. France was giving priority to its army and the construction of the defensive Maginot Line over its navy. Russia was greatly weakened by the revolution, civil war, and Stalin's purge of the office corps. Finally, the United States returned to a policy of near-isolationism, concentrating its efforts in the Americas. In sum, Britain was in the enviable position of "not wanting to quarrel with anybody because we have got most of the world already, or the best parts of it, and we only want to keep what we have got and prevent others from taking it away from us" (Pratt 1975, 3).

However, by the early 1930s, Britain's global interests were again challenged in disparate parts of its empire by different emerging contenders for regional hegemony. Britain faced an emerging Japan, Soviet Union, and the United States in the Far East, a rising Germany on the Continent, and an emerging Italy in the Mediterranean. As well, Britain faced nationalist challenges within its empire in Egypt and India, and a civil war in Palestine. The Spanish civil war (1936) posed a threat to Britain's passage through the Straits of Gibraltar and the strategic Balearic Islands to its Far Eastern empire. Economically, Britain's traditional exporting industries were succumbing to foreign

competition, while Britain's growing dependence on trade with its empire meant that more than ever Britain needed to protect its foreign commercial interests.

As in the two decades prior to World War I (see Chapter 3), in encountering rising contenders for regional leadership in disparate parts of its empire, Britain's leaders were faced with the dilemma of how to reconcile the nation's military capabilities and its global commitments without undermining its fiscal capacity or threatening its national security. Defending its global interests with its existing rate of defense spending was dangerous because Japan, Germany, and Italy launched large rearmament programs, overwhelming Britain's existing military capability. Failure to increase its military capability risked leaving Britain weak and vulnerable to attack everywhere. However, in matching the combined defense spending of three rising powers in different parts of the globe, Britain risked undermining its fiscal strength through prolonged military expenditure. Finally, global retreat was dangerous because Britain risked strengthening the war-making capacity of an emerging revisionist challenger, threatening its own national security interests. In addition, Britain's dependence on non-European trade meant that the loss of a sphere would erode its fiscal strength and ultimately its military power.

After successfully managing its decline prior to World War I, Britain failed prior to World War II, accelerating its fall from the ranks of the great powers to a second rate power. The nature of Britain's foreign commercial policy contributed to its failure. As a declining imperial hegemon, Britain could only select from a range of security strategies that either eroded its fiscal strength or its national security interests. In the short run, Britain was able restore the balance between its capabilities and commitments by lowering the costs of hegemony, remaining in the ranks of the great powers longer than any of its alternative options. However in the long run, Britain undermined its national

security interests, accelerating its decline from the ranks of the great powers. This chapter examines the strategy Britain used to balance its military capabilities and its global interests, and why this strategy failed. The first section discusses the rising contenders for regional leadership that Britain confronted. The next two sections focus on two debates that occurred among Britain's policy makers on how to manage its decline. The final section discusses why, although aware of the dangers of this option, Britain selected a foreign policy strategy of accommodation over a strategy of devolution or increased resource extraction, and why this strategy failed in the long term.

The Emerging Contenders for Regional Leadership

Scholars who examine Britain's diplomatic history in the decade prior to World War II tend to focus on Great Britain's position in a single region, the Continent, the Mediterranean, the Far East, or the Empire. Had Britain confronted a single emerging challenger it could have concentrated its resources from the other parts of its empire, overwhelming the contender's without any debate over alternative foreign policy strategies and the related financial and security consequences.¹¹¹ However, in the 1930s, Britain confronted an emerging Germany, Japan, and Italy, rising at different rates, and in disparate parts of its empire, as well as challenges from within its empire. As one author notes, "there is no major discussion of British foreign policy in the 1930s which faces the problems, as the Chamberlain administration had to, as part of a concurrent though rarely concerted attack on Britain's position in Europe, in the Mediterranean and the Middle East, and in East Asia and the Pacific" (Watt 1965b, 208). In over-simplifying London's predicament, it is difficult to understand the dilemma that Britain faced in striking a

¹¹¹ Some exceptions include Pratt (1975); Gibbs (1976); Parker (1975); French (1993); Walker (1980); McKercher (1991).

balance between its military capabilities and global interests while protecting its long term fiscal strength and national security interests.

First, Britain confronted a number of disparate rising contenders for regional leadership. In the Far East, Britain confronted an emerging Japan, the United States, and to a lesser extent, the Soviet Union; in the Mediterranean, Britain faced an emerging Italy; and on the Continent, Britain encountered a rising Germany. Second, differential rates of industrial growth meant that these contenders encroached on Britain's empire at different rates. Germany was the first power to encroach on, and based on some indicators, surpass Britain in key sectors such as iron/steel production, energy consumption, and relative shares of world manufacturing (Kennedy 1987, 200-202). Behind Germany, Japan overtook France in the 1930s and was rapidly gaining on Britain's industrial lead. Finally, on most economic indicators, Italy remained a distant third rate power. Third, Britain's regional leadership was challenged by rising contenders in different periods during the 1930s. In 1931, in invading Manchuria, Japan was the first power to challenge Britain's regional hegemony. Italy's invasion of Abyssinia in 1935 and its attempt to create a new Roman Empire threatened Britain's passage through the strategic Mediterranean Sea. Finally, while Britain never dominated the Continent, in 1938, beginning with the Anschluss, Germany sought hegemony over Central and Eastern Europe.

Britain's Homewaters: Germany

In 1933, Hitler was appointed Chancellor of Germany. Soon after, Hitler announced that Germany intended to withdraw from the League of Nations and from the Disarmament Conference in Geneva. In 1934, Hitler supported a Putsch in Vienna, with the aim of uniting Austria and Germany (Anschluss). However, Germany was deterred

from moving forces into Austria by Mussolini's deployment of four divisions to the strategic Brenner Pass on the Austro-Italian border.

In 1935, in violation of the Versailles Treaty, Hitler announced the existence of the Luftwaffe and revealed that Germany had reached air parity with Britain and reintroduced conscription, creating an army of thirty-six divisions. In response, Britain, France, and Italy formed the Stresa Front, condemning Germany's violation of the Versailles Treaty and announcing their intention to stand firm against further violations. In the same year, Britain and Germany concluded a naval pact, allowing for a limited German naval buildup but preventing a repeat of the 1909-1912 Anglo-German naval race (yet, Germany's sanctioned naval buildup created divisions among the Stresa front).

In 1936, the German army marched into the demilitarized zone of the Rhineland, further challenging the Versailles Treaty and the Locarno Treaty. Germany and Japan also signed the Anti-Comintern Pact. In the same year, Germany introduced the Four Year Plan, intended to prepare the German economy for war in four years by reducing its dependency on foreign food and raw materials. In 1938, Germany resumed its expansion, but this time towards the East. In the search for *Lebensraum* or greater 'living space,' Hitler invaded Austria, resulting in the Anschluss.¹¹² Next, Hitler prepared to restore the Sudeten Germans to the homeland.¹¹³ In an attempt to prevent war, at the Munich Conference, Chamberlain and France's Prime Minister, Eduard Daladier, approved self-determination of the Sudeten Germans and the cession of the area to Germany (both France and Russia had an alliance in Czechoslovakia). In return, the great powers

¹¹² On November 5, 1937, Hitler exposed to the German military chiefs and the foreign minister the "fundamental principles" regarding German foreign policy. He explained his determination to conquer the necessary 'living space' for the Germanic race on the Continent even at the risk of general war.

¹¹³ In May, 1938, rumors were rife that Germany was set for an attack on Czechoslovakia. At that moment France and Russia declared their willingness to stand by their Czech ally, and Britain made it clear that it could not be expected to be a disinterested onlooker. As a consequence, Germany hastily withdrew (Holborn 1966).

guaranteed what remained of Czechoslovakia. However, in March 1939, the German army invaded Prague and Memel (on the Baltic), and shortly after, Hitler denounced the 1935 Anglo-German Naval Agreement, calling for a massive naval construction program.

The Far East: Japan

Europe was only one of several spheres where Britain had to devote its resources. In 1931, Japan invaded South Manchuria and in 1932, advanced into North Manchuria, creating the client state of Manchuko. Of greater concern to Britain, Japan attacked Shanghai, the center of British commercial interests in China (Britain devolved Manchuria to Japan prior to World War I; see Chapter 3).¹¹⁴ In 1933, Japan gave notice of its intent to withdraw from the League of Nations, and in 1934, denounced the Washington Naval Agreement (1922), insisting on parity with the British and American fleets. In 1936, Japan concluded the Anti-Comintern Pact with Germany.

Until 1937, Japanese expansion was directed mainly to the north of the Yangtse. The Sino-Japanese War marked the beginning of Japan's expansion into south China, threatening Britain's center of investment and trade in the Yangtse Valley. In 1937, Japan invaded China, quickly extending its control over northern and coastal China, and in 1938, Japan extended its control over the Yangtze valley and Canton, close to centers of British trade and investment (Lowe 1977).

¹¹⁴ China was economically valuable to Britain. In the first six months of 1937, Britain exported more than four million pounds to China. Britain's total investments in China totaled 250 million pounds or 6 percent of British overseas holdings (Lee 1973, 16). As well, if Britain become involved in a war it would be essential to maintain trade with its possessions in South Asia, which supplied rubber, tin, oil, food (Lee 1973, 18).

Mediterranean: Italy

Italy was the final emerging contender for regional hegemony (Lowe and Marzari 1975). Beginning in 1935, Mussolini sought to re-create the Roman Empire in the Mediterranean, stretching from North Africa, to the Red Sea, to the Adriatic (Robertson 1977; Cassels 1983). In 1935, Italy invaded Abyssinia (during the height of Italy's invasion, the German army marched into the Rhineland). In response, with Britain's commitment to collective security, the League of Nations imposed economic sanctions in order to compel Italy to back-down. However, by 1936, at great financial expense, Italy defeated the Abyssinian army, and sanctions were dropped.¹¹⁵ In an attempt to repair Anglo-Franco-Italian relations (for fear that Italy might be pushed into the German camp), the British and French foreign ministers proposed the Hoare-Laval plan, calling for Italy to receive a mandate over the fertile plains of Abyssinia and for the Abyssinian emperor to retain his kingdom in the mountains. However, the plan was eventually rejected by the British Cabinet.

By 1937, Italy was actively supporting Franco's war against the Republicans (along side Germany) in the Spanish Civil War. For Britain, a friendly Spain was important for the security of Britain's Atlantic (Canary Islands) and Mediterranean trade routes (Gibraltar, Balaeres Islands). Italy was also subsidizing Arab nationalists in Egypt and Palestine in order to undermine Britain's position in the Red Sea, and stationing troops in Libya with sufficient stores to attack Egypt (Watt 1975).

In 1937, Italy was the last of the three dictators to leave the League of Nations, joining the German-Japanese Anti-Comintern Pact. To reduce tensions, the Anglo-Italian

¹¹⁵ The Ethiopian war plus the intervention in Spain drained Italy's budget. From 1934-5 to 1939-40, over 51 percent of Italy's state budget went to Ethiopia, Spain, Albania, other colonies, and the military (Knox 1982, 31).

"Gentlemen's Agreement" was signed to preserve the status quo in the Mediterranean; Britain recognized Italy's position in Abyssinia and in return Italy agreed to withdraw a substantial number of volunteers from Spain. In 1939, Italy formally annexed Albania, and began to set its sights on Greece and Turkey (Knox 1982). After rejecting previous German approaches, Italy and Germany signed a formal alliance, the Pact of Steel. For Italy, the Pact of Steel allowed Rome to protect its backside while expanding its empire in the Mediterranean.

The Offstage Superpowers

United States

After World War I, the United States called for the construction of a navy "second to none," making the United States the main rival to the Royal Navy. However, by 1921, the United States supported the Washington Naval Conference to force naval disarmament and to break up the Anglo-Japanese Alliance (1902). To prevent an Anglo-American naval construction race (in the most expensive warships), at the Washington Conference, Britain conceded to American demands for naval parity with the Royal Navy for capital ships, and at the London Conference (1930) this limitation was extended to cruisers and destroyers.

Concomitant with these naval agreements, the United States pursued a strategy of near-isolationism, concentrating its efforts in the Americas. In 1934, Congress passed the Johnson Act which forbid private or public loans to the governments that had defaulted on their debts to the United States, including Britain. The Neutrality Acts (1935, 1936, 1937) further restricted FDR's foreign policy options. These acts forbid the United States from shipping arms or other weapons to any belligerent nation. Missing out in the profits of European rearmament, the 1937 Neutrality Act allowed belligerents to purchase certain

war materials from the United States but only on a "cash and carry" basis. The intention was to minimize the risk of involvement in a European war, while allowing Americans to profit.

In 1939, in protest against Japan's expansion in the Far East, the United States terminated the 1911 Japanese-American commercial treaty. Tied by the Johnson Act and the Neutrality Acts, in 1940, the United States transferred fifty World War I destroyers to Britain in exchange for ninety-nine year leases on bases in the British West Indies (instead of money from cash-poor England), and in 1941, FDR proposed the "lend-lease" policy in which the United States would lend or lease goods to Britain.

The Soviet Union

Dating from the nineteenth century until the mid-1930s, Britain viewed the Soviet Union as the primary challenger to its leadership in India and China. However, the Russian revolution and civil war, collectivization of the early 1930s, and the Great Purge of the army between 1936-38 greatly weakened the Soviet fighting capability. Until 1933, the Soviet Union remained isolated from world politics. In 1934 the Soviet Union gained membership in the League of Nations and in 1935 signed treaties with France and Czechoslovakia. The 1938-39 border clashes with Japan forced Moscow to divert resources and soldiers to the Far East. In 1939, the Nazi-Soviet pact provided Moscow with a buffer zone on its western border and time to rearm.

In summary, beginning in the early 1930s, Britain confronted a rising Germany, Japan, and Italy on disparate fronts, challenging Britain for regional hegemony. Had Britain confronted a single contender, it could have concentrated its resources in the respective region. However, in encountering several rising contenders in different locales, Britain was confronted with the dilemma of balancing capabilities and

commitments without eroding its economic strength or undermining its national security objectives.

Britain: Declining Imperial Hegemon

The nature of Britain's international commercial policy restricted its range of foreign policy options for restoring the balance between its capabilities and commitments. By the 1930s, Britain had become an imperial hegemon. In 1932, at the Ottawa Conference, Britain broke from its historic Open Door policy, adopting a commercial policy of imperial preferences.¹¹⁶ The Ottawa Conference produced a network of bilateral agreements among the commonwealth countries, granting special trading privileges to British Commonwealth countries. Britain offered imperial preferences in return for concessions by the Dominions for British manufactured goods (the exchange was primarily foodstuffs from the dominions for British manufactured goods). The result was that Britain's exports to the Dominions received preference, but chiefly by increasing the tariff against foreign goods.

Britain's drift toward protectionism meant that London no longer differentiated among emerging contenders. Instead, Britain viewed all rising contenders, both liberal and imperial, as a threat to either its commercial interests or its national security, eliminating the foreign policy option of devolution from its range of security strategies. First, in devolving hegemony Britain risked undermining its economic strength because no successor would maintain Britain's preferential system in the locale. The commercial policies of emerging imperial Germany, Italy, and Japan were directed at replacing Britain's preferential system with their own exclusive economic spheres intended to

¹¹⁶ Many of the dominions were keen on building up their infant industries behind tariffs intended to protect them from more efficient producers (Porter 1994).

promote self-sufficiency and economic autarky. In contrast, the commercial policy of liberal United States called for eliminating Britain's imperial preference system and restoring the Open Door economic order. Consequently, the United States was seen as a challenger to Britain's system of imperial preferences. Second, in devolving hegemony Britain risked eroding its national security because these emerging contenders would capture economic and military assets, increasing the war-making capacity of a future rival.

Britain's growing dependence on trade with its empire meant that more than ever London needed to maintain and defend its access to its foreign commercial interests. Between 1910 and 1935, British exports to its empire rose from 35 percent to 50 percent, while imports from its empire rose from 25 percent to 40 percent (Porter, 1983, 94). With Britain highly dependent on foreign trade, the loss of British access to global markets would have a detrimental effect on Britain's wealth and balance of trade, both key elements of its war chest (and necessary to pay for Britain's rearmament program).

Imperial Japan

Until the 1930s, Anglo-Japanese relations were based on decades of cooperation (see Chapter 3). However, by the 1930s, Japan's commercial and security policies were designed to create an exclusive hegemonic position in East Asia. As the decade progressed, Britain's leaders recognized that Japan wanted to consolidate its hold on North China, dominating the political and economic life of the rest of China, and ultimately extending its control over the rich resources of Southeast Asia. Many in Britain suspected that Tokyo had long-range designs on Australia and even India. For Britain, Hitler's wish to bring into the Reich merely those neighboring areas with substantial German population seemed less objectionable than Japan's declared goal of a

new order in East Asia. The Foreign Office responded by claiming that Britain would not accept changes in the regional status quo (Lowe, 1981).

In the mid-1930s, Japan's leaders announced their intention to implement a "Monroe Doctrine for East Asia." The Amu statement (1934), Hiorta's Fundamental Principles of National Policy (1936), and the New Order (1938) all stressed that Japan regarded East Asia as its exclusive sphere of influence (in violation of the Nine Power Treaty) and objected to western intervention in China (Trotter 1975; Crowley 1966; Lee 1973). The Asian "Monroe Doctrine" first applied to Japan, Taiwan, Korea, north China, and Manchuko (the inner ring of Japanese expansion). However, after 1937, the prospect of Japanese penetration into China south of the Great Wall and into south-east Asia (creating an outer empire) threatened Britain's regional hegemony and the centers of British trade in the Yangtze valley and southern China.¹¹⁷ By 1940, Japan openly declared its sphere of influence to include East and south-east Asia, known as the Greater East Asia Co-prosperity Sphere (Nish 1977; Beasley 1987).¹¹⁸

Britain's leaders, and especially the Foreign Office, opposed Japan's bid for regional hegemony because as an imperial successor Tokyo would block England's future access to its valuable markets, investments, and resources in the locale, especially the potentially lucrative China market.¹¹⁹ As Trotter notes, by mid-1933 the Foreign Office

¹¹⁷ Interestingly, as Tokyo met resistance to its expansion in China, Japan became dependent on imports from the United States for goods such as machine tools and aviation fuel to continue its war effort (Barnhart 1981). Like Germany and Britain, rearmament greatly reduced Japan's stock of foreign currency.

¹¹⁸ In 1941, Japan's war plans called for turning the Far East into a Greater East Asia Co-prosperity Sphere, with Japan, north China, and Manchukuo as its industrial base. The other countries were to provide raw materials and form part of a vast consumer markets, building a degree of economic strength that would enable Japan, first to meet and contain any counter-attack from outside, then to incorporate India, Australia, and Russia's Siberian provinces by further wars (Beasley 1981, 272). The chain of islands stretching from Malaya to northern Australia was of crucial economic and strategic significance to Japan because of the vital raw materials, especially oil (Lowe 1977).

¹¹⁹ In an attempt to side-step Britain, in the spring of 1935, Japan's Ambassador Saito Hiroshi tried to convince Secretary of State Cordell Hull that the two governments should issue a joint declaration

agreed that "Japan's aim was the domination of China and that the failure of western power to assist China would lead eventually to the formation of a Sino-Japanese bloc which would admit westerns only on sufferance" (1975, 35). The combination of the depression, the loss of its market-share in the Americas and Europe, and the costs of rearmament, meant that Britain's trade with China was more important than ever in order to maintain a positive balance of trade.

Britain viewed an emerging Japan as a threat to the existing regional order for a three reasons. First, Britain's leaders believed that Japan would monopolize trade with China, and especially the Yangtze Valley, in the same manner as it did with Manchukuo, excluding Britain from its profitable trade with China. In fact, in 1937, Japan restricted foreign shipping on the Yangtze, eliminating British competition, and in 1938, the Japanese Diet approved a bill creating a North China Development Company, with the goal of establishing monopolies in transportation, communications, electricity, and mining (Nish 1977; Lee 1973).

Second, as part of Japan's attempt to make North China an exclusive Japanese domain, Japan moved to incorporate China into its expanding Yen bloc. Japan unsuccessfully sought to do this by replacing the Chinese currency (the *fapi*) with the Federal Reserve Bank notes. In response, Britain's foreign secretary (Halifax) advocated a 10 million pound loan to the Chinese currency stabilization fund (Lowe 1977).

Third, Japan's ultimate objective was autonomy and economic self-sufficiency.¹²⁰ Japan's leaders defended the concept of the new order, referring in particular to the growth of powerful economic blocs in the world, such as those associated with the British

designating the United States as the stabilizing power in the eastern Pacific and Japan as the stabilizing power in the western Pacific.

¹²⁰ Japan was hit hard by the great depression (Beasley 1987).

Empire, the United States and Latin America, and Russia.¹²¹ Monopolization of this sphere would provide the resources and markets necessary for Japan to build the industrial strength it needed to confront the Soviet Union and the Anglo-American states (Beasley 1987). After 1937, the Greater East Asia Co-Prosperity Sphere, stretching from Manchuria to the Dutch East Indies, would grant Japan control over the region's tin, oil, rubber, bauxite and other strategic raw materials.

Imperial Germany

Like Japan, Britain viewed Germany as an imperial challenger seeking to create a closed self-sufficient sphere in Central and Eastern Europe.¹²² Such a sphere would block Britain's future access to the region and strengthen Germany's position when it turned westward. Like Japan, Germany moved from a policy of autarky and self-sufficiency to a policy of forceful expansion known as *Lebensraum* or the creation of living space.

In the early 1930s, Hitler's economic minister Hjalmar Schacht advocated solving Germany's trade and economic problems by integrating Germany into the world economy and searching for colonies (Hildebrand 1970). However, by 1936, Hitler rejected returning Germany to the world economy arguing that foreign trade could not solve Germany's economic and political problems. Instead, Hitler supported a policy of economic autarky. Hitler's Four Year Plan was intended to reduce German dependence on foreign suppliers and to conserve available foreign exchange for the importation and

¹²¹ Japan viewed Korea and South Manchuria as an area of prime importance. Japan's investment in China, including Manchuria, represented 82.9 percent of its total foreign investment (Trotter 1975, 19).

¹²² British leaders recognized that massive German military spending would undermine Germany's fiscal strength, further encouraging German expansion in order to acquire critical resources (in 1938, 17 percent of Germany's GNP was being spent on rearmament). Consequently, in the late 1930s, Britain's leaders discussed economic appeasement in the form of foreign credits and lower tariffs to Germany so that Hitler could purchase the goods Germany needed, quelling the urge to expand (Kennedy 1981; MacDonald 1972).

stockpiling of strategic materials and food imports (foreign exchange was needed to pay for raw-material imports for rearmament). The urgency was to prepare the army and the economy for war in four years (Holborn 1966). To achieve self-sufficiency, the Plan created rudimentary synthetic oil and rubber industries, as well as increased home production of certain raw materials, such as iron and light metals, which could be substituted for unavailable metals (Weinberg 1980). However, the problem with such a plan was that German dependence on overseas raw materials would always require substantial German participation in world trade (Kaiser 1980; Murray 1984, 5-6)¹²³ Neither a policy of participation in the global trading order nor economic autarchy could satisfy Germany's economic needs (Craig 1978).

For Hitler, the ultimate solution lay only in the conquest of *Lebensraum*; the acquisition of greater living space in Eastern Europe (Calleo 1978; Carroll 1968). Hitler proposed to solve Germany's economic problems by conquering Austria and Czechoslovakia in order to clear land for German colonization (Kaiser 1980). A dominated Eastern Europe would serve as a territorial and agricultural base from which Germany could compete with the British Empire and the United States.¹²⁴

Imperial Italy

Up until the rise of Mussolini in 1922, Italy pursued a liberal commercial policy. Beginning in 1935, like Japan and Germany, Mussolini advocated a commercial policy of economic autarky. Italian agricultural policy ("battle for wheat") was aimed at freeing Italy from dependence on foodstuffs from abroad. However, Italian autarky was largely

¹²³ Not all German policy makers agreed with Hitler's drive for self-sufficiency. Schacht rejected the autarky theories of the Nazis, recognizing that German dependence on overseas raw materials would always require substantial German participation in world trade.

¹²⁴ Whereas the conservatives wanted to pursue colonial interests, refraining from action in Europe.

impossible since Italy was highly dependent on foreign strategic raw materials and imported energy (Knox 1984a).

Italy's commercial policy of autarky concerned Britain. Britain feared that an economically backward country like Italy would block Britain's future access to its markets and investments in the region. Unable to compete with more efficient foreign powers, Italy would exclude them from any region which it came to dominate. As one author claims, "Italy was in decline and therefore dangerous" (Pratt 1975, 84).

Liberal United States

In contrast to Germany, Japan, and Italy, the United States was a liberal contender which viewed Britain as an obstacle to the liberalization of global trade after the war. In the aftermath of the Ottawa Agreements of 1932, one goal of the United States was the restoration of the Open Door economic order (Appleman 1972; Gardner 1956; McKercher 1993). In fact, Secretary of State Cordell Hull called Britain's Ottawa Agreements the "greatest injury, in a commercial way, that has been inflicted on this country since I have been in public office." Britain's imperial preference system (as well as Germany's *Mittleuropa* in central and eastern Europe and Japan's New Order in Asia) was seen as a barrier to American recovery from the depression since foreign markets could provide an outlet for surplus agricultural and manufactured products (Williams 1972).

The United States used the Atlantic Charter and the Lend-Lease Act to force Britain to reverse its imperial preference system (Gardner 1956; Kimball 1971).¹²⁵ The United States tried to write a nondiscrimination clause into the Atlantic Charter (Anglo-

¹²⁵ Interestingly, the State Department led the fight to use the Lend-Lease Act to eliminate Britain's preferential system, while the Treasury Department opposed such moves (Kimball 1971).

American declaration of war aims, signed in 1941) calling for "access, on equal terms, to the trade and to the raw materials of the world which are needed for their economic prosperity" (cited in Gardner 1956, 123). However, for the sake of good Anglo-American relations, FDR agreed to Churchill's request to water down the accord by replacing it with "due respect for our existing obligations" (cited in Kimball 1971, 250). The Lend-Lease Act was less vague. In the Lend-Lease Act (1942), Clause VII called for "the elimination of all forms of discriminatory treatment in international commerce" (cited in Kimball 1971, 253).¹²⁶ The goal of both clauses was to destroy Britain's imperial economic bloc and to breakup the sterling area. With such a policy, the United States operated at cross purposes with Britain in the Middle East and Asia.

In addition to destroying Britain's imperial preference trading system, the United States sought to dismantle the British Empire (at least until the rise of the Cold War), by promoting a policy of self determination. Part III of the Atlantic Charter called for "sovereign rights and self-government restored to those who have been forcibly deprived of them." On India, Roosevelt repeatedly offered advice to Churchill on the desirable steps to Indian independence.

In summary, although Britain confronted a mix of emerging liberal and imperial contenders, its imperial foreign economic policy ensured that it viewed all rising contenders as threats to its commercial and security interests. An imperial Germany, Italy, and Japan sought to replace Britain's imperial preference system with their own exclusive spheres, while a liberal United States sought to reverse Britain's preference system. Consequently, the nature of Britain's foreign commercial policy excluded the foreign policy option of devolution. In devolving regional leadership, Britain would

¹²⁶ One concern in Congress was that Lend-Lease would help Britain compete with the United States in world markets. Consequently, there were strict rules to what Britain could reexport, and Lend-Lease was terminated abruptly at the end of the war.

strengthen the war-making capacity of these challengers while losing exclusive access to its valuable markets, investments, and resources in the locale.

Domestic Constraints on Britain's Foreign Policy Adaptability

The nature of Britain's international economic policy limited that country's range of foreign policy options for managing its decline to either a strategy of increased resource extraction or one of accommodation. Britain's foreign policy alternatives were further restricted by domestic political constraints. Confronting different emerging contenders for leadership in disparate parts of its empire, Britain's leaders debated whether to restore the balance between its capabilities and commitments by increasing its military capabilities or reducing the costs of hegemony. In particular, whether to increase Britain's rate of domestic resource extraction for military spending or to reach some accommodation with imperial Germany, Japan, and/or Italy in order to limit their military buildup. The immediate cause of this debate was Japan's invasion of Shanghai and Hitler's announcement of Germany's rearmament program. In response, the three military services and the Foreign Office advocated a large military buildup; only from a position of strength could Britain negotiate with its rivals, anything less would tempt the emerging contenders to challenge Britain's regional hegemony by preemptive war. The Treasury Department countered that Britain's economy could not sustain a massive rearmament program, favoring a policy of accommodation. A series of smaller debates focused on the nature of Britain's rearmament program and how to prioritize defense expenditure among the services (Peden 1979a, b; Shay 1977; Trotter 1975). The outcome of this debate would influence whether Britain's foreign policy of domestic resource extraction or accommodation was more attractive.

Fiscal Orthodoxy and the Chancellor of the Exchequer

As the central department of finance, Britain's Treasury Department was responsible for oversight of all government spending (Peden 1979a; Shay 1977; Parker 1975; Kennedy 1983). The Treasury had considerable influence over what proportion of the national wealth should be allocated to defense and how the services would allocate their resources. First, the Treasury was responsible for levying and creating new taxes. Second, since there was no Ministry of Defence, the allocation of funds was negotiated directly between the Treasury and the three services. This meant that the Treasury also had the function of coordinating among the services and a substantial voice over Britain's grand strategy (see the Appendix for a discussion of the concept of Treasury Control; Peden 1979a; Shay 1977).¹²⁷ The autonomy of Britain's Treasury was intended to safeguard the country's fiscal strength by preventing excessive extraction of societal resources for military purposes, while allowing for modest increases in the rate of defense spending.

The philosophy of the Treasury remained rooted in the Gladstonian tradition of limited government expenditure, low taxation (especially direct taxation), and minimal intervention in the economy in order to safeguard Britain's financial strength.¹²⁸ The heart of the Treasury's position was that finance was the fourth branch of defense, upon which the three branches of the Services (and traditionally Britain's allies) would rely in the event of a prolonged war. Britain's leaders intended to pay for a prolonged war by running down its war chest, which was composed of gold and foreign exchange reserves,

¹²⁷ Fisher, the Permanent Secretary of the Treasury, viewed the Treasury as a 'general staff'. In 1936, Sir Thomas Inskip was appointed Minister for the Co-ordination of Defence. This fell well short of a Minister of Defense because it lacked a department and had no executive powers. The Treasury also had to prevent a chaotic competition among the services for scarce resources which would have slowed down the rate of rearmament.

¹²⁸ The Treasury adamantly opposed any suggestion of government industrial control during peacetime.

the sales of foreign securities, and its credit-worthiness (Peden 1979a, 1984).

Consequently, the Treasury opposed ever-increasing military spending in peacetime because it would result in a balance of trade deficit, heavy peacetime borrowing and taxation, a budget deficit, and/or inflation, or a reduction in Britain's war chest.¹²⁹

In peacetime, the priority of the Treasury was to lower direct and indirect taxes and to begin repayment of the Sinking Fund, leaving little room for additional military spending. As the backbone of Britain's war chest, these two financial reserves would be mobilized in the event of a prolonged conflict. First, the Treasury opposed high taxation during peacetime because it would leave little room for expansion during wartime and it would erode foreign confidence in Britain's economic stability. For the Treasury, this meant that in peacetime its priority was to ensure that defense spending did not exceed the level which the economy could sustain. Second, to protect Britain's international credit-worthiness, London continued its debt repayment to the Sinking Fund. While Britain's tradition of war finance had dictated that the national debt should be kept down to the lowest possible level by paying for wars out of current taxation, and in particular through an income tax, the outcome of war was often high debt. However, failure to meet past debt responsibilities would damage Britain's ability to obtain new foreign loans at reasonable interest rates during an emergency. Thus, the Treasury's peacetime goal was to husband Britain's financial strength for a prolonged conflict by restricting its current rate of extraction for military and societal spending.

¹²⁹ The limit of borrowing was dictated by the classical economic belief that a nation could only borrow as much as its citizens saved (Shay 1977, 160-161). Any borrowing in excess of this limit would simply mean printing money which would give way to inflation and inflation would damage Britain's international credit and trade.

Defense Requirements Committee (D.R.C.) and the Treasury's Reply

In 1919, financially exhausted from World War I, Britain's Cabinet implemented the Ten Year Rule, calling for the armed services to assume, when drawing up their yearly estimates, that Britain would not become involved in a major war for ten years.¹³⁰ In 1932, in the aftermath of Japan's invasion of China and Germany's announcement of rearmament, the Cabinet revoked the Ten Year Rule, warning that this did not justify immediate increases in defense spending without considering Britain's economic crisis. However, with the suspension of the Ten Year Rule, the services began to make new demands for military expenditure. Consequently, in 1934, the Cabinet created the Defense Requirements Committee (D.R.C.) with the goal of preparing a program for Britain's rearmament.¹³¹

Between 1934 and 1935, the D.R.C. issued three reports on Britain's rearmament program. In the initial stages, the D.R.C.'s rearmament program was intended to remedy, by 1939, the "worst deficiencies" in the defense services that disarmament and the Ten Year Rule had caused, while a longer period would be necessary to remedy all military deficiencies.¹³² According to the D.R.C.'s First Report, in the Far East, the Navy would

¹³⁰ The Ten Year Rule assumed "that the British Empire will not be engaged in any great war during the next ten years, and that no Expeditionary Force is required for this purpose." Consequently, defense spending fell from 604 million pounds in 1919, to 111 million pounds in 1922, to a low of 103 million pounds in 1932 (2.8 percent of Britain's GNP). The combination of the depression, societal pressures, and Treasury control contributed to the further reduction in military spending. The outcome was that actual military preparedness fell well below the minimum levels dictated under the Ten Year Rule.

¹³¹ The D.R.C. consisted of the Chiefs of Staff Sub-Committee or C.O.S. (the C.O.S. was made up of the Chief of Naval Staff, the Chief of the Air Staff, and the Chief of Imperial General Staff), and the secretaries of the Foreign Office and the Treasury.

¹³² Under this program, Britain would spend much less than Germany on rearmament. Germany was spending the equivalent of 500 million pounds a year, while in 1937 Britain spent on 137 million pounds (Peden 1979a).

In 1936, the five year rearmament program approved by the Cabinet relaxed the procedure for approving the annual review of Estimates. To increase the speed of rearmament, instead of withholding sanction until the entire Vote had been approved by the Cabinet, the Treasury would now sanction items

play the primary role, while the Army and Airforce would help defend ports and bases. Since 1922, Britain's leaders had agreed that in the event of war in the Far East, the main fleet would sail to Singapore via the Mediterranean, with reserves left behind to defend the homewaters. To deal with Japan, the D.R.C. called on Britain to modernize its capital ships and to buildup Singapore's defense by 1938 in order to demonstrate Britain's commitment to the region, followed by a new attempt at diplomatic rapprochement with Tokyo (Gibbs 1976). The D.R.C.'s Third Report (1935) called for an upward revision of the navy's existing One-Power Standard to a Two-Power Standard (referred to as the New Standard).¹³³ The New Standard would ensure that the Royal Navy would be sufficient in size to send a fleet to Singapore to meet the Japanese threat in the Far East, while maintaining a force in its homewaters to defend against Germany and a force to defend its trade routes (Howard 1972).

While the D.R.C. viewed Japan as the immediate threat, Germany was seen as the long range threat to Britain's national security interests.¹³⁴ Britain's primary fear was that Germany might launch a preemptive knock-out air strike against Britain. In order to deter a German air attack, the D.R.C. recommended the completion of a fifty-two

individually. Also, contracts were placed on a long term basis to accommodate the on-going nature of rearmament (Peden 1979b, 40).

¹³³ The Navy had two on-going debates with the Treasury. The first was over the role of the Navy. For the Navy, Japan posed a greater threat to Britain's interests than Germany. The First Lord of the Admiralty stressed that the entire Empire in the East, from India to New Zealand was threatened by the possibility of further Japanese expansion. Second, and related to the role of the Navy was the size (and hence funding) of the Navy. The Navy called for an upward revision of the existing One-Power standard (adopted in 1925) to a Two-Power. Not until August 1939 did Cabinet accept a Two-Power Standard of twenty battleships capable of taking on both Japan and a European enemy at the same time.

¹³⁴ Much of the early discussions in the D.R.C. focused on a dispute over Britain's priorities: whether the Continental or Far Eastern theater would receive priority. The Navy favored the Far East, while the Air Force emphasized the dangers of an air threat from Germany, and the Army called for the need for a Continental Field Force. The Foreign Office (Vansittart) and the Treasury (Fisher) argued that Germany posed the greatest threat. Hankey was convinced that Japan posed the long term threat to Britain's empire. However, the compromise reached by Hankey was that Japan posed the immediate threat and Germany the long term threat (Smith 1978).

squadron bomber and substantial reinforcements of the Fleet Air Arm. The D.R.C. also called for the creation of air reserves. An Army expeditionary force was to be prepared to put four infantry divisions, one tank brigade, one cavalry division, and two air defense brigades on the Continent within one month of war, with the goal of defending the Low Countries (Gibbs 1976).

Even though the Secretary of the Treasury, Warren Fisher, played an active role in shaping the D.R.C.'s Report, the Chancellor of the Exchequer, Neville Chamberlain, (1931-37) criticized Hankey's rearmament program.¹³⁵ Chamberlain condemned the D.R.C.'s reports as the "broad road which leads to destruction" (Howard 1972). To Chamberlain, the heart of the matter was how the additional military expenditure called for in the D.R.C.'s reports could be financed without undermining Britain's fiscal strength. His reply to the D.R.C.'s recommendations was that although facing an increasingly hostile international environment, Britain had to balance its immediate military preparedness against the potential of a long and costly war.

For Chamberlain, the D.R.C.'s intensive peacetime rearmament program would drawdown the financial resources Britain needed in the event of a prolonged war (Kennedy 1983). First, Britain was already running a trade deficit and the D.R.C.'s rearmament program would increase the size of this deficit.¹³⁶ Britain's dependence on foreign imports for food, raw materials, and engineering products required that England maintain a high level of exports in order to strengthen its balance of payments. Since rearmament would require an increase in imports, Britain would have to increase its exports or run a negative balance of payments, drawing down its foreign currency and

¹³⁵ The rivalry between Chamberlain and Hankey was nurtured by the fact that Hankey had a naval background and perhaps favored the navy, while Chamberlain preferred the airforce (Greenwood 1994).

¹³⁶ Between 1931 and 1938, Britain ran a balance of trade deficit and a balance of payments deficit in every year except for 1935 (Murray 1994, 403).

gold reserves (i.e., its war chest). The Treasury feared that a long run balance of payments deficit would reduce international confidence in the stability of the pound, further undermining Britain's financial reserves.¹³⁷

Second, rearmament would cause dislocation of both skilled labor and industry. After World War I, Britain experienced a rapid demobilization of its war industry (Peden 1979a, b).¹³⁸ The movement of skilled labor and the conversion of civilian industry to military production would hurt Britain's balance of trade by diverting labor and factories from the production of foreign exchange earning export goods. Third, Britain could only finance the D.R.C.'s rearmament program by large increases in borrowing and/or taxation (Parker 1975; Peden 1979a, 1984). Borrowing was opposed by the Treasury because deficit spending would cause inflation. Inflation would adversely affect trade by increasing the price of Britain's exports, resulting in a rise in imports and a decline in exports. Alternatively, increased taxation was opposed by the Treasury because it would drawdown Britain's ability to mobilize additional resources in the event of prolonged war and jeopardize Britain's economic recovery (Peden 1979a; Parker 1975).¹³⁹ The Treasury argued that if taxes were increased too much (for military or social welfare), it would lower consumer demand, hindering Britain's economic recovery.

¹³⁷ A recession in the U.S. further reduced the demand for British exports.

¹³⁸ According to Parker, the main barrier to rearmament was not the Treasury's concern about finance but a shortage of skilled labor, which was confirmed by the Ministry of Labor. This argument challenges Keynes' argument that Britain needed to simply pursue a strategy of deficit spending to resolve its weak economy. The lack of skilled labor meant that deficit spending would be inflationary. Lord Weir, the government's industrial adviser, explained in January 1936 that many of the industries which rearmament rested were already at full employment (Peden 1979a).

¹³⁹ Chamberlain also worried about the negative political repercussions of increased taxation for additional defense spending (the political survival of the Conservatives depended upon bringing Britain out of the depression and back to prosperity). The government desire to grant tax reductions and complete the return of the wages of government employees to their pre-austerity budget levels, while balancing the budget, meant that any increase in defense spending was not welcome.

Finally, Chamberlain argued that a strong British economy would deter emerging contenders from challenging its regional hegemony (Peden 1984; Smith 1978; Coughlan 1972; Greenwood 1994). From Britain's perspective, it had a financial advantage over its enemies in a long war due to its strong economy and large war chest. In particular, Britain's superior war potential would deter a rising challenger because any conflict would become a costly and protracted war, which Britain would win.¹⁴⁰ Consequently, Britain had to safeguard its fiscal strength, for if the emerging challengers detected a strain in Britain's economy, they would no longer be deterred by the prospect of a long war (Peden 1979a).

With finances in mind, Chamberlain put forth an alternative rearmament program to the D.R.C.'s with the intention of restoring a balance between Britain's capabilities and commitments by lowering the costs of hegemony. For Chamberlain, Britain's economic staying power meant that it was better placed than its rivals to finance a prolonged and sustained war (Smith 1978). The real threat to Britain's national security was from a German preemptive air strike. Consequently, Chamberlain's rearmament strategy emphasized building up the R.A.F. to create a "shop window" deterrent against a German air attack by constructing as many front line bombers as possible, with few air reserves.¹⁴¹ Only in the long run should Britain pursue an offensive posture; if war never came, Britain would not undermine its economy with unnecessary military spending. In the

¹⁴⁰ The Treasury position was that "our general economic strength is not merely the condition of continued prosperity, but as a deterrent to would-be aggressor it is little less important than ships and aeroplanes and guns" (CAB 21/534).

¹⁴¹ To deter Germany, the air proposals were publicly announced (Gibbs 1977, 107). One debate between the Treasury and the Air Staff centered on the question of reserves. The Air Staff demanded that sufficient reserves also be provided in order to maintain Britain's front-line strength despite losses, calling such a policy "window dressing" (Gibbs 1977). The Treasury argued that the bulk of the reserves should be provided after 1939 (Peden 1979a). A second debate, after 1937, centered on the ratio of bombers to fighters. Later, Chamberlain and Fisher would favor fighters over bombers, while the Air Staff favored the latter.

short run, the buildup of the R.A.F. would deter Germany by demonstrating that it could not win a short war with a knock-out blow, while in the long run, Britain's economic strength would demonstrate that Germany could not win a protracted war. In 1937, with the advent of radar, which would allow fighters to find and confront an enemy's attacking bombers, as well as with advances in fighter planes, the Treasury called for the construction of cheaper fighter planes over more expensive bombers (Peden 1979a; Greenwood 1994). This purely defensive strategy would show Germany that it had no chance of successfully knocking Britain out in a single blow (Smith 1978). Once the nation survived, Britain could focus on a more offensive and Continental role.

Building up the R.A.F. would allow Britain to reduce the costs of hegemony without retrenching from its empire (retrenchment would strengthen the war-making capacity of the rising challengers). By 1938, the notion of a Continental commitment virtually ceased to exist (Howard 1972). For Chamberlain, a Continental army was expensive and would cause economic dislocation.¹⁴² The advent of long range aircraft meant that the R.A.F. could simply fly over the Low Countries, reducing their strategic worth and further reducing the Continental role of the Army. Also, Chamberlain encouraged the Cabinet to oppose any upward revision of the Navy's One-Power Standard to a Two-Power Standard. Instead, Chamberlain took the position that it was vital to get on better terms with Japan, even at the risk of undermining Anglo-American relations.¹⁴³

¹⁴² In contrast to some critics, Chamberlain did not oppose sending an Army to the Continent eventually (Murray 1979a). Instead, he opposed the building of an Army in peacetime and in the initial stages of war (Gibbs 1977). However, Britain rarely committed large armies to the Continent, instead preferring to play the role of financial backer to its allies. As well, British labor kept at home would build the equipment to support the armies of its continental allies. Finally, the outbreak of civil disturbances in Palestine beginning 1936 required 18 battalions of the British Army.

¹⁴³ Since Chamberlain viewed Germany, not Japan, as the main menace, he argued that Singapore should be completed "if only out of good faith to the Dominions" and used as a base for submarines and other light craft (Gibbs 1977, 124).

The immediate issue for the Treasury was how to pay for rearmament.¹⁴⁴ In a breach of financial orthodoxy, in 1937, under the Defence Loans Act, the government borrowed 400 million pounds over a five-year span at a rate of 80 million a year (the business community supported borrowing over increased taxation). In addition to direct and indirect taxation, industries which gained from the boom set off by rearmament were taxed a percentage of total profits. A second problem for rearmament was the shortage of skilled labor. Chamberlain bitterly opposed proposals that skilled labor be transferred from civilian factories to military industries on the grounds that it would lead to dislocation in the economy, weakening Britain's exports. The Treasury also opposed industrial mobilization of the economy for rearmament on the grounds of a laissez-faire industrial policy.

Chamberlain, Prime Minister, Anschluss and Munich, and the Decline of Treasury Control

In 1937, Neville Chamberlain succeeded Stanley Baldwin as Prime Minister, and John Simon became the new Chancellor of the Exchequer. On becoming Prime Minister, Chamberlain suspended Britain's rearmament program until it was reviewed in light of the nation's financial and industrial resources. The review was conducted by Sir Thomas Inskip, whose first report called for a policy of "rationing" or restrictions on the aggregate sum for each service in order to force each department to prioritize its individual programs.

The Treasury's concern was not unwarranted. The level of rearmament achieved in 1937 and 1938 threatened Britain's financial stability and fiscal strength (Peden 1984). By 1939, Britain had already diminished its war chest to pay for the necessary imports

¹⁴⁴ In response to the defense budget of 1937, Chamberlain warned that "Before long, people would be talking about an unbalanced Budget, and we might find that our credit was not so good as it was a few years ago."

(compared to 1914, Britain had less resources and could not borrow from the United States). In the event of a long war, Britain needed financial resources in order to purchase supplies overseas. However, greater rearmament would divert additional industrial capacity from exports and increase imports, contributing to a negative balance of payments. In addition, new loans for rearmament would undermine confidence in Britain's financial position, threatening its credit worthiness (foreign loans and credit) and reducing Britain's gold and foreign exchange reserves, all necessary to sustain a prolonged war.

Members of the Navy and the Army countered that Britain could afford a large rearmament program.¹⁴⁵ Proponents argued that the danger of underrating Britain's defense may lead to "defeat in war and complete destruction" while the danger of overrating the nation's financial resources can "only lead to severe embarrassment, heavy taxation, lowering of the standard of living and reduction of social services" (Shay 1977, 201). Furthermore, the Foreign Office opposed any accommodation with Japan, Germany, or Italy, and some called for a preventive attack, especially against much weaker Italy, while the military advantage was still with Britain (Trotter 1975; Shay 1977; Peden 1979a). It was feared that closer ties with Japan would signal acceptance of Japan's expansion in China and alienate the United States.¹⁴⁶ Similarly, for Eden there was no point at which Hitler would cease expansion that was compatible with Britain's interests. Finally, coming to terms with Italy would mean recognizing it as the leading Mediterranean power (Carr 1937).

¹⁴⁵ On the competition between the Foreign Office and the Treasury over foreign policy see Lowe (1981); Trotter (1975).

¹⁴⁶ This policy might give Japan a free hand against the Soviet Union (and Russia would cease to act as a potential check on Germany) as well as the added confidence in her expansionist tendencies

In 1939, in his Final Report on Defense Expenditure in Future Years, even Sir Thomas Inskip broke with the Treasury strategy of reducing the costs of hegemony (Shay 1977; Smith 1978). Inskip's report proposed that the bulk of the five year rearmament spending be concentrated in the coming two years. In negotiating with the emerging challengers from a position of strength, Britain could reach an agreement, eliminating the need for spending on the longer-range projects. If Britain failed to reduce the number of threats by diplomacy, than additional defense spending would be necessary. The benefit of his plan was that if appeasement failed, the nation would not be left unarmed.

Budgetary rationing did not survive the Anschluss, and early 1939 saw the decline of Treasury control over rearmament (Dunbabin 1983; Gibbs 1976). The Anschluss and the Munich Agreement gave the services a new reason to reintroduce defense programs that had been previously rejected. First, the Army's continental role was restored (Bond 1980; Howard 1972). The Cabinet agreed to create a full-scale Continental army of thirty-four divisions. The Navy was finally given financial carte blanche for a Two-Power Standard, however, too late for the war.¹⁴⁷ The Air Ministry also took advantage of the Munich crisis, calling for a major expansion in fighter production.

However, as Chamberlain had predicted, Britain's economy could not sustain this massive rearmament program. Britain's defense spending jumped from 8.1 percent of GNP in 1938, to 21.4 percent in 1939, to 51.7 percent in 1940 (Dunbabin 1975, 588). Between April, 1938, and March, 1939, Britain's gold reserves alone declined from 800 million pounds to 300 million pounds (Parker 1975; Peden 1984). By 1941, gold stocks had dwindled to almost nothing and Britain was dependent upon American financial and military assistance to defend its empire.

¹⁴⁷ While no decision was taken before the war to abandon the Far East, by May, 1939, the Admiralty's Director of Plans recorded that only four capital ships would be available for the Far East if Britain were at war with Italy and Germany (seven if Italy was neutral; Peden 1979a).

In summary, in the decade prior to World War II, the Treasury Department was able to effectively scale back proposals for Britain's rearmament program. While recognizing the dangers of this strategy, the Treasury was primarily concerned with protecting Britain's fiscal strength in peacetime, husbanding its resources in the event of a prolonged war. As Inskip wrote "If we are to emerge victoriously from such a war, it is essential that we should enter it with sufficient economic strength to enable us to make the fullest use of resources overseas, and to withstand the strain."

Britain's Response: Managing Hegemonic Decline

Alternative Strategies for Restoring the Balance between Capabilities and Commitments

Encountering a rising Italy, Japan, Germany, as well as the United States and the Soviet Union in disparate corners of its empire, Britain's existing military capability was overwhelmed. As Bradford Lee notes "British statesmen from Lansdown to Churchill grappled with one overriding problem, how to maintain Britain's leading position in the world as her relative power declined. Rarely was this task more difficult than in the late 1930's" (1973, 1). As an imperial hegemon, Britain selected from a different range of strategies for managing decline as compared to its options prior to World War I. Britain's leaders debated two strategies to correct the imbalance between capabilities and commitments, domestic resource extraction to increase its military capability or accommodation to reduce the number of potential threats and the cost of hegemony.

After the Ten Year Rule was revoked in 1932, the Services, the Foreign Office, the D.R.C., and even Inskip, called for the Prime Minister to **increase domestic extraction** in order to implement a large rearmament program. They argued that only from a position of strength could Britain negotiate with the emerging contenders (Coughlan 1972). Such a position would require that Britain modernize its capital ships

and increase the Fleet Air Arm; buildup a reserve fuel oil for the fleet; and complete the Singapore naval base by 1938. Failure to rearm would only tempt the rising contenders to launch a preemptive strike against Britain's regional hegemony.

In contrast, Prime Minister Chamberlain called for Britain to seek some rapprochement with Japan, Germany, and/or Italy. **Accommodation** would slow down the military and economic ascent of these emerging contenders, and reduce the costs of hegemony to a level that Britain could afford. First, for Chamberlain "Germany was the key to Britain's world predicament." If Germany could be appeased, England's strength would then suffice against Italy or Japan. Second, by improving relations with Japan, Britain could concentrate its limited resources on defense spending in Europe and avoid the nightmare of a costly two front war in separate parts of its empire. Chamberlain advocated accommodation with Japan, even if this undermined Anglo-American relations (Gibbs 1976, 94; Barnett 1972; Lowe 1981).

Accommodation

As a domestically constrained imperial hegemon, Britain's most attractive option to manage its decline was a foreign policy of accommodation. Although aware of the dangers of this foreign policy strategy, Britain had few alternatives. Domestic resource extraction for rearmament was rejected because Neville Chamberlain, among others, argued that Britain's economy could not withstand the pressures of a massive rearmament program. Had London initiated a rearmament program to keep pace with the combined military buildup of Germany, Japan, and Italy in the early 1930s, Britain risked drawing-down its war chest well before the outbreak of World War II, leaving it few resources in the case of a prolonged conflict. Alternatively, devolution was rejected because it risked

strengthening the immediate war-making capacity of imperial Germany, Italy, and Japan, while endangering Britain's future access to its commercial interests in these locales.

In accommodating Japan, Germany, and Italy, Britain remained in the great power ranks longer than if the country had pursued its alternative options. Through concessions, Britain was able to balance its capabilities and commitments by lowering the cost of hegemony. In particular, a strategy of accommodation allowed Britain to impede the ascent of the imperial challengers (if only temporarily) and to lower the costs of leadership in the Far East, Mediterranean, and its homewaters. In reducing the risk of a preemptive war and the likelihood of a costly arms race, Britain lightened the unbearable burden of preparing for a preventive war against three rising challengers in disparate parts of its empire to a level that it could afford, gaining time to rearm at the moderate pace dictated by rationing and postponing a showdown until its armed forces had been further strengthened. As one author summarizes, "the balance struck between defensive strength and economic stability in 1937-1939 at least allowed Britain to survive the initial Nazi onslaught, and to have the financial credit to draw upon the considerable resources of the Empire and Commonwealth during the war" (Peden 1984, 26).

However, in the long run, Britain accelerated its decline from the ranks of the great powers by strengthening the war-making capacity of imperial Germany, Italy, and Japan. Concessions allowed these emerging challengers to buildup their military and/or expand without the fear of a British preventive attack. However, since none of these rising contenders was willing to accept a permanent junior position in the locale and since each preferred an alternative commercial arrangement, preemptive war was seen as inevitable. Consequently, as the arms control and arms limitation agreements expired, and/or when the challengers cheated on the accords or repudiated them, Britain had

insufficient military capability to defend its imperial commitments, leaving it weak and vulnerable to preemptive attack everywhere.

Accommodation of Germany

Britain's policy-makers, and especially Prime Minister Chamberlain, argued that Germany was "the key to Britain's predicament" of too many rising challengers and too few resources (Barnett 1972; Medlicott 1969; Cozier 1976). If Britain could deter Germany or at least slow-down its rate of military and economic ascent, then neither Japan nor Italy would confront Britain alone, and if they did, Britain would have sufficient resources to defend against attack. In Europe, Britain reached an accommodation with Hitler, limiting Germany's "illegal" rearmament (conscription, remilitarization of the Rhineland, and naval and air production) and restraining the extent of its territorial expansion in central Europe. However, Britain was unwilling to devolve hegemony over eastern Europe to Germany for fear that Hitler would harness its resources against western Europe.

First, in 1935, London and Berlin signed the Anglo-German Naval Agreement. The Naval Agreement permitted the maintenance of a German navy no larger than 35 percent of the size of Britain's surface fleet and 45 percent in submarines (Hall 1976; Watt 1956; Salerno 1994; Haraszti 1974).¹⁴⁸ Limiting the German fleet assured Britain of an adequate defense at home, while providing for a sufficient force to protect against Japanese aggression in the western Pacific. To a British Admiralty concerned by its weakness in the Far East, the Naval Agreement was attractive since it made the dispatch of a force to Singapore more feasible by granting Britain a substantial naval advantage in

¹⁴⁸ With this agreement, Britain unilaterally altered the naval limitation provisions of the Versailles Treaty, harming relations with France and Italy.

European waters (Howard 1972). Britain had added pressure to reach an agreement with Germany, because in 1934, Japan announced that it did not intend to renew the Washington and London Naval Treaties when the latter expired in 1936.

The Anglo-German Naval Agreement also prevented a repeat of the costly naval race that occurred prior to World War I. An Anglo-German agreement would allow Britain to rearm at a moderate rate without threatening its fiscal strength or undermining its national security, and permit Germany to buildup its fleet without the threat of a preventive British strike. In London there was also the belief that bilateral negotiations might move from naval matters to the urgent question of air power and a multi-lateral Air Pact directed against surprise aerial bombardment. Between 1934 and 1938 there were several attempts to conclude an air pact with Germany.

Second, in a series of high level visits with Hitler, British leaders announced their willingness to accommodate Hitler's demands in Eastern Europe (i.e., to revise the Versailles Treaty in terms of self determination in Danzig, Austria, and the Sudeten part of Czechoslovakia) in exchange for moderating Germany's foreign policy (Barnett 1972; Schwoerer 1970; Hildebrand 1970; Craig 1978; Calleo 1978). The overall aim was to integrate Germany into a four-power European order (with Britain, France, and Italy) and bind Germany to a new European system (replacing the Versailles Settlement) in exchange for German claims on Austria, the Sudetenland, Danzig, and increased economic influence in southeastern Europe (Hillgruber 1981). In 1934, Anthony Eden met with Hitler, calling for limitation of armaments and German return to the League of Nations in exchange for territorial concessions. A year later, during the Simon-Eden meeting with Hitler (Simon was Britain's Foreign Minister), Britain announced that it would allow Berlin to take economic leadership over Central and Eastern Europe in exchange for Germany's commitment to a permanent European peace settlement, return

to the League of nations, respect for the independence of the Central and East European countries, and the prospect of a limitation of armaments (Holborn 1966; Hildebrand 1970).¹⁴⁹

In 1936, Eden and the Foreign Office put-forth a detailed plan for pursuing a *modus vivendi* with Germany (Medlicott 1968). It proposed an air-pact (to replace the Locarno Treaty), limitation of land armaments, and recognition by Britain and France of Germany's special interest in Central and Eastern Europe. Consequently, in 1937, in a meeting with Hitler, Lord Halifax acknowledged Germany's economic position in Central and Eastern Europe, in exchange for German involvement in a comprehensive European settlement (Schwoerer 1979). Halifax mentioned that "the British did not believe that the status quo had to be maintained in all circumstances" and "among the questions in which changes would probably be made sooner or later were Danzig, Austria, Czechoslovakia."¹⁵⁰ For Britain, such an Anglo-German understanding would secure a European peace.

In 1938, Britain and Germany signed the Munich Agreement. The Munich Treaty was Britain's final diplomatic initiative with Germany. It gave Germany undisputed control over southeastern Europe on the condition that Hitler would not go to war and would respect certain rules of international law (Kaiser 1980; Hildebrand 1984). In particular, an Anglo-German declaration signed at the Conference stated that the two states would deal with future questions of common concern by "the method of consultation" (Holborn 1966). Britain hoped that Germany's future expansion in

¹⁴⁹ According to Hildebrand (1970), Göring sought to direct Hitler along the path of a peaceful 'liberal-imperialistic' policy by creating a strong position for the Reich in Europe and overseas. Britain hoped to use colonies to compensate Germany for the territory it demanded in Eastern Europe (Shay 1977). After the 1935 meeting, Hitler capitalized on the issue of the return of colonies as a bargaining chip to exchange for a free hand in Eastern Europe (Hildebrand 1970).

¹⁵⁰ *Documents on German Foreign Policy, 1918-45, Series D (1937-45), Vol I, p. 69 f.*

southeastern Europe would be through peaceful economic and political penetration (Holborn 1966). By tying Germany to the West, Britain sought to curb the danger of a violent German expansion to the east and the continental hegemony that would follow.

In the long run, the Anglo-German Naval Agreement, the Anschluss, and the Munich Treaty, greatly strengthened Germany's economic and military power, undermining Britain's national security. In the case of the Munich Treaty, Germany seized foreign exchange and strategic raw materials, as well as industrial power (especially the Skoda arms factory) and equipment to arm forty German divisions. In 1939, following England's guarantee of Polish independence, Hitler denounced the Anglo-German Naval Agreement and announced his "Z-Plan," which called for building a large navy (Cowman 1994).

Accommodation of Italy

Traditionally, Britain and Italy experienced cordial relations. Italy was seen as a bastion against German expansion in Central and Eastern Europe. In Britain, no thought had been given nor preparations made for a confrontation with Italy. In fact, like France and the United States, Italy was excluded from the Empire's strategic list of possible enemies. The advent of a Fascist dictatorship under Benito Mussolini in 1922 had not modified these traditionally cordial relations (Barnett 1972). As late as 1935, Anglo-Italian relations strengthened since Mussolini also recognized the danger that Hitler posed to European stability.¹⁵¹

In the aftermath of Italy's invasion of Ethiopia, London was reluctant to antagonize Rome because it would complicate Britain's defense problems (Shay 1977;

¹⁵¹ In 1934, after the Nazi murder of Austria's leader Dollfuss, the Italian's moved troops to the Brenner pass so that Italian troops could help cut down the Nazi uprising which had occurred in parts of the country in order to prevent an Anschluss.

Pratt 1975). First, a hostile Italy would force Britain to divert ships from the Far East or its homewaters, or risk having insufficient ships to defend the region. In contrast, a neutral Italy meant that Britain's battlefleet could be shifted to the Far East, with a small squadron retained in home waters to contain the German navy (Watt 1975). Second, a hostile Italy could block Britain's passage through the Mediterranean on its way to Singapore. The Mediterranean-Suez-Red Sea route was the shortest, fastest, and cheapest route to Singapore. Finally, a war with Italy risked weakening Britain's already overstretched navy. In particular, Treasury opposition to the New Standard eliminated a preventive strike since the loss of any ships in a conflict with Italy would undermine Britain's other naval commitments, while naval agreements precluded the construction of new capital ships until after 1936.

Britain's only alternative to restore the balance was a strategy of accommodation, restricting the extent of Italy's expansion in the Mediterranean (Murray 1979b; Cassels 1983).¹⁵² Anglo-Italian concessions took the form of political agreements, not military agreements (like the military limitations between Britain and either Germany or Japan). The first of three attempted agreements with Italy was the Laval-Hoare Pact (1935). This proposal was a British-French plan to exchange territorial concessions in Abyssinia for Italian acceptance of the status quo. Britain offered Italy large segments of Abyssinian territory currently occupied by Italian troops and frontier adjustments between Abyssinia and Italian Somaliland in favor of Italy. However, the British Cabinet eventually rejected this proposal.

¹⁵² Britain was unwilling to devolve leadership over the Mediterranean to a rising Italy. The Foreign Office and Naval Ministry recognized that Italy would not maintain the status quo. Vansittart saw the Ethiopian adventure (1935) as a "stepping stone to greater things" such as the conquest of the Mediterranean" (Salerno 1994).

Second, the Anglo-Italian Gentlemen's Agreement (1937) called for Italy and Britain to disclaim "any desire to modify the status quo as regards national sovereignty of territories in the Mediterranean Area" (Mills 1937). Both sides recognized free passage through the Mediterranean and agreed to observe the regional status quo (this agreement prompted Eden's resignation; Pratt 1975). However, several days after the signing of the agreement, Italy sent a large force to support nationalist Spain.

Finally, a more comprehensive Mediterranean settlement, known as the Easter Pact (1938), covered most of the areas of rivalry and was intended to remove Italy from the list of Britain's enemies. Its main point was Britain's recognition of Italy's Ethiopian conquest and a commitment to work towards League recognition, in exchange for Italy's agreement not to seek territorial advantages in Spain, to withdraw a substantial number of volunteers from Spain, cease anti-British propaganda in the Middle East, reduce troops in Libya, and respect the Mediterranean and Red Sea status quo (Craig and Gilbert 1953; Pratt 1975).

Accommodation of Japan

Finally, Britain accommodated Japan in the Far East with the intention of retarding Japan's naval ascent and reducing the fiscal strain of preparing for war in three separate theaters (and especially a costly naval race with Japan).¹⁵³ Britain's primary strategy was a series of naval limitation agreements. Britain was unwilling to devolve leadership over the Far East to Japan for fear of losing access to the potentially profitable China market.

The Washington and London Naval Agreements limited Japan's naval rearmament and prevented a prohibitively expensive naval race in the Far East. For Britain, naval

¹⁵³ On the question of a "Far Eastern Munich," see Shai (1974).

arms limitation with Japan between 1921 and the mid-1930s constituted the most successful aspect of the effort to reduce the military spending of a rival power to a level Britain could afford (Murfett 1992; Trotter 1975; Lowe 1981; Louis 1971). The Washington Naval Conference approved three agreements, the Four Power Treaty; the Nine Power Treaty, and a naval construction ratio. First, bowing to American suspicions, Britain replaced the Anglo-Japanese Alliance of 1902 with the Four Power Treaty signed by the United States, Britain, Japan and France (Nish 1977). The four states agreed to common consultation, disputes were to be referred to a conference of the major interested powers. Second, the Nine Power Treaty affirmed China's integrity and sovereignty, preserving the territorial status quo. Third, the Washington Conference called for immediate cancellation of all existing capital shipbuilding programs; a naval holiday of ten years duration in which no capital ship construction would be allowed, and the scrapping of a number of new and old ships. According to the agreement, the Americans would have 18 capital ships (500,000 tons), British would have twenty-two (600,000 tons), and Japan would have ten (300,000). The result was a ratio of 5:5:3, between Britain, the United States, and Japan.¹⁵⁴ This ratio would just permit the Admiralty to send a fleet to the Far East while keeping a 'one power standard' against the next largest European navy (Kennedy 1983).

In order to gain Japan's acceptance, Britain accepted the status quo in the Pacific, granting Japan local naval hegemony (Nish 1977; Kennedy 1976). Britain and the United States also agreed not to fortify any of their island possession in the Pacific and neither upgrade nor build any new naval bases in the region. This meant that the United States

¹⁵⁴ The Coolidge Conference (Geneva Naval Conference of 1927) met to discuss the extension of a shipbuilding ratio to vessels under 10,000 tons. However, Britain argued that it needed cruisers to guard imperial communications. The conference ended in failure because United States and Britain could not solve the issue over the number of cruisers.

could not improve existing naval facilities in the Philippines, but with the exception of Hawaii. Britain could build up Singapore, but not Hong Kong, into a first class naval base. Consequently, neither Britain nor the United States had a base within striking distance of Japan.

At the London Naval Conference (1930), Japan signed a second naval limitation treaty. Unresolved at the Washington Conference was the matter of limiting warships displacing less than ten thousand tons. While Japan pushed for a 70-percent ratio in heavy cruisers, Britain and the United States wished to extend the 60-percent ratio for capital ships to all categories of vessels. The compromised agreement was a 10:6 ratio on large cruisers, parity on submarines, and a 10:7 ratio other categories of auxiliary craft (Iriye 1971).

In the long run, the London and Washington Agreements strengthened Japan's war-making capacity, undermining Britain's national security by increasing the latter country's vulnerability to a preemptive attack in the Far East. In 1934, Japan announced its intention to abandon the ratio system or any other system of naval limitation not common to all naval powers. As expected, at the Second London Naval Conference (1936), Japan demanded a common upper limit, seeking parity with the fleet strengths of Britain and the United States (London opposed this proposal because parity would undermine Britain's ability to protect its homewaters and the Far East). By the mid-1930s, despite further discussions, the Washington Naval System broke down. For Britain, the London and Washington Naval Agreements meant that neither Britain nor the United States had a naval base within striking distance of Japan, giving Tokyo local naval hegemony (McKercher 1993). Second, these agreements allowed Japan to encroach on and surpass Britain's naval supremacy in the Far East without fear of a preventive strike.

In particular, the naval agreements allowed Japan to prepare for preemptive war against Britain's interests in the Far East without incurring a preventive attack.¹⁵⁵

In summary, in the short run a strategy of accommodation retarded the military ascent of imperial Germany, Japan, and Italy, and reduced the costs of hegemony in Britain's homewaters, the Far East, and the Mediterranean, ensuring that Britain remained in the ranks of the great powers longer than its alternative options. In particular, in failing to slow their ascent, Britain risked overwhelming its immediate military capability, leaving it weak and vulnerable to preemptive attack across its empire. Alternatively, devolution risked increasing the war-making capacity of these rivals, undermining Britain's immediate national security.

However, in the long run, as an imperial hegemon, Britain could only select from a range of security strategies which risked eroding its fiscal strength or its national security interests, accelerating its decline from the ranks of the great powers and, concomitantly, reducing its influence in the international system. In particular, a strategy of accommodation undermined Britain's national security by strengthening the war-making capacity of imperial Germany, Italy, and Japan. As imperial challengers, since each preferred an alternative commercial arrangement and none were willing to accept a permanent position of inferiority to Britain in the respective locale, preemptive war was seen as inevitable. Consequently, under the guise of the Washington and London Naval Agreements, the Anglo-German naval, and the Munich Agreement, Germany and Japan built up their military capability without the fear of a British preventive strike. Thus, the outcome of Japan's refusal to renew the Washington Naval Agreement in 1934 and Germany's military and economic gains from the Munich Agreement (equipment for forty German divisions, the Skoda arms works), and its defection from the Anglo-German

¹⁵⁵ According to Kennedy (1983), Japan exceeded the tonnage limits of the treaties.

Naval Accord in 1939, was that Britain had insufficient military capability to defend its global commitments, leaving it weak and vulnerable to preemptive attack everywhere.

Alternatively, as a liberal hegemon, Britain could have selected a security strategy of devolution, safeguarding its fiscal strength and national security interests. In devolving hegemony to the United States, Britain could concentrate its freed-up resources in its homewaters and the Mediterranean against Imperial Germany and Italy, strengthening Britain's immediate war-making capacity in these locales, without eroding its war chest or its national security. However, Britain's desire to preserve its imperial preference system explains why London postponed devolution of regional hegemony to the United States.¹⁵⁶ Imperial Britain was correct to stand firm against the United States. Washington used the leverage created by London's dependence on American financial assistance to destroy Britain's imperial economic bloc, dismantling Ottawa and breaking up the Sterling area (Kimball 1971, 1974). The United States included clauses in the Atlantic Charter and the Lend-Lease Act calling for the elimination of non-discriminatory trade barriers (Churchill called Lend-Lease the "most unsordid act"). In 1945, in exchange for a loan of \$3.75 billion, London agreed to dismantle much of its imperial

¹⁵⁶ In the long term, Britain became dependent upon the United States to defend its global interests. As the arms control and arms limitation agreements with Germany, Japan, and Italy began to fail, Britain could no longer defend all of its commitments. Beginning with the Far East, Britain devolved hegemony to the United States (Reynolds 1981; Murfett 1984; Haggie; 1981; Cowman 1994; Pratt 1971; Hess 1987). As one author argues, "The United States assumed this role and British policy was not conditional upon vital decisions made in Washington. There was no sudden decision or moment when the United States formally took over from Britain. Rather it was a gradual development, perhaps without the American leaders fully realizing what was happening in the earlier stages" (Lowe 1981, 113). By 1941, Churchill deferred to the United States "in the matters concerning the Pacific theater of war" (Lowe 1977, 191-193). On Britain's retreat from the Middle East, see Abadi (1982).

In devolving leadership to the United States, Britain no longer needed to send the main fleet to Singapore in the event of a Far Eastern war (Kennedy 1976). Britain concentrated these freed-up resources in the Mediterranean (Alexandria) and its Home waters. With the active support of the United States, instead of sending eight capital ships to the Far East (which would be one less capital ship Japan had in Far Eastern waters), Britain reinforced the China Fleet by only two capital ships (Gibbs 1976, 427).

trading bloc in 18 months (France was also forced to curtail government subsidies and currency manipulation in exchange for a loan; LaFeber 1991a, 12; Gardner 1956).

Conclusion

By the outbreak of World War II, Britain fell from the ranks of the great powers to a second rate power, resulting in a corresponding reduction in its influence over the international system. Beginning in the 1930s, Britain faced an emerging Germany on the Continent, a rising Japan in the Pacific, and a rising Italy in the Mediterranean. London's fundamental problem was how to stave off war when Britain lacked the military and economic strength to confront the combined military capability of Germany, Japan, and Italy. As Britain was a domestically constrained imperial hegemon, a strategy of accommodation restored the balance between Britain's capabilities and commitments without a massive (and costly) rearmament program. By persuading Germany, Japan, and Italy to limit their armed forces, Britain was able to lower the costs of hegemony. Although aware of the dangers of this strategy, Britain had no other alternatives. Devolution would have threatened Britain's national security by strengthening the war-making capacity of the emerging challengers. Increased domestic resource extraction for a large rearmament program was blocked by Chamberlain and the Treasury.

While accommodation ensured Britain's immediate survival, in the long run, as an imperial hegemon, Britain could only select from a range of security strategies which accelerated its rate of decline from the ranks of the great powers. In pursuing a policy of accommodation, Britain focused on its fiscal concerns, eroding its national security by strengthening the war-making capacity of imperial Germany, Japan, and Italy. In particular, Japan's refusal to renew the Washington Naval Agreement, Germany's economic and military gains in Eastern Europe due to the Munich Agreement, and

Germany's defection from the Anglo-German Naval Accord in 1939 meant that Britain's capabilities were insufficient to defend its imperial commitments. Thus, Britain was vulnerable to preemptive attack everywhere, encouraging Germany, Italy, Japan, and the United States to challenge Britain's regional hegemony in different parts of its empire.

Many scholars argue that a better alternative strategy for Britain to restore the balance between its capabilities and commitments was a massive rearmament program. However, even a domestically unconstrained Britain could not launch a rearmament program against several rising contenders without undermining its fiscal strength in the short run, leaving it few resources for a prolonged war. Britain's rearmament against the combined military buildup of three challengers beginning in 1939 could not be sustained by its economy; by 1941, gold stocks had dwindled to almost nothing and Britain was dependent upon American assistance to continue its war effort. Had Britain initiated a rearmament program in the early 1930s, it would have hastened its decline well before the outbreak of World War II. Thus, as one author summarizes, "whereas Churchill's policy of all-out rearmament ensured Britain's rapid decline, Chamberlain may have glimpsed the possibility of delaying this as long as possible" (Richardson 1988, 297).¹⁵⁷

¹⁵⁷ Of course the counter argument is that if Britain had threatened force earlier, it might have been able to deter Germany.

CHAPTER 5

THE DISSOLUTION OF THE SPANISH MONARCHY: SPAIN'S FOREIGN POLICY OF RESOURCE EXTRACTION (1621-1640)

In the late sixteenth century, Spain was the pre-eminent world power and its wealthy overseas empire was the envy of the emerging European states. In 1580, Spanish claims became even more all-embracing when King Philip II of Spain secured the Crown of Portugal and its overseas empire in Brazil, Africa, and the East Indies, adding to Spain's global empire. Spain found itself in an unrivaled position, dominating the world's trade routes, markets, resources, and strategic lines of communication. Spain's empire (referred to as the Spanish system or the Spanish Monarchy because much of it was a collection of inherited lands and ruled under different constitutions) included parts of western and central Europe, the East Indies, the coasts of Africa and India, and the Americas. In dominating the richest regions of the world, the Spanish Crown became the largest handler of bullion, and accounted for nearly all of the world's deposits of good quality marine salt, provided the bulk of Europe's sugar, and became Europe's leading emporium of pepper. This great wealth allowed Spain to extract resources (and borrow money) at short notice and in large amounts in order to finance a large standing army and navy for the defense of its extensive Continental and overseas empire.

However, Spain's imperial wealth and its scattered empire also attracted rising challengers for regional hegemony. As early as the 1570s, emerging states began to encroach on Spain's global interests at different rates and in disparate regions (and without the expense of imperial defense).¹⁵⁸ On the Continent, Spain confronted an emerging Britain, France, and United Provinces (Dutch), as well as periodic challenges from the Ottoman Sultan.¹⁵⁹ In the East and West Indies (Asia and America), and in Africa, Spain's empire was challenged by British and Dutch assaults. In the Mediterranean and North Africa, attacks by the Barbary pirates and Ottoman Empire harassed Spanish shipping and trade. Finally, in Germany, Spain supported the Catholics against the Protestants, in France the Catholic League against the Huguenots, and Spain's Austrian cousins against the Turks.

In encountering these emerging challengers, Spain's King Philip IV (1621-1665), and his Count-Duke of Olivares, Gaspar de Guzmán (1622-1643), had to decide how to restore the balance between Spain's military capability and its foreign commitments. Failure to narrow the growing gap between Spain's capabilities and its global interests would undermine Madrid's immediate national security. In particular, insufficient military capability would leave Spain weak and vulnerable to attack everywhere, tempting an emerging France, Britain, and/or the United Provinces to challenge Spain for regional hegemony. However, to match or even out-pace the combined military buildup of these emerging contenders (in preparation for preventive wars) was dangerous because prolonged and excessive resource extraction would undermine Spain's fiscal strength and ultimately its military capability. Finally, global retreat was a dangerous alternative

¹⁵⁸ On the debate of when to date the beginning of Spain's decline, see Kamen (1978); Stradling (1979a).

¹⁵⁹ The United Provinces or the Dutch consisted of the seven northern provinces of the Netherlands which rebelled against Spain beginning in the 1570s.

because abandonment of strategic and valuable locales might strengthen the war-making capacity of future challengers, eliminating Spain's exclusive access to its investments, raw materials, and trade in the locale.

Like pre-World War II Britain, in the long term, Spain failed to manage its decline, accelerating its fall from the ranks of the great powers to a second-tier power. The nature of Spain's foreign commercial policy contributed to its failure. As a declining imperial hegemon, Spain could only select from a range of security strategies which either eroded its political economy or its national security. In the short run, Spain selected a security strategy of increased extraction (in order to prepare for preventive wars against an Emerging France, England, and United Provinces), ensuring that it remained in the ranks of the great powers longer than under alternative options. However, in the long run, a strategy of extraction undermined Spain's industrial base, and ultimately, its ability to construct and maintain a modern military force, leaving it vulnerable to attack. This chapter examines how Spain restored the balance between its military capabilities and global obligations, and why this strategy failed. The first section examines the rising contenders for regional hegemony which Spain confronted. The next two sections focus on a debate among the Crown, the Arch-Duke, and their ministers on how to restore the balance between Spain's capabilities and commitments. The final section discusses why Spain selected a security strategy of resource extraction over the alternative strategies of accommodation and devolution, and why this foreign policy option failed.

The Emerging Challengers for Regional Leadership

The major challenges to Spain's empire came from the French army, and the English and Dutch navies. The conventional view that Spain lost its global hegemony to

France in 1659 with the signing of the Peace of Pyrenees oversimplifies the dilemma that Spain confronted in this period. Had Spain encountered only an emerging France on the Continent, Madrid could have concentrated its extensive military and naval resources from its global empire, overwhelming France's military capability.¹⁶⁰ In contrast, as discussed below, Spain's hegemony was challenged by several contenders, who rose at different rates and challenged Spain's leadership in disparate parts of its empire (as well as its corridors of communication between these locales). In oversimplifying Spain's predicament, it is difficult to understand the dilemma that Madrid confronted in restoring the balance between its capabilities and commitments while at the same time protecting its fiscal strength and its national security.

First, rather than confronting a single emerging contender for global hegemony, Spain confronted a rising United Provinces, France, Britain, as well as lesser challengers such as the Ottoman Empire and Sweden under Gustavus Adolphus. In addition, these contenders challenged Spain's hegemony at different rates and in disparate parts of its empire. Beginning in the 1570s, the Dutch challenged Spain's position in the Low Countries (Flanders). By 1600, an emerging United Provinces challenged Madrid's leadership in the Spice Islands in Asia (the Portuguese under Spain had been the major suppliers of spice to Europe, accounting for 75 percent of Europe's spice imports; Scammell 1989, 97).¹⁶¹ Two decades later, with the creation of the Dutch West India Company (1621), the United Provinces concentrated on capturing Spain's (Portugal's) sugar plantations in Brazil. Following on the heels of the Dutch assault, Britain was repelled by both Spain (and the Portuguese) and the Dutch, failing in its initial attempt to

¹⁶⁰ Around 1620, Spain had four field armies (Flanders, Rhineland, central Europe, Italy), each around 20,000; twice as many garrison troops; 50 galleons under construction; auxiliary naval squadrons. In all, in 1626 Spain had 300,000 men under arms (Stradling 1981, 62).

¹⁶¹ The Portuguese captured the spice trade from Arab traders.

gain a foothold in the Far East.¹⁶² Subsequently, the British concentrated their assault on the Portuguese empire in the Indian subcontinent and Indian Ocean, while financially and militarily supporting the Dutch revolt on the Continent against Spain. Finally, beginning in the late 1620s, no longer preoccupied by religious wars, France under King Louis XIII and his foreign minister, Cardinal Richelieu, challenged Spain's European empire in Italy, Germany, and even Flanders (the surrender of La Rochelle in 1628, the largest of the Huguenot towns, marked the end of the religious wars between the Catholics and the Huguenots), and in the 1650s, France assaulted Spain's overseas empire as well.

Second, rather than being challenged in a single instance, differential rates of industrialization meant that contenders for regional hegemony encroached on and in some instances surpassed Spain's industrial lead, with some challengers rising earlier and faster than others. The major sectors of industrialization in the seventeenth century included textiles, metallurgy, and shipbuilding (Lynch 1992). The Dutch were the first to surpass Spain in a number of key industrial sectors, such as shipbuilding. As well, as the leading commercial power, the Dutch were able to convert their financial and industrial strength into military power, building and maintaining the largest navy in the world and a powerful army. England was the second power to encroach on Spain's lead, especially in key sectors such as textiles and metallurgy. England eventually eclipsed Spain and the Dutch, challenging the Dutch empire in the East Indies, parts of Africa, and the Americas.¹⁶³ Finally, with the end of the religious wars in France, Paris began to

¹⁶² In this discussion, Spain includes Portugal and its empire.

¹⁶³ There were a series of Anglo-Dutch conflicts in the late seventeenth century (three wars). The British Navigation Acts of the seventeenth century were designed to eliminate the Dutch from distribution functions within England's realm, which the English hoped would then correct their problematic balance of payments by lowering Dutch gains. The Navigation Acts (1651) were intended to give a monopoly to English shipping by decreeing that imports had to come straight from the source country and be carried in ships from the source country or England.

encroach on Spain in metallurgy, which was an essential component for creating a modern military.

Netherlands: United Provinces, England, France

The Dutch republic was a loose confederation of seven provinces (known as the United Provinces) that had successfully rebelled against Spain beginning in the 1570s (the ten southern provinces remained loyal to Spain or suppressed by Spain and were called the Spanish Netherlands). This rebellion, or the Eighty Years' War, lasted until Spain formally recognized the Dutch Republic in the Treaty of Munster in 1648.

In 1609, after years of fighting, Spain and the United Provinces agreed to the Twelve Years' Truce (Truce of Antwerp).¹⁶⁴ However, in 1621, upon expiration of the truce and with the renewal of its war on the Spanish Netherlands (including the North Sea and the Atlantic approaches), the United Provinces was the first contender to challenge Spain and its empire in the East and West Indies. Since the Low Countries were characterized by a dense network of forts, strongholds, fortified towns, and dikes, the war quickly became a costly land war of attrition on both sides. Beginning in 1626 (and for the next eight years), the Dutch launched a series of offensives against the Spanish Netherlands. In 1628, the Dutch position in Europe was strengthened by three events that occurred in disparate parts of Spain's empire, (1) the onset of the Mantuan Succession crisis in Italy between France and Spain (opening another front); (2) the loss of the annual Spanish treasure fleet to the Dutch off of the coast of Cuba (New Spain silver fleet); and (3) the fall of the Huguenot stronghold at La Rochelle to Louis XIII's army (freeing the French army for war against Spain in Italy).

¹⁶⁴ To many in Castile, the truce represented a political, military and ideological defeat. In this humiliating truce, the Crown unofficially recognized Dutch sovereignty.

In 1629, in preparation for the Dutch assault on the Spanish Netherlands, the Dutch army ballooned to 128,000 men, including West India Company troops, nearly four times the size of the Spanish army of Flanders (Israel 1982, 176-77). In 1632, the Dutch forces continued to pressure Spain in the Netherlands, threatening Antwerp and capturing Maastricht, one of the most serious defeats suffered by Spain during the war. In 1635, opening a second front in the Netherlands, France declared war on Madrid, threatening Spain's strategic lines of communication and military highway, known as the Spanish Road, which connected northern Italy (Milan) and the Spanish Netherlands (control over the Spanish Road allowed Spain to shift resources between the fronts in Italy and the Netherlands).¹⁶⁵ Advancing north with 30,000 troops through Luxemburg and meeting up with 30,000 Dutch troops, France penetrated the Spanish Netherlands south to Antwerp, before being repelled by Spain's army of Flanders.

Italy: France, Turks

In Italy, Spain controlled almost half of the peninsula, the states of Lombardy, Naples, Sicily, and Sardinia. The initial threat to Spain's leadership in Italy came from the Ottoman Empire. By the mid-1570s, the Ottoman threat had receded because Istanbul was preoccupied with Persia, only to be replaced by the French onslaught on Spain's European hegemony. In 1625, the French invaded the Valtelline pass (strategic Alpine pass) in North Italy, and blockaded Genoa, threatening to cut the Spanish Road (in the same year, the English fleet launched a raid on Cadiz, now Spain was at war with France, the United Provinces, and England simultaneously).¹⁶⁶ In 1629, opening another front and further stretching Spain's resources, Cardinal Richelieu led the French invasion of

¹⁶⁵ For a discussion of the Spanish road, see Parker (1972, 80-105).

¹⁶⁶ Overland transport was much cheaper than ocean transport.

Spanish Italy, resulting in the War of Mantua, in an attempt to assert France's pre-eminence in Europe and to capture the wealth of Northern Italy (this contest was resolved in 1631 in France's favor).¹⁶⁷ In the aftermath of the War of Mantua, France continued to harass Spain's empire in Italy.

Germany: Sweden, Germany, France

In 1618, the Protestant estates in Bohemia revolted against their new Catholic ruler, Archduke Ferdinand.¹⁶⁸ Spain's concern was that a successful revolt by Bohemia would be followed by the spread of subversion throughout the empire. In the early 1630s, the Swedish King, Gustavus Adolphus, moved into Germany, inflicting one defeat after another on the Habsburg forces. In 1632, France entered the fray against Spain, taking Lorraine, and in 1633, blocking the Spanish Road. From 1632-4, the French also subsidized the anti-Habsburg states.

East and West Indies: Dutch, English, French

Europe was only one of several fronts Spain had to devote its economic, military, and political resources. In 1580, Spain acquired Portugal and its extensive empire in Brazil and the East Indies. In the Far East, the rising sea-powers of the United Provinces, and later England, challenged Spain's hegemony from the Cape of Good Hope to the

¹⁶⁷ In 1627, the Duke of Mantua died, leaving a succession problem. The most convincing claimant to the duchy was the French Duke of Nevers. Spain occupied Mantua and the strategic town of Casale, along the Spanish road, fearing that the succession of a French client would endanger Spain's interests in northern Italy and threaten its strategic communications with the Netherlands. In 1628, with the fall of Huguenot town of La Rochelle and the ending of the religious wars, Louis XIII began to focus on Spain's European empire.

¹⁶⁸ While England did support the Protestant rebellion in Germany, the deepening constitutional quarrel between Parliament and Crown contributed to England's growing isolation. The Commons were well aware of the danger to their position which a royal army would represent. It would outweigh not only their control over taxation but also their own military force. The issue over who controlled the military contributed to the English Civil War.

Spice Islands. Dutch encroachment on Spain's Far Eastern empire began in earnest in 1602, with the creation of the mercantilist long distance trading company, the Dutch East India Company (the Verenigde Oostindische Compagnie or VOC). By 1619, the VOC had made substantial inroads in the Indies, establishing its principal Far Eastern base at Batavia (Jakarta).

In the aftermath of the Dutch-Spanish Twelve Years' Truce (1621), VOC forces launched a new wave of offensives against Spain's eastern empire (the VOC was aided by a temporary truce in its conflict with the English East India Company, lasting until 1624). The Dutch target was Spain's empire in Malaysia and the Islands of Indonesia, also known as the Spice Islands. In particular, the VOC sought to capture Spain's profitable traffic in pepper and spices (cloves, nutmeg, cinnamon, mace), and replace it with the VOC's own spice monopoly.¹⁶⁹ The Dutch also challenged Spain's possession of Manila (which linked China, Japan and the New World), China's foreign trade, and Taiwan. By 1623, the Dutch had ninety ships, four large garrisons, and twenty forts in the region (Israel 1982, 117).

Following on Dutch footsteps, England sought to carve-out its own exclusive sphere in Spain's East Indies as well. However, the English East India Company (EIC, 1600) was repelled from the region by both Spanish (and Portuguese) and VOC counter-pressure in the 1620s. While the English did make some headway in the region (in Indonesia), the EIC concentrated its assault on Portugal's empire in the Indian Ocean, and particularly in India, beginning with Surat (India), and extending to Basra and Hormuz

¹⁶⁹ Spain's spice trade included Malacca (in Malaysia), the Moluccas (islands of Indonesia), Bandas (islands of Indonesia), as well as Macoa (China coast), Goa (India), and Ceylon. In 1605, the Dutch made their first significant break-through in the East Indies in capturing Amboina and the Moluccas from the Portuguese. Eventually, the Dutch would conquer the bulk of Portugal's empire in the Indies.

(Oman) in the Persian Gulf, to the Red Sea, and even the coast of East Africa, forcing Spain to divert resources from the other fronts to this region (Newitt 1986).¹⁷⁰

A similar pattern of encroachment unfolded in Spain's empire in the West Indies. During the Twelve Years' Truce, the Dutch were the first to challenge Spain's hegemony in the West Indies. In 1621, with the expiration of the truce, the Dutch created the West India Company (WIC), based on the successful VOC, with the goal of territorial acquisition in the Americas. The WIC's first major assault was a large-scale attack on the sugar-producing province of Pernambuco (Brazil) and Puerto Rico in 1624. In 1628, ships from the Dutch WIC captured Spain's entire Mexican silver fleet at Matanzas Bay in Cuba (10 million ducats; or equal to two-thirds of the annual cost of the Dutch army), dealing a blow to Spain in the midst of the latter's costly confrontation with France over Mantua (Italy). By 1630, the Dutch secured a foothold in Brazil in the province of Pernambuco, and by 1632-3, the Dutch were on the verge of capturing the region's wealthy sugar plantations.

Elsewhere in the Americas, operating from sparsely populated islands, the French and English used small ships to harass Spanish trade in the Caribbean (the English force was centered in Jamaica and France in St. Dominique). French and English buccaneers crossed the Isthmus, attacking the Spanish Pacific trade as well. Farther north, Dutch, French and English expansion centered on North America, well out of Spanish reach. The English established colonies in Virginia (1607), Plymouth (1620), Massachusetts (1630).

In summary, Spain's rate of decline was far from simultaneous, rapid, or uniform in nature across its empire. While Spain had the revenue, armies, and resources to defeat

¹⁷⁰ According to Israel (1989), the Ambonia massacre of English troops by the Dutch marked the end of British activity in the East Indies.

any single rising challenger, in confronting an emerging France, Britain, and the United Provinces, as well as weaker powers such as the Ottoman Empire and Sweden, at different rates and in disparate parts of its empire, Madrid was faced with the impossible dilemma of restoring the balance between its capabilities and commitments while safeguarding its fiscal strength and its national security interests.

Spain: Declining Imperial Hegemon

The nature of Spain's foreign commercial policy restricted its range of foreign policy options for restoring the balance between its capabilities and commitments. As an imperial hegemon, Spain acquired an empire with the primary goal of achieving economic self-sufficiency. In particular, mercantilism was a system designed to increase the economic wealth and military power of the state (Spero 1985). It was widely believed that a favorable balance of trade would bring in gold and silver, increasing the nation's wealth and ultimately its military strength. For Spain, overseas colonies guaranteed exclusive access to markets and raw materials, and the use of metropolitan shipping, while shutting out foreign commercial competition.¹⁷¹ Also, colonies were a source of direct revenue for the Crown not subject to domestic constraints (in the case of Spain, Castile's Cortes).

As a result of Spain's mercantilist foreign economic policy, Madrid did not differentiate among emerging contenders, but instead viewed France, England, and the United Provinces as a threat to its national security and commercial interests, eliminating the foreign policy alternative of devolution of regional hegemony. First, in devolving hegemony, Spain risked undermining its economic strength because no potential

¹⁷¹ Dutch ships were banned by the Spanish crown from the Flemish sea-ports and from carrying Spanish wool and salt to Italy.

successor would maintain its mercantilist system in the locale. The commercial policies of imperial France, Britain, and the United Provinces were directed at carving-out their own exclusive economic spheres intended to promote self-sufficiency. Consequently, they would replace Spain's mercantilist system with their own. The loss of access to its overseas empire would deprive Madrid of the resources it needed to fight on several fronts simultaneously. Second, in devolving hegemony, Spain risked eroding its national security because these emerging contenders would capture economic and military assets, increasing their war-making capacity and further hastening their rate of ascent.

Imperial Hegemon

The Treaty of Tordesillas of 1494 divided the world between Spain and Portugal. This treaty led both Spain and Portugal to believe that they had an exclusive right to all land that did not have a settled and effective government (Garraty and Gay 1981). In 1580, the Spanish land claims became more all-embracing when Philip II of Castile secured the Crown of Portugal and Lisbon's large overseas empire.

Beginning in 1503, to protect its monopoly on its overseas trade from foreign penetration (and domestic competition), Spain created exclusive trading companies. In the Americas, participation in colonial trade was limited to a single Spanish trading company, the *Casa de la Contratación*, based in Seville, with a branch in Cádiz (Williams 1966; Israel 1990). The *Casa de la Contratación* checked, taxed, and regulated the entire commerce between Spain and the Americas. Under the *Casa de la Contratación*, each year two large convoys under heavily armed escort sailed from Spain, one to Portobelo and the other to Veracruz. No ships were allowed to sail except in the convoys, no ports could be used for trans-Atlantic trade except the designated few, and no foreigners were allowed to engage in the trade.

Based on the *Casa de la Contratación*, Spain established additional monopoly trading companies, including in 1624, the Seville Admiralty Board or *Almirantazgo de los países septentrionales*, assigning it jurisdiction and control over all trade with northern Europe, and later extended exclusive rights to the whole of the Iberian Peninsula (Israel 1986; 1990). The purpose of this mercantilist trading company was to replace the Dutch as the main trading partners of the Hansa towns of north Germany, and to check Flemish, German, Danish-Norwegian, French, and English commerce in the region (Baltic trade was seen as the cornerstone of Dutch economic power and wealth). By weakening the mercantilist system of the competing states, and especially undermining Dutch economic power, Madrid hoped that Amsterdam would return to the bargaining table and sue for a truce on Spanish terms.

The *Almirantazgo* had two roles, (1) organize an armed convoy system (like the Americas trans-Atlantic convoy system) between Flanders and Spain (stationed on Germany's Baltic coast), and (2) head a system of customs to control trade between all Andalusian ports and northern Europe with the ultimate goal of interlocking the *Almirantazgo* with a global network of monopoly trading companies in the Levant and India. While the *Almirantazgo* failed in creating a convoy system, it succeeded in injuring the Dutch by excluding their goods from ports in Flanders, the Iberian Peninsula (Spain, Portugal), Italy, and the Spanish overseas ports (to the benefit of the English and French as long as they remained neutral). Madrid also had the right to check and certify that cargoes for the Iberian and Italian Peninsulas were non-Dutch (cargoes lacking certificates were confiscated). The *Almirantazgo* halted Dutch shipping, denied the Dutch access to the salt pans in Spain, blocked Dutch goods from entry into Spain, and excluded spices from the Dutch East Indies (Israel 1990, 19). However, the success of

the *Almirantazgo* forced the Dutch to seek commodities at their source, in the Spanish Indies.

Rising Imperial Challengers

Not only was Spain an imperial hegemon, but the rising contenders, such as Britain, the United Provinces, and France, sought to replace Spain's preferential monopoly with their own mercantilist order, blocking Spain's future access to its markets, investments, and resources in the respective locales. As imperial challengers, none of these contenders would maintain Spain's exclusive position in the region. In fact, the trading companies of Britain, the United Provinces, and France tied up much of their resources in military enterprises such as armed ships and escorts, troops, and fortresses and fortified settlements with the primary goal of carving-out their own mercantilist system and blocking foreign access to the region. Some of these monopoly companies include the Dutch East Indies Company (1602) and the West Indies Company (1621), the English-created Muscovy Company, the Levant Company (1605), the Massachusetts Bay Company (1628), and the East India Company (1601); the French-created *Compagnie des îles d'Amérique* (1627); Swedish African Company, Muscovy Company (1555), the Spanish Company (1577), the East India Company (1601), and the Virginia Company (1606).¹⁷² Consequently, Spain viewed all of these emerging contenders for regional hegemony as adversaries and future rivals.

¹⁷² According to Williams (1966, 31), in England, trading companies were usually created as a result of mercantile pressure on the government. In France, trading companies were usually established as the result of government initiative. The great Dutch trading companies were the product of a partnership between the government and merchant classes.

United Provinces

The Dutch used the years of the Spanish-Dutch Truce (1609-1621) to consolidate and extend their gains in the East and West Indies at the expense of Spain's Portuguese empire. As the Dutch encroachment continued during the truce, one Spanish minister after another came to the conclusion that "[the truce] has been worse than if the war had gone on" (Elliott 1963, 321).¹⁷³ Relentless Dutch pressure to carve out its own mercantilist spheres of influence in the East and West Indies undermined Spain's imperial wealth in two ways. First, in capturing the wealthy sugar plantations in Brazil, the treasure fleets in the Americas, and the spice trade in the east Indies, the Dutch trading companies blocked Spain's access to its valuable markets, resources, and investments in the region, which Madrid needed to finance the defense of its empire. Second, with fewer resources coming in from its empire, the Dutch challenge pressured Spain to increase its domestic rate of extraction for the defense of its empire, diverting resources from domestic investment.

In 1602, the States-General of the United Province merged the competing trading companies in the East into one great national concern, the United Netherlands Chartered East India Company or VOC (Parry 1966; Boxer 1965; Furber 1976). The charter granted the VOC exclusive rights for twenty-one years for the trade between the Cape of Good Hope and the Megallan's Straits. The States-General granted the governing body or court of seventeen directors significant autonomy, including the right to conclude treaties of alliance, to wage defensive wars, to build fortresses and strongholds in the region, seize foreign ships, establish colonies, and coin money. The VOC could also enlist

¹⁷³ The truce talks between Spain and the Dutch nearly broke down over the question of Dutch commercial access to Spain's empire in the East and West Indies. This dispute was resolved by making no mention of the issue of overseas trade in the final truce (Parker 1979, 54).

civilian, naval, and military personnel who would take an oath of loyalty to the Company and to the States-General (Scammell 1989). The Dutch state provided the VOC with soldiers, artillery, and even loaned the company ships. In return, the state claimed the prospective territories, 20 percent of all profits, and payment upon the renewal of the charter (Stamp 1957). Thus, the VOC was virtually a state within a state, backed, financed, and sustained by the wealth of Holland.

The aim of the VOC was to capture Portugal's lucrative spice trade in the East Indies and to exclude Spain and England from this region by establishing a monopoly on the purchase of spices (Scammell 1989; Furber 1976).¹⁷⁴ Local producers were compelled by armed force to supply their produce only to the Dutch, while infringement brought a violent response by the Dutch (Furber 1976, 45; Chaudhuri 1965).¹⁷⁵ When the English EIC tried to break into the spice trade, the Dutch responded with the same naval and military ferocity used against Spain and Portugal.¹⁷⁶ In monopolizing the lucrative spice trade with Europe, the Dutch could increase their economic strength (and convert it into military power) by determining prices while simultaneously eroding Spain's fiscal power and its military strength.

Following a similar pattern, in the Americas, the Dutch created two state-chartered monopoly companies during the Twelve Year Truce with Spain, the New Netherlands Company and the Northern Company, to challenge the Spanish monopoly in

¹⁷⁴ The Dutch unwillingness to disband the East India Company prevented a full peace in 1607-9 (Israel 1982).

¹⁷⁵ In both the Bandas and Ambonia, the chiefs that did not make oaths to the Dutch were executed. Seapower allowed the Dutch to restrict the growth and harvesting of cloves to Dutch Ambonia, with trees elsewhere destroyed by the VOC (Scammell 1989, 102).

¹⁷⁶ The Dutch expansion in the region was assisted by a "cold" truce between the VOC and the English EIC, allowing the Dutch to concentrate their forces against the Spanish. Under this agreement East Indies trade was to be shared on the ratio of 2/3 for the Dutch and 1/3 for the English, and a joint fleet organized for protection from the Portuguese (Stamp 1957, 150). The Dutch concluded this treaty because its Twelve Year Truce with Spain was about to end.

the West Indies. Both companies were designed to exclude Spanish and English traders from the region. In 1621, the New Netherlands Company was absorbed into the West India Company (WIC), modeled on the VOC.¹⁷⁷ Like the VOC, the WIC was given a monopoly on all Dutch trade and navigation with America and West Africa, as well as the authority to make war and peace with the indigenous powers, to maintain naval and military forces, and to exercise judicial and administrative functions in those regions. Similar to the VOC, the WIC offensive role in the war against the Iberian Atlantic empire was emphasized from the start. One author calls the WIC "an offensive weapon for striking against the roots of Iberian power in the New World" (Boxer 1965, 49). According to another, the object of the WIC was "as much war and piracy as trade" (Howat 1974, 65). As a purchaser of weapons, munitions, foodstuffs, and cloth, the WIC came second only to the state itself (Israel 1982).

The West India Company's main target in the Americas was Spain's lucrative sugar-producing areas in northeast Brazil, the annual Spanish treasure (bullion) fleet, and the salt pans in Punta de Araya (after 1621 the Dutch were excluded from the salt pans in Spain). The WIC's intention was to dominate Brazil's sugar production and to monopolize the trade between the Americas and Europe, excluding Spain from its traditional markets in the region.

England

In 1600, England's Elizabeth I issued the charter granting the English East India Company (EIC) a monopoly on the country's trade with Asia, primarily with India (other English charter companies include the Muscovy Company, Turkey Company, Vencie

¹⁷⁷ The formation of the WIC was suggested much earlier but was delayed by the conclusion of the Twelve Years' Truce.

Company, Levant Company; Lloyd 1984). Further strengthening the monopoly, in 1609, the Stuart government prohibited the importation of pepper by any trader except the East India Company (Chaudhuri 1965). In contrast to the Dutch companies, the EIC lacked government support, and its powers were less extensive, being instead a chartered monopoly encouraging private enterprise.

By the late 1620s, driven out of South China and Asia after open war with Spain, and from the Indonesian Archipelago by the VOC, the English EIC struggled to survive before establishing itself in the Portuguese dominated Indian Ocean, where there was less Dutch activity (however, the EIC would become the power *par excellence* in the East, replacing the Dutch).¹⁷⁸ Like the Dutch, the EIC's commerce between Asia and Europe was conducted in Company ships and the English came to monopolize various posts. The EIC challenged Portugal in Surat (India), paving the way for English expansion into Persia and the strong-hold of Hormuz (1622), as well as inter-port trade with South-East Asia. Laying the foundations of Britain's domination over the subcontinent, Surat became England's center for trade in the Northwards sphere of India, Persia, Bengal, Calcutta. Alarmed by English inroads into the Persian Gulf, Portugal attempted to clear the Gulf of foreign ships.

In the West Indies, well out of Spain's sphere, the English moved into North America. By the death of James I in 1625, the English established exclusive colonies in Virginia, New England, and some of the small West Indian Islands that the Spaniards had not considered worth settling. For instance, the New Netherlands Company was given a three-year trading monopoly over the area between New France and Virginia. During the

¹⁷⁸ In the Spice Islands, the Dutch overran Britain's base in Amboyna, massacring the soldiers. The EIC also faced domestic challenges that threatened its survival (Newitt 1986). The effect of the war on the EIC was devastating. It required troops, armed ships, and fortresses, which greatly reduced the profitability of the Company (Chaudhuri 1965).

reign of Charles I there was a great flood of emigrants to North America and the West Indies. Some of these southern settlements were founded with the intention of establishing bases to attack the Spanish treasure fleets (Scammell 1989, 40).

France

Finally, while France under Cardinal Richelieu concentrated on conquest in Europe (Spanish Netherlands, Germany, Italy), following the conclusion of the religious wars between the Catholics and the Huguenots, Richelieu established a number of monopoly companies in order to compete with Spain and the ascending European powers with the goal of making France a major maritime and naval power. For Richelieu, economics was a weapon to undermine Spanish power. In 1627, Richelieu established the *Compagnie des îles d'Amérique*, or the Company of the American Islands, in the Leeward Islands and extended it to Martinique and Guadaleoupe in 1635 (the various French possessions in the West Indies were also turned over to the Company of the American Islands). In 1628, Richelieu established the Company of New France to administer the North American (Canada) settlements, granting it a permanent monopoly of the fur trade stretching from Florida to the Arctic Circle and from Newfoundland to the Great Lakes. By formally linking trade with colonization, the government hoped that the profits from the one would cover the expense of the other (in 1664 its trade was handed over to the newly created Company of the West Indies, modeled on the pattern of the Dutch trading companies. Colbert's plan was to increase French wealth at the expense of the Dutch empire).

In summary, the nature of Spain's foreign economic policy meant that it viewed an emerging France, England, and United Provinces as challengers to its national security and commercial interests. Consequently, Spain's imperial commercial policy excluded

the foreign policy option of devolution. For their part, these contenders sought to carve-out their own exclusive mercantilist spheres from Spain's empire. In devolving regional hegemony, Spain risked strengthening the war-making capacity of future rivals, while losing future access to its markets, resources, and investment in these locales since no emerging contender would maintain its mercantilist position.

Domestically Unconstrained: Royal Absolutism

Spain's imperial commercial policy limited its range of foreign policy options for managing decline to either a security strategy of increased resource extraction or a strategy of accommodation. In confronting a rising imperial France, England, and United Province for regional hegemony, Spain's leaders discussed whether to restore the balance between its capabilities and commitments by increasing its rate of domestic resource extraction for military spending or by coming to agreement with some/all of the rising contenders in order to slow their rate of encroachment.¹⁷⁹ The immediate cause of this debate was the revolt in Bohemia in 1618 and the looming expiration of the Twelve Years' Truce between Spain and the United Provinces in 1621. Spain could either extend the truce or renew its war against the Dutch. Olivares and his advisers called for the renewal of the Dutch war because the humiliating Truce of 1609 undermined Spain's international reputation (Jago 1981; Lynch 1992). Through a series of victories, Olivares intended to force the Dutch back to the bargaining table, while deterring France and England from challenging it in other parts of its empire. However, other ministers opposed the strategy of resource extraction, and especially the resumption of the costly war in the Netherlands, calling for some sort of accommodation with the United

¹⁷⁹ As part of this debate, the King and his ministers focused on the proper ordering of Spain's commitments in the Netherlands and Italy, or "Lombardy or the Low Countries." The outcome would influence which region received priority in terms of resources (see Israel 1977; Parker 1979).

Provinces, England, and/or France. The outcome of this domestic debate would influence whether Spain would select a security strategy of increased resource extraction or accommodation.

Reputation and the Castilian Cortes

Ministers in Philip IV's Council of State, the Council of Finances, Ambrogio Spínola, commander of the Flanders army (and was the chief proponent for the original truce), and Spain's archduke in Brussels, called for Spain to end the costly war in Flanders.¹⁸⁰ In opposing the ever-increasing costs of renewing the conflict, they called for Spain to restore the balance between its capabilities and commitments by reducing the cost of hegemony through some accommodation with an emerging United Provinces, England, and/or France.

In contrast, Philip IV and Olivares believed that any accommodation, especially a repeat of the 1609 Twelve Years' Truce with the United Provinces, would undermine Spain's reputation, and ultimately erode its military power.¹⁸¹ In particular, the signing of a truce with a much weaker United Provinces was seen as a threat to Spain's reputation of invincibility, especially to Olivares (Brightwell 1974b; Israel 1982, 12). For Philip IV and Olivares, Spain's reputation was an important weapon for a world wide empire (Elliott 1963).¹⁸² However, this reputation could only be sustained by the victorious display of military power. A blow to Spain's reputation in one locale would have

¹⁸⁰ So did the Councils of Portugal and the Indies, due to Dutch damage to Portugal's overseas empire (Elliott 1963; Parker 1980).

¹⁸¹ For Spain, there were three points the Dutch had to agree to for a lasting peace: recognition of Habsburg sovereignty; freedom of worship for Dutch Catholics; and commercial access to Antwerp through the Scheldt estuary.

¹⁸² The role of reputation in motivating Spain's foreign policy is discussed by numerous authors. For instance see, Parker (1979); Stradling (1988); Elliott (1989). Also see Orme (1992).

ramifications in other parts of its empire, encouraging other emerging states to challenge its maritime and colonial interests. In 1635, Olivares wrote "the first and most fundamental dangers threaten Milan, Flanders, and Germany. Any blow against these would be fatal to this monarchy; and if any one of them were to go, the rest of the monarchy would follow, for Germany would be followed by Italy and Flanders, Flanders by the Indies, and Milan by Naples and Sicily" (cited in Elliott 1991, 97). The reverse was also true, successful assertion of power in one theater of operation could deter challengers on other fronts. Consequently, Spain's foreign policy after 1621 was to restore its reputation by forcing Amsterdam back to the bargaining table through a series of quick victories for a better agreement than the truce of 1609 (Stradling 1986).

Maintaining Spain's reputation would require preparation for preventive wars against the combined military buildup of France, England, and the United Provinces, entailing great expense. For Philip IV and Olivares, the main barrier was the Cortes of Castile (Spain's Parliament). Historically, the Cortes of Castile existed to vote taxes, not to make laws, depriving the Crown of fiscal autonomy (see Lynch 1992; Jago 1981). Since the beginning of the fourteenth century, the Crown could not impose new taxes without the prior consent of the Cortes. However, the Crown had little reason to request increases in the rate of resource extraction. During most of the fifteenth and sixteenth century ordinary sources of revenue, such as existing taxes, ecclesiastical revenue, and returns from the Indies, allowed the king to pay his way without going frequently to the Cortes for additional revenue.

Beginning in 1590, with the increasing cost of hegemony due to the Dutch, French, and English ascent, the Crown began to demand increases in the rate of societal resource extraction for military spending. The immediate cause was the defeat of the Spanish armada in 1588 by England. In response, the Castilian Cortes granted Philip II

the first *millones* (which were renewed periodically after 1601). The *millones* were a new sales tax on basic foodstuffs such as meat, vinegar, wine, and oil. It took the form of a fixed grant by the Castilian Cortes to the Crown, with each town in Castile responsible for raising a certain levy (at the apex of the *millones* structure stood the Castilian Cortes, which represented 18 towns, two deputies each, who voted on a sum to be granted to the Crown).¹⁸³ As a contractual relationship (until 1626), one condition imposed by the Cortes on the Crown was that the *millones* could only be used to meet the expenses for which it had been approved (Thompson 1982).¹⁸⁴

The government of Philip IV was contemptuous of the *millones* and unwilling to accept any encroachment by the Cortes' on the royal prerogative (Jago 1981). Although the Castilian Cortes attempted to assert their independence, the Crown challenged the administration of the *millones*.¹⁸⁵ Philip IV and Olivares set out to weaken and circumvent the Cortes, granting the Crown fiscal autonomy and complete control over public revenue (Jago 1981).¹⁸⁶ To exert their independence, many towns gave their

¹⁸³ Representation in the Cortes had its benefits since such towns were able to favor themselves at the expense of the unrepresented towns.

¹⁸⁴ New taxes and renewal of existing subsidies required the consent of a majority of the 18 towns represented by the Cortes. The Cortes depended for their assembly on royal summons. A minister of the Crown would summon the Cortes for financial needs. The deputies of the Cortes would then agree on an amount to be raised, and imposing as a condition of the grant that it be applied to the expenditure for which it was requested.

¹⁸⁵ Castile was directly ruled and taxed by the crown, making it easier for Philip IV to extract revenue and man-power for Spain's armies. In contrast, in the rest of the empire the authority of the crown was constrained, particularly in Aragon, Catalonia, and Valencia. Although there were attempts to get other kingdoms of the Monarchy to come to Castile's assistance and share in the burden of the empire's defense, they were successful in resisting such moves.

In terms of the Cortes, it is important to note that the crown paid the expenses of the members of the Cortes while in session and rewarded good voting behavior. Olivares was also able to pick his own men in some towns.

¹⁸⁶ Up until the 1630s, scholars differ on the influence of the Cortes over the crown. At one extreme Elliott (1963) and Stradling (1988) view the Cortes as a peripheral institution of little political importance (and a rubber stamp), while Jago (1981), and to a much greater extent, Thompson (1982), argue

deputies to the Cortes only the provisional power to vote, reserving for themselves the right to ratify the grant offered to the Crown. The Crown opposed this move to usurp power, instead favoring deputies having full voting powers.

In 1632, when Philip IV convoked the Cortes, he insisted that the cities grant their delegates full powers enabling them to conclude agreements directly with the Crown. Isolated from the immediate control of their cities, the Crown was able to capture the administration of the *millones* through financial inducements to the deputies and by the appointment of senior royal officials to share administrative responsibilities. Consequently, during the 1630s and 1640s, the Cortes voted significant increases in the *millones*, granting most of Philip IV's requests. By the 1650s, the king wrested the *millones* from municipal control, and in 1658, succeeded in annexing the commission of *millones* to his Council of Finance, dissolving the Cortes in 1664 (Lynch 1992, 130; 1969, 88-93; Thompson 1982; Stradling 1988, 129-150).

In addition to the *millones* (which accounted for 50 percent of revenue in the 1640s), Olivares had several other means to extract domestic resources for military spending. First, the *alcabala* was a 10 percent tax on sales (2.7 million ducats in 1612, yet many individuals were exempt or paid a reduce rate; Lynch 1992). Second, there were revenues from ecclesiastical sources. Third, 20-30 percent of the registered bullion that crossed the Atlantic belonged to the Crown, known as the "royal fifth" (both gold and silver). More importantly, these remittances assured a regular supply of silver which was necessary for large-scale borrowing (Elliott, 1992, 237). The Spanish monarchy operated on credit (or deficit finance) and the annual silver receipts were the most negotiable security for its loans (Stradling 1981).

that the Cortes could determine "what would be taxed, how, and at what rates" (1982, 36). There is consensus that by the 1630s, the Cortes were greatly weakened.

Finally, Madrid resorted to the coinage of copper or *vellón* coins in order to save the silver with which it had previously been alloyed, while the government accrued the profit. Between 1621-6, the Crown coined 19.7 million ducats of *vellón*, from which it made a profit of 13 million ducats, only stopping in 1628 due to domestic opposition from the business community (Parker 1992, 118). In 1628, the Crown agreed "never to increase the tale of copper *vellón*" but in 1636 new restamping was decreed. Further, the Crown compensated merchants who had their gold and silver returns confiscated with *vellón*. The problem was that coinage of *vellón* wreaked havoc with the rate of exchange, confused the monetary system (much of the copper used in the process had to be purchased from Sweden through the Dutch), and its debasement contributed to inflation (Lynch 1992). As taxes were paid in copper *vellón* and defense expenditures abroad had to be made in silver, the Crown itself was one of the biggest losers.

Domestic Reforms, Union of Arms, National Banking System, Revitalized Economy

In the search for additional necessitated by the rising costs of hegemony, Olivares attempted a series of domestic reforms (in terms of men and revenue; Elliott 1963, 1991; Lynch 1992). Olivares' ultimate goal was the unification of the empire. The problem for Philip IV was that outside of Castile, Madrid had limited constitutional power to extract revenue and resources. The constitutional structure of the Spanish empire and the diversity of the laws within it prevented the central government from taxing the periphery by executive means; the Spanish monarchy was not a federal system, but a union with independent and partially autonomous provinces (Lynch 1992).¹⁸⁷ Aragon, Catalonia, and Valencia were governed independently, with their own laws and tax systems. In each case, the king was represented by only a viceroy. In Sicily, Naples, and the duchy of

¹⁸⁷ As a loose collection of jurisdictions, Stradling notes that Spain lacked a corporate identity (1984, 78).

Milan, the king of Spain governed by governors. In the Low Countries, the king ruled through archdukes. Portugal was completely autonomous in fiscal matters. Consequently, the burden of defense of the empire fell primarily on Castile, with some provinces bearing little or no costs of defense. For Olivares, unification or castilianization of the Spanish Monarchy was the solution to this problem (the seat of the Monarchy was in Madrid). However, a unified Spain with shared rights and duties would require that provincial laws and liberties be brought into conformity with Castile's, which the provinces were likely to fight.

Short of unification, in 1625, Olivares called for the creation of a burden sharing arrangement known as the "Union of Arms" (which was designed to replace the *millones*). Under the existing system, Castile contributed the bulk of revenue for imperial defense, followed by the Italian states, and then the Low Countries, whose defense was subsidized by Castile (Lynch 1992, 43). Navarre, Aragon, and Valencia granted occasional amounts to Castile, and finally, Portugal and Catalonia refused to contribute to imperial defense beyond their frontiers. The Union of Arms (see table 3) was a burden sharing scheme, assigning each kingdom and province of the monarchy (Castile, the Crown of Aragon, Portugal, Naples, Sicily, Flanders, and the Indies) responsibility for the provision of a quota of men for the army. Under the Union of Arms scheme a common reserve of 140,000 men would be supplied and maintained proportionally by all the provinces of the Monarchy, taking some of the burden off of Castile (Elliott 1963, 330).

Table 3.--Union of Arms

Region	Men (thousands)	Region	Men
Castile	44	Aragon	10
Catalonia	16	Milan	8
Portugal	16	Valencia	6
Naples	16	Sicily	6
Flanders	12	The Islands	6

Notes: Stradling 1981, 96

The barrier to Olivares' plan was the autonomous rights of the regions. Initially, the Cortes of Aragon, Valencia, and Catalonia objected to raising money and troops for use outside of these provinces. However, in 1626, Valencia and Aragon agreed to a subsidy to support troops for fifteen years. Peru and Mexico were also assigned a financial quota to apply to the naval defense on the transatlantic route. Better equipped to resist the Crown, the Catalan's Cortes and Portugal (after incorporation into Spain, Portugal maintained its administrative and fiscal independence) rejected the Union of Arms, contributing to the revolts in Catalonia and Portugal in 1640.

Second, in the continued search for additional resources, Olivares called for the creation of a national banking system (1623), under royal jurisdiction, allowing Spain to mobilize credit for the defense of the empire at relatively low rates. A chain of banks would assist the Crown to reduce its debts, lowering its dependence on foreign loans (Elliott 1963). Unfortunately, the banks were mistrusted and the idea was abandoned in 1626. Finally, attempts were made to generate additional wealth by promoting the economic revival of Castile through the creation of trading companies and new industry,

and encouraging trade by improving the infrastructure such as roads and navigation of rivers.

In summary, by the 1630s, Philip IV had gained significant fiscal autonomy over Cortes, granting him the capability to extract an ever-increasing amount of resources from Castile for the defense of the empire. The combination of declining returns from the Americas, the exhaustion of Castile, and French, English, and Dutch encroachment, put added pressure on Spain to extract additional resources from its empire, including the non-contributing provinces of Catalonia and Portugal.

Spain's Response: Managing Hegemonic Decline

Domestic Resource Extraction

Facing so many potential contenders for regional hegemony, Spain's existing rate of resource extraction was insufficient to defend its global empire. As Paul Kennedy notes, "[Spain's] price of possessing so many territories was the existence of numerous foes" (1987). The dilemma for Philip IV and Olivares was how to restore the balance while protecting Spain's fiscal strength and national security. Spain's imperial commercial policy excluded a strategy of devolution of regional hegemony. Viewing imperial France, England, and the United Provinces as threats, devolution would undermine Spain's national security by strengthening the war-making capacity of these rising challengers. Restricted to a strategy of accommodation or extraction, as a domestically unconstrained imperial hegemony (with the weakening of the Castilian Cortes), extraction was a more attractive option. Accommodation, in order to lower the costs of hegemony, was rejected for fear of undermining Spain's reputation.¹⁸⁸ Both Philip IV and Olivares believed that accommodation in one locale would threaten Spain's

¹⁸⁸ See Chapter 2 and 3 for a discussion on the chainstore paradox.

reputation for defending the remaining parts of its empire. Even the president of the Council of Finance agreed that "the lack of money is serious, but it is more important to preserve reputation" (Elliott 1989, 124). Instead, by increasing its rate of resource extraction for military spending, Spain could deter France, England, and/or the United Provinces from challenging its regional hegemony, and in the event that deterrence failed, prepare for preventive wars while it still had the advantage. Concerned that the loss of a valuable locale to one of these challengers could tip the delicate balance of power against Spain, the Crown stood firm in the bulk of his empire, including the Netherlands, Germany, Italy, and the Indies, trimming Spain's commitments only in less valuable regions whose loss would have little impact on the global balance.

In the short run, in increasing the rate of extraction, the King had sufficient military capability to defend his extensive global commitments, ensuring that Spain remained in the ranks of the great powers longer than its alternative options of devolution or accommodation. By imposing new and ever greater taxes on wealthy Castile and borrowing heavily, the Crown was able to out-pace the combined military buildup of France, the United Provinces, England, and lesser powers such as the Ottoman Empire and Sweden, often fighting on several fronts simultaneously. Failure to increase its rate of resource extraction while maintaining its empire would have left Spain weak and vulnerable to attack everywhere. A disequilibrium between Spain's military capability and its global commitments was especially dangerous because this imbalance might tempt some or all of the rising imperial states to challenge Spain's leadership by launching preemptive strikes. Alternatively, in accommodating France, Britain, and/or the United Provinces, Spain risked undermining its immediate national security by strengthening their war-making capacity.

In the long run, a strategy of extraction eroded Castile's economic base, which was necessary to finance a large and modern military, contributing to its fall from the ranks of the great powers to the "sick man" of Europe. The problem for Spain was that it had no good options. As an imperial hegemon, Madrid could only select from an array of security strategies that risked eroding either its fiscal strength or its national security. Consequently, with Spain showing little concern for finances, the wars in the Netherlands, Italy, France and Germany, and the expeditions to recover possessions in the Americas were paid for by higher and new taxes in Castile and Italy, heavy government borrowing, confiscated private returns from the Americas, *vellón* coinage, and suspension of debt payments (the annual royal budget was 12-15 million ducats, with one-third of the Crown's budget going to service the debt). In fact, Philip IV and Olivares rarely consulted the Council of Finances (the treasury) in the formulation of foreign policy. The consequence was that excessive and sustained resource extraction for military spending diverted resources from domestic investment, contributing to Castile's de-industrialization and de-population. Unable to keep pace with the combined military buildup of the emerging contenders, Spain became weak and vulnerable to preemptive attack. The stress of extraction also contributed to revolts in disparate provinces, and ultimately to the break up of the Spanish monarchy.

Standing Firm in the Netherlands

In the Netherlands, Spain stood firm against the emerging Dutch Republic, even in the face of financial and military support from Britain and France. Lasting more than eighty years, Madrid's defense of the Spanish Netherlands against the Dutch, English, and French, was extremely expensive in terms of resources, men, and money. The Spanish Netherlands were valuable to Spain for a number of reasons. First, at stake in the Low

Countries was imperial defense (Lynch 1969). The Dutch waged an aggressive war on Spain's overseas possessions. Engaging the Dutch in a war in the Netherlands would reduce the resources Amsterdam could allocate to the conquest of Spain's empire.¹⁸⁹

Second, Flanders (one of the states in the Spanish Netherlands) was a center of mercantile wealth and capital. In retrenching, either the Dutch or the French would capture the economic wealth of the region, increasing their potential war-making capacity.¹⁹⁰ The added wealth from Flanders would grant the Dutch East and West India Companies or France additional resources for the war on Spain's remaining empire (See Brightwell, 1974a). Finally, from the Spanish Netherlands, Spain could protect Italy and Spain from invasion by France (Israel 1990). With an entrenched army in its rear, close to Paris, France could not shift the bulk of its forces southwards for an all-out attempt on either Spain or Italy without being exposed.

Through a series of quick victories to repair its reputation, Madrid intended to renegotiate the peace treaty with the Dutch from a position of strength (and detach them from their alliance with France). Consequently, beginning in 1621, Spain's army of Flanders went on the offensive, reconquering parts of the Netherlands (Breda in the north in 1625, virtually surrounding the United Provinces).¹⁹¹ However, after the victory at Breda (1625), financially exhausted and short of money, Madrid took the defense in the Low Countries.

¹⁸⁹ From the Dutch perspective, expansion in Asia at the expense of Portugal and Spain was seen as a way to divert Spanish energies and resources away from the United Provinces (Scammell 1989).

¹⁹⁰ In Europe, the Eighty Years' War marks the decline of Antwerp as a financial center (part of the Spanish Netherlands), undermined by the Dutch blockade of the Scheldt during the war, while the growth of Amsterdam strengthened the United Provinces.

¹⁹¹ With the intention of inflicting damage on Dutch trade in the Mediterranean, a Gibraltar *armada* was established and Gibraltar's harbor was improved and fortified. Additional funds were allocated to the main Spanish fleet, *the armada del mar oceano*.

The problem for Spain was that the Low Countries were consuming a large amount of resources. During the Twelve Year Truce, Spain's cost of maintaining its army of Flanders was 1.5 million ducats annually. This number ballooned to 3.5 million annually after 1621. Naval construction for the defense of the Atlantic and English Channel added an additional 1 million ducats per year. As a direct consequence of this heavy military spending, in 1627, Madrid decreed bankruptcy since the Crown could not finance both the war and service the debt to the bankers (declining return from the Indies hit a low of 1 million ducats in 1627).¹⁹² The worst was yet to come. In 1628, the cost of the Mantuan war with France and the loss of revenue due to the capture of the Mexican silver fleet, in addition to the declining returns from the Indies, brought the campaign in the Low Countries virtually to a halt for several years.

In response to its dire financial condition, Madrid instructed the army of Flanders to pursue a less costly defensive strategy in the form of economic warfare against the Dutch (however, the maritime war on Dutch shipping and trade required the construction of a costly naval squadron based in Dunkirk). In fact, no military campaigns were prepared between October, 1628, and May, 1629, because no money arrived from Madrid (Parker 1972, 256). To further reduce the costs of hegemony, there was discussion of a *rapprochement* with France, which ultimately failed. Even after 1629, provisions sent to the Netherlands were limited because money was needed to fight the French in Mantua and the Dutch in the Americas.

¹⁹² Elliott claims that this bankruptcy was in reality a ruse to reduce the crown's dependence on the Genoese bankers and to lower the high rates of interests on the *asientos* by encouraging competition from Portuguese businessmen (189, 125). Spain's growing dependence on the Portuguese bankers is interesting for two reasons. First, the crown's growing dependence on the Portuguese bankers meant that it was more difficult to reach a peace settlement with the Dutch on the issue of Brazil. The rationale is that Portuguese bankers were unwilling to abandon their Brazilian empire to the Dutch. Second, many of the Portuguese bankers were Jews who had fled Spain. Later, the financing of the Spanish army of Flanders and the trade between Spain and Holland was undertaken largely by the Jewish community of Amsterdam (Parker 1980, 279).

Beginning in 1634, the Crown again renewed its effort to restore Spanish prestige (especially after the humiliating setbacks by the Dutch in 1629-1633), hoping to inflict enough defeats on the Dutch front in order to produce terms for a satisfactory truce (Israel 1982). This formidable buildup was possible by increasing the rate of extraction in Castile and Italy. In 1635, in the aftermath of France's invasion of the Low Countries (opening a new front), Spain's Cardinal-Infante invaded France, advancing to within 80 miles of Paris before petering out into a costly war of attrition (and one of the most expensive defense budgets ever). In 1637, the Dutch front was once again the center of conflict (while the French were preparing to attack the Basque country of northern Spain). The Spanish land offensives were a final attempt to improve Spain's bargaining position with the Dutch. However, French and Dutch attacks stalled the Spanish offensive, especially with the French closure of the Spanish road in 1638 (Parker 1972, 80-105).

The final phase of the Dutch-Spanish war was a last Spanish offensive at sea intended to reverse its position in northern Europe and to restore its hegemony in the Atlantic. In 1639, at great expense, two large *armadas* were dispatched from Spain, one to the English Channel to force military supplies through to Flanders (with the closure of the Spanish Road in 1638, the Spanish were forced to reinforce the army of Flanders by sea) and to challenge the Dutch for supremacy at sea, and the second force to Brazil to recapture Pernambuco and its sugar plantations from the Dutch. In the English Channel, both Spain and the Dutch deployed about 100 ships each, with 20,000 Spanish and Italian troops, while the *armada* sent to reconquer Brazil included a powerful fleet of forty-one ships and 5,000 troops (reinforcement from the region brought the *armada* up to eighty-six ships and 10,000 troops). Unfortunately for Spain, its Continental *armada* was

defeated in the Battle of the Downs in the English Channel, and its America's *sarmada* was defeated by bad weather and the Dutch off the coast of Brazil.¹⁹³

The Netherlands war was a colossal drain on Spain's overstretched resources. As one of Philip IV minister's noted, "The war in the Netherlands has been the total ruin of this monarchy." The war in the Netherlands was costly for Castile in both men and money. On average, 8,000 men a year were recruited from Castile for 80 years out of a population of 4.5 million (Parker 1979). Spain's expenditures on the army of Flanders increased from 1.5 million ducats during the Truce to 3.5 ducats a year after 1621 (while in the best years the treasure fleets was bringing in 1.5 million ducats), with another 1 million ducats allocated to the Atlantic fleet (between 1635-7, Spain spent 15 million ducats in Flanders; Israel 1990, 37). In fact, between 1566 and 1654, Castile sent the Military Treasury in the Netherlands roughly 218 million ducats, while during this same period Castile received only 121 million ducats from the Indies (Kennedy 1987, 51; Parker 1980, 174). The difference in revenue was made up by ever-greater taxation in Castile, the coinage of *vellón*, and heavy government borrowing.

Standing Firm in Italy

Spain also stood firm in Italy in the face of Ottoman and French challenges. Spain's empire in Italy was important for a number of reasons. First, it was the outer perimeter of Spain's defenses against the Ottoman Empire. As late as 1600, Turkish

¹⁹³ In 1640, the Spanish Netherlands were invaded by both the French and Dutch. Spain's response was to strike into France from Flanders in order to put pressure on France so as to limit their support for the revolts in Catalonia and Portugal. In 1643, the army of Flanders was defeated in Rocroi, with the bulk of the high-grade troops captured or killed. In 1645, they captured 10 major towns in the Spanish Netherlands. In 1646, as the French conquest of Flanders continued, the Spain and the United Provinces began to negotiate a peace.

It should be noted that Spain's loss of Portugal's empire in the Americas, and especially in Brazil to the Dutch, put additional pressure on Spain's relationship with the Portuguese, contributing to the revolt in 1640.

successes in Croatia brought Ottoman forces within 100 kilometers of Trieste. Second, Italy was a wealthy region in which the Spanish King extracted additional resources for the defense of his empire, and its loss would strengthen the war-making capacity of imperial France (especially the loss wealthy Milan). Finally, Italy was the gateway of the strategic Spanish Road which connected Italy to the Netherlands (especially with the closure of the sea-route to Flanders, or the English Road). Stradling calls this area the "nerve-centre of communications and of the whole warmachine" (1981, 88). Control over strategic passes such as the Valtelline Pass were key in regulating the flow of armies and commerce in Europe (linking Spanish and Austrian Habsburgs, and Spain's empire in Italy and the Low Countries).

In 1628, to defend Italy from France, Spain initiated the War of Mantua, forcing Madrid to fight simultaneously in Italy and the Netherlands. In a supposedly quick and easy war, Spain invaded Mantua to capture the strategic passes around Casale, making its position in Northern Italy impregnable (while its loss would undermine Spain's reputation). Unfortunately for Spain, the end of the religious wars in France freed the French army to oppose Madrid by aiding the new Duke of Mantua. The ensuing war with France forced Spain to divert valuable resources away from the Netherlands. In 1631, the Peace of Cherasco, recognized Nevers' succession, a victory for France, further eroding Spain's reputation and threatening the strategic Spanish Road. In the aftermath of Mantua, the French continued to harass Spanish Italy, launching offensives against Milan (1637-1648), Genoa (1645), and later assaulted Naples (1647).

The second front opened by the three year struggle for control of Mantua placed an enormous additional strain on Castile's resources and diverted resources from the Netherlands front, bringing the campaign to a virtual halt (during this period, Spinola, the commander of the army of Flanders, called for renewal of the Dutch truce). Financing of

the wars against France in the Netherlands and Italy were achieved by augmenting the *millones*, at the same time when the loss of the treasure-fleet played havoc with royal finances. In 1629, the Mantua conflict required 1.8 million ducats, and in 1630, in addition to the 1.8 million from the two treasure fleets, the Crown added a half million loan to cover the cost of the conflict (Lynch 1992, 106).

Standing Firm in northern Europe

In addition, Spain stood firm in the face of challenges to its position in northern Europe. Spain supported the King of Bohemia in his attempt to put down the Protestant revolt. Germany was an important link in Madrid's defense of the strategic Spanish Road which connected the Low Countries and Italy (the Lower Palatinate was an essential part of its strategic communication). The loss of this locale would undermine Spain's ability to reinforce its position in the Spanish Netherlands and to move men and troops between the Low Countries and Italy, as needed.

To defend its position in Germany and especially its strategic communications with its empire, Spain contributed men and money to a joint Habsburg force, costing 350,000 ducats a year (Stradling 1981). In 1619 and 1620, this force crushed the Bohemian revolt, capturing Alsace, which was vital to Spain's communications between Lombardy and the Low Countries, and the Lower Palatinate, important for communications between Italy and the Netherlands. In 1632, to counter the gains of Sweden and France, Olivares renewed his collaboration with Austria, signing a treaty of mutual assistance known as the Catholic League, requiring additional contributions of men and money.

Standing Firm in the Americas

Outside of Europe, Spain stood firm in the wealthy East and West Indies. Spain could not retreat from the Americas for three reasons. First, as a source of extreme wealth (silver and gold, sugar, salt), the America's remittances contributed to the Crown's total income. The Spanish Crown received its "royal fifth" of the silver and gold mined in the American empire, while the private silver and gold returns increased the tax base and wealth which the Crown could extract (by the 1630s, due to the growing burden of empire, the Crown confiscated private shipments of bullion in exchange for *vellón*).¹⁹⁴

Second, the wealth of the Americas allowed Spain to borrow money at short notice and in great amounts (Brightwell 1974b, 271-272). Madrid's credit-worthiness was the real strength of Spain. Spain's credit-worthiness was determined by the size and reliability of its forthcoming revenue. For the crown, the silver bullion of the Americas provided a large and relatively reliable source of revenue that Spain could borrow against. In fact, Spain often owed several years of bullion to Italian and Portuguese creditors. Consequently, any decline or loss of this remittance would undermine Spain's ability to finance its imperial defense.

Third, in retrenching from the Americas, Spain risked strengthening the war-making capacity of the United Provinces and England. As an imperial challenger, the Dutch would bloc Spain's future access to the America's by creating its own exclusive sphere in the region. In capturing the wealth of this region, the Dutch would have the resources to continue Holland's assault on Spain's empire and Flanders. The Dutch already had the world's largest navy and the only standing army in Europe comparable in strength to Spain's (Israel 1990).

¹⁹⁴ Silver came primarily from Mexico and Peru and was shipped to Spain in two annual convoys

Spain was prepared to defend its empire in the Americas, building new fortresses, strengthening garrisons, and stationing additional troops and ships throughout the region (especially the silver producing areas of Peru and Mexico). Up until 1621, Spain maintained only a few fixed garrisons in the Americas (primarily in Cartagena, Veracruz, Callao, and Acapulco). After 1621, the Dutch WIC and English penetration could be prevented only if a much more ambitious defense policy was adopted. In 1625, 1630, and 1639, Spain sent large *armadas* to Brazil in order to retake territory lost to the Dutch. To recapture lost territories in the Caribbean, Spain implemented a scheme to base a permanent naval task force strong enough to expel Dutch fleets (Israel, 1982, 280; 1990, 267-70).¹⁹⁵ The Crown also built a cordon of strong-holds in forward positions across the Caribbean to provide bases for rapid deployment, and new militias were established in Cuba and Mexico, and a standing army in Chile.

Spain's forward policy in the Americas imposed enormous strain on its imperial finances and colonial treasuries, diverting resources from other fronts. In addition to resources from Castile, the Council of the Indies was directed to find 500,000 pesos yearly in New Spain for the building, arming and maintenance of fourteen heavy galleons. In 1624, the viceroy of Peru spent 200,00 ducats on defense, and by 1643, the amount had risen to 948,000 ducats (Parker 1979, 190). The same pattern held for Mexico. Following the partial success of the Union of Arms in Europe, Olivares expanded it to the New World, forcing an additional 250,000 ducats from New Spain and a further 350,000 from Peru (Lynch 1969, 99).¹⁹⁶

¹⁹⁵ This task forces was *Armada de Barlovento* consisting of eight galleons. The armada was manned and supplied by the Americas.

¹⁹⁶ In the East, the VOC waged a relentless war against Spain's Portuguese empire, with the Crown concentrating its efforts on the defense of the Americas over Asia. In conquering Portugal's major bases in the region, the Dutch supplanted Portugal and Spain in the Far East and gradually dislodged the traders of the English EIC from their footholds in the Spice Islands. In 1619, the VOC established a colonial capital in Batavia (Jakarta), clashing with the English base in nearby Bantam. In the Indian Ocean, the Dutch again

Deindustrialization and depopulation

Favoring security over finances, the wars in the Netherlands, Italy, France and Germany, and the expeditions to recover possessions in the Americas were paid for by higher and new taxes in Castile, Italy, and New Spain, government borrowing, confiscated private remittances, *vellón* coinage, and suspension of debt payments. In the long term, too heavy a burden on Castile's economy could not be borne indefinitely without ruining Spain's future capacity to wage war. In particular, excessive and prolonged military spending eroded Spain's economic base, and ultimately its military power. In contrast, neither France, the United Provinces, nor England were saddled with the expense of imperial defense. These challengers did not have to build, maintain, and defend fortresses and navies to protect their empire and strategic lines of communication. Furthermore, they were not burdened with the cost of fighting several challengers in disparate regions and fronts simultaneously.

The link between Spain's excessive defense spending and its decline from the ranks of the great powers is several-fold. First, excessive and sustained military spending diverted resources from domestic investment, limiting the scope of Spain's future economic growth. Facing several emerging contenders in disparate parts of its empire, rising defense expenditures forced Philip IV to turn towards the Cortes on eight occasions for additional revenue. The *millones* was initially set at 2 million ducats a year, and in 1626, the Crown raised it to 4 million ducats a year.¹⁹⁷ Beginning in the 1630s, with the weakening of the Cortes, the deputies voted unparalleled increases in the number and

clashed with Portugal (and the English East India Company), conquering Goa and Ceylon. Thus, by the mid-seventeenth century, the VOC had a chain of trading posts, forts and concessions stretching from the Indian subcontinent to Japan.

¹⁹⁷ By a new tax on paper, salt, and ship anchorage.

scale of the *millones*. In 1632, the Cortes granted an extra subsidy of 2.5 million ducats every six years.¹⁹⁸ In 1623, the Council of Italy was informed of the need to exploit the resources of Naples and Sicily. In the 1620s, Naples' *millones* was 1.2 million ducats annually, and reflecting the increasing cost of imperial defense, by the 1630s, the amount rose to 3.5 million ducats annually.

The crushing weight of defense expenditure fell almost exclusively on Castile. Increases in the *millones* (a tax on basic foodstuffs) and the *alcabala* (10 percent tax on sales paid by the localities) deprived Castile of capital for domestic investment and forced the peasants into subsistence farming, undermining Castile's home market (contributing to the prolonged famines in the 1620s and 1640s).¹⁹⁹ High prices meant that peasants had little left over for consumption; heavy taxes, increased rents, and depressed living standards left the peasants with little reason to remain on the land, contributing to Castile's massive depopulation (in addition to the *millones* and *alcabala*, peasants had to pay tithes to the church, rent to his lord, and seigniorial dues; Elliott 1989, 223; Lynch 1992; Parker 1980, 147). The loss of skilled labor further undermined the likelihood of Castile's economic revival.

Increased taxation was insufficient to cover the widening gap between revenue and expenditure, resulting in reckless government borrowing which eroded Spain's credit-worthiness (further undermining Spain's long run ability to construct and maintain a modern military force). As the magnitude of Spain's debt accumulated, the cost of paying

¹⁹⁸ To be raised from new taxes on sugar, paper, chocolate, fish and tobacco, and by doubling the regular *millones* subsidy (Stradling 1969).

¹⁹⁹ For instance, between 1621 and 1627, taxation had increased two-fold and borrowing five-fold (Stradling 1988, 68).

interest on this debt rose, absorbing an ever-larger amount of the tax-revenue.²⁰⁰ The larger the state's debts became, the harder it was to meet Spain's debt; and, as collection became more difficult, higher guarantees from the Crown were demanded. At the same time, due to Dutch and English assaults, unpledged revenues became scarce, thereby constraining the ability to repay its past loans and secure future loans. At repeated intervals, Philip IV discovered that the treasury had no unpledged income or that no one was willing to lend additional funds.²⁰¹ As a consequence, in 1627 and again in 1647, Philip IV reneged on payments of 'domestic' or non-military loans, declaring bankruptcy. Interest payments were suspended and negotiations with creditors were initiated to alter the terms of the outstanding loans. However, repudiating Spain's debt was dangerous because it deprived the Crown of future means of financing imperial defense. Without the services of the bankers, the Crown could not gain credit. After the double blow of suspension of payments in 1627 and the loss of the treasure fleet at Matanzas in 1628, the Crown was unable to raise credit on a large scale, further undermining Madrid's ability to finance a modern military (Stradling 1981).

Second, the Crown's fiscal policy, the erosion of the home market, foreign encroachment on Spain's colonial trade (reducing the influx of private capital into Castile), and the Crown's attempt to squeeze revenue from Castile, contributed to unfavorable investment conditions. Spain's fiscal policies proved self-defeating when applied to the Castilian merchant community. *Vellón* coinage and the debasement of coinage, intended to increase the Crown's profits, resulted in the out-flow of capital and

²⁰⁰ In Spain, there were two types of loans: *juros* and *asientos* (Rasler and Thompson 1989). *Juros* represented funded debts. Annual interest payments would be derived from future specified revenue sources, as in pledging repayment for a loan via some percentage of the sales tax. *Asientos* were unfunded debts that tended to involve high interest rates.

²⁰¹ This relationship could break down as a result of various events. A slump in silver returns might prevent due repayment, a sudden military emergency might oblige the government to meet its costs directly, the crown's demand for loans might exceed what its bankers were ready to advance.

severe inflation, discouraging domestic investment. In 1628, the nominal value of the *vellón* coinage was reduced by 50%, bringing instant relief to the royal treasury, but heavy losses to individuals holding *vellón* (Elliott 1984). As well, merchants in Seville whose American silver was confiscated were compensated with relatively worthless state bonds (*juros*), further undermining Castile's business community. In 1629, over 2 million ducats in pure silver were expropriated (Stradling 1981, 99). The consequence was a decline in the confidence in Seville's business community, contributing to the decay of the once profitable trade between Seville and America, and the decline in the Sevillian system of credit to the Crown (Elliott 1963).

The high cost and lack of exports meant that Spain increasingly carried foreign goods, instead of its own products, to Spanish colonies in the Americas (Elliott 1989, 235). The colonies, and especially Mexico and Peru, developed their own indigenous industries and agriculture, growing less dependent on the mother country. As well, despite economic embargoes, Spain lost a large share of its domestic market to the English, French, and Dutch. The outcome was that Spain became increasingly dependent upon Britain, France, and the United Provinces for industrial and agricultural imports, undermining the former country's ability to make an economic recovery, and contributing to its relative industrial and technological decline.

Third, in diverting resources from domestic investment to military spending (and discouraging domestic investment), Spain's economy began to suffer severe dislocation, lagging behind France, England, and the United Provinces in key growth industries of the period (Lynch 1992, 211-220; Elliott 1989, 233).²⁰² In the seventeenth century, virtually

²⁰² During the decade 1610-20 the remittances from the Americas began to decline. Instead of the 2 millions of the early 1600s, the amount fell as low as 800,000 in 1620; recovering in the 1620s but between 1621 and 1640, 1.5 represented an exceptional year and not more than 1 million could be expected (Elliott 1989, 237). In 1640, no treasure arrived from the Indies and in 1641, the *Tierra Firme* fleet brought the crown only half a million ducats, followed by an equally small return from the New Spanish fleet. In both cases, the crown compensated half of the merchants' returns and compensated them with *vellón*.

every sector of Spanish industry was depressed, and Spain was growing increasingly backwards in textiles, metallurgy, and shipbuilding. In the textile industry, technical inferiority and inflation meant that Spain lost its market share to competition from English cloth.²⁰³ In the sixteenth century, Spain possessed a small but active metallurgical industry, which was an essential component for creating a modern arms industry. By 1619, the metallurgical industry could no longer meet domestic demands. Consequently, Spain became heavily dependent upon foreign-based iron production for the supply of military parts, particularly France and England, and by the 1650s its factories had nearly ceased production. In the case of shipbuilding, Spain failed to keep pace with the new techniques of the north-European dockyards. As Lynch notes, Spanish shipyards produced "huge and ponderous galleons, floating castles which were years behind the vessels of northern Europe in maneuverability and adaptability" (1992, 218; Elliott 1989, 233). As Madrid began to lag behind in productive investment in new products, its traditional wares-silk, textiles, leather, wood, wool and iron were priced out of their customary markets in Europe. Castile's increasing technological backwardness reduced Spain's future economic growth.

Finally, de-industrialization and de-population undermined Spain's capacity to finance and field a modern army and navy in defense of its global commitments, leaving Madrid weak and vulnerable to preemptive attack. In particular, Madrid fell technically behind the emerging challengers in naval construction, and was unable to recruit or finance an adequate number of troops or supply its infantry. On repeated occasions, financial exhaustion forced Spain to seek a cessation in its military activities, especially in its costly war in the Netherlands. Reductions in the army's budget meant that Madrid

²⁰³ According to Lynch, in one major textile city, the number of textile looms declined from 600 in 1580 to 300 during Philip IV's reign to a low of 159 in 1691 (1992, 212).

could no longer afford a modern military, sending the army of Flanders into battle against the French with inadequate cavalry because horses were too expensive (Lynch 1992, 165; Stradling 1984). The absence of a cavalry contributed to Spain's defeat at the battle of Rocroi (1643), eroding the reputation of the army of Flanders. In fact, the loss at Rocroi is often seen as the end of Spain's military power (Lynch 1992, 165; Stradling 1979b). In sum, the attempt to compete with the combined military buildup of France, England, and the United Provinces was too great for Spain's resources, and in the process, the Crown undermined Castile's economic base, and ultimately its military strength.

Revolt: Dissolution of the Monarchy

In the long run, excessive and prolonged rates of resource extraction contributed to the dissolution of Spain's global empire. The depression in Atlantic trade due to Dutch and English encroachment forced the Crown to look elsewhere for additional revenue. However, the stress of Spain's Union of Arms scheme, intended to create new sources of revenue, contributed to the revolts in Catalonia and Portugal in 1640, embroiled Spain in a costly civil war, and diverted dwindling resources from other fronts. By 1648, Spain was dependent upon its former Dutch rival to finance its war against their mutual French adversary in the Spanish Netherlands.

Decline in the revenue from the Atlantic trade and silver supplies (and growing debt), the collapse of Spanish shipping, and Castile's inability to meet the demands for manpower and money, forced Philip IV either to look elsewhere for additional resources or abandon his military buildup in defense of the empire. Introduced in 1626, the Union of Arms was designed to create an army recruited and paid in appropriate proportions by the various provinces. While opponents to this scheme in Valencia and Aragon eventually conceded, the Catalans refused to cooperate. For Olivares, this open

opposition to Madrid was a public trial for the Union of Arms; retrenchment would affect the compliance of the other provinces (Lynch 1992).

In order to force Catalonia into making a contribution, Olivares made the province a theater of operation in the war with France (which had been under siege by France since 1637). When Olivares planned military operations for 1639, he deliberately chose Catalonia as the front to fight France in order to force Catalonia to contribute to the Crown. However, in May, 1640, pent-up anger at the presence of the royal army in Catalonia exploded into rebellion. As Parker notes, "there are few clearer examples than the revolt of Catalonia of the role of war in turning a tense political situation into open rebellion" (1980, 257). Catalonia formed an alliance with France (and was ultimately annexed), forcing Spain to divert reserves to Catalonia.

Desperate for additional revenue and new recruits, Spain attempted to integrate Portugal into the Union of Arms as well. Portugal supplied no regular revenue to the central treasury and its Iberian defenses were subsidized by Castile, which was also expected to come to the defense of Brazil. Olivares offered improved status and opportunities in exchange for Portuguese troops and money. However, in 1640, Portugal declared its independence from Spain.²⁰⁴ Again Richelieu extended French assistance, opening a second front on the peninsula, and in 1641, the Dutch concluded a ten-year truce with Lisbon, and in 1661, an alliance with England. With troops in the Catalian front, Italy, Germany, and the Low countries, and Spanish naval losses in Brazil and the battle of The Downs, Spain had few troops to resist Lisbon.

1640 marks the beginning of the dissolution of Spain's empire and the erosion of its European primacy. In 1640, both Catalonia and Portugal renounced their allegiance to

²⁰⁴ The revolt in Portugal opened new opportunities for a truce with the Dutch since the conflict in the Americas was no longer an issue.

Philip IV (in 1647-8, Naples and Sicily rebelled).²⁰⁵ With the loss of Portugal, Spain lost most of its wealthy overseas empire, especially Brazil. Lacking resources to continue fighting on several fronts simultaneously, in 1644, Philip IV released a decree informing his ministers that he sought peace on all fronts.²⁰⁶ In 1648, in the Treaty of Munster, Spain recognized Dutch independence and gave the Dutch all the territory they occupied in the Americas, promising not to trade with Spanish domains.²⁰⁷ In return, the Dutch came to Spain's aid against the French assault on the Spanish Netherlands. Concerned about the growing power of France (and the possibility of a Franco-Spanish settlement), the Dutch preferred a weak Spanish buffer between itself and France, so the financing of the Spanish army of Flanders was undertaken by Amsterdam (Parker 1980, 279).

Spain's power and influence over the rules of the international system was on the wane. In 1659, in the Treaty of Pyrenees, Spain ceded to France territory in the Netherlands, and more significantly, parts of northern Catalonia. In 1667, Louis XIV attacked the Spanish Netherlands (the War of Devolution) and only the intervention of the maritime powers fearful of French continental hegemony prevented its loss. At the subsequent Conference of Aix-la-Chapelle, Spain was hardly consulted when deciding which gains France should retain (Stradling 1971).²⁰⁸ The process of dissolution

²⁰⁵ The fact that there was no revolt in Castile removed an essential condition for the complete collapse of the Spanish system

²⁰⁶ Olivares pushed for victory in the Netherlands and an acceptable truce with the Dutch, rather than concentrating on the French front. His rationale was that a truce would detach the Dutch from their alliance with France.

²⁰⁷ In the United Provinces, the champions of war with Spain in Flanders were also losing ground. The rationale was in part a result of the cost of war and the fear of an ascending France in Flanders. Both the East India Company and the West India Company, and the Republic of Zeeland, strongly opposed peace with Spain. After 1645, Holland (especially, Amsterdam, the Republic's richest city) refused to provide funds for the war, and supplying more towards the war effort than the other six provinces, this brought the army to a complete halt. Peace was partially the result of pressure from Holland.

²⁰⁸ According to the treaty, Spain was compelled to make payments to the Swedish army (i.e., Protestant mercenaries) for the defense of the Netherlands against France.

continued with the independence of Portugal (1668), and the loss of Flanders and Italy at the Peace of Utrecht (1713).

In summary, in facing an emerging France, England, and the United Provinces, Spain selected to restore the balance between its capabilities and commitments by increasing its rate of resource extraction for military spending. Concerned that the emerging contenders would accumulate power dwarfing its own military capabilities, Philip IV selected to stand firm in the bulk of his empire, retrenching only from areas of lesser strategic worth. The rationale was that the "loss" of a valuable locale such as Flanders, Italy, Germany, and/or the Indies could tip the delicate balance of power against Spain, endangering its survival. In contrast, retrenchment from less vital locales would have little if any impact on the global balance.

The problem with the strategy of extraction is that Madrid ignored the fiscal consequences of managing decline. In particular, excessive and sustained defense spending diverted resources from domestic investment, limiting Castile's future economic growth and eroding its economic base. Ultimately, Spain undermined its ability to finance a modern military force, leaving it weak and vulnerable to attack everywhere. Furthermore, Spain's need for ever-increasing resources provoked social unrest in its empire, and especially in Catalonia and Portugal, contributing to its dissolution.

Conclusion

Beginning in 1621, Spain faced an emerging France, United Provinces, and England as well as numerous other challenges to its hegemony in disparate parts of its empire. By the Treaty of Westphalia in 1648, Spain was increasingly dependent on the remaining great powers to protect its national interests. In the short term, a strategy of

resource extraction, ensured that Spain remained in the ranks of the great powers longer than its alternative options. In increasing its rate of extraction, Spain had sufficient military capability to defend its global commitments against the combined military strength of France, England, and the United Provinces. Alternatively, a strategy of accommodation risked undermining Spain's immediate national security by eroding its reputation, encouraging contenders to challenge it in the remaining parts of its empire. However, in the long term, as an imperial hegemon Spain could only select from a range of security strategies which risked either eroding its political economy or its national security interests. In selecting a strategy of extraction, Spain favored its national security interests over its political economy, eroding its industrial base and ultimately its ability to construct and maintain a modern military force, leaving it weak and vulnerable to preemptive attack.

Some scholars suggest that Spain should have "cut its coat according to its cloth" by abandoning parts of its empire. For example, John Lynch notes, "the logical procedure would have been to concentrate her efforts and resources on this front [the Americas, Spain's greatest source of power] by cutting them elsewhere" (1964, 347; see also Kennedy 1987, 49). In 1635, the Count of Huanes, called for abandoning both Flanders and Milan (see Elliott 1989, 133). In abandoning its position in other locales, such as Flanders and Italy, Spain could have concentrated the freed-up resources in the Americas or invested this "peace-dividend" at home. In either case, Madrid could have defended its remaining commitments with fewer resources, protecting its fiscal strength. However, as an imperial hegemon, Spain could not devolve hegemony without eroding its immediate national security (and its reputation), accelerating its decline over its alternative strategy of extraction. In retrenching from Italy, the Spanish Netherlands, Germany, and the East Indies, the emerging imperial contenders such as imperial France,

the United Provinces, and/or Britain could capture the economic and military assets in these wealthy locales, greatly strengthening their war-making capacity and ability to threaten Spain in its homeland and its remaining commitments. Thus, while a strategy of extraction ensured that Spain remained in the ranks of the great powers longer than its alternative options, as an imperial hegemon, Madrid could only select from a range of strategies which risked eroding its long term fiscal strength or its national security.

CHAPTER 6

CONCLUSION: PAX AMERICANA OR THE END OF THE AMERICAN CENTURY?

Summary

This dissertation is about managing hegemonic decline. The grand strategy of a declining hegemon is to remain a chief player in the great power game as long as possible. In remaining in the great power ranks, the declining great power can continue to influence the rules of the international system in order to advance its security and commercial interests. The time-frame I examine is the period in which the distribution of power is changing from hegemonic to multipolar. Besieged by emerging contenders in disparate parts of its extensive formal and/or informal empire, the dilemma for a declining hegemon is how to restore the balance between its military capabilities and its overseas obligations while safeguarding its political economy and its national security.²⁰⁹ In restoring the balance, a security strategy which favors either political economy or national security will accelerate its ranks from the great powers. In the short term, both liberal and imperial hegemons can select a security strategy which will accelerate or decelerate its rate of decline. However, in the long run, while decline is inevitable, only a

²⁰⁹ In particular, in maintaining its global commitments without increasing its rate of resource extraction in order to strengthen its military will leave it vulnerable to attack every where, while excessive and prolonged increases in order to keep pace with the military buildup of several emerging challengers will erode its fiscal strength and ultimately its military capability. Finally, in abandoning its empire in order to restore the balance it risks strengthening the war-making capacity of a rising challenger.

liberal hegemon can select a security strategy that safeguards its fiscal strength and its national security interests, remaining in the ranks of the great powers longer than an imperial hegemon can.

For both realist and globalist theorists, managing hegemonic decline is not an issue. For realists, a declining hegemon can always maintain a balance between its capabilities and commitments. In the face of emerging contenders, the declining hegemon will restore the balance between capabilities and commitments by either increasing military spending or reducing global obligations as necessary. In terms of increased military spending, there is little discussion among realist scholars of the fiscal consequences of defense expenditure, since ensuring the nation's security is its primary concern. Consequently, it is assumed that the state can bear the costs of increased defense spending. In reducing foreign commitments, the hegemon will only trim its commitments in less strategic locales, and always standing firm in strategic regions. For realists, neither domestic politics nor international institutions will constrain the state's choice of foreign policy strategies for restoring the balance.

For globalists, managing hegemonic decline is not an issue since the great power cannot affect its rate of decline. Differential rates of growth between the rising and declining states mean that a hegemon's decline will occur globally and universally (to defend its commitments it will have to undertake larger and more costly defensive efforts, accelerating its decline). As an emerging contender encroaches on the hegemon, the challenger will launch a preemptive strike, resulting in the rapid and complete loss of the hegemon's global empire to the new leader. Thus, for globalists, a hegemon cannot manage its decline.

Finally, for domestic politics arguments, domestic constraints will influence a hegemon's foreign policy adaptability. Domestic politics' arguments maintain that only a

domestically unconstrained hegemon can restore the balance by either increasing military spending or reducing global commitments. Domestic constraints, which include regime type, state-society relations, entrenched domestic groups, and biases of political leaders, prevent the hegemon from increasing military spending or reducing global commitments.

I argue that a hegemon can manage its decline and that its foreign commercial policy will influence, (1) how it restores the balance and (2) how long it can remain in the ranks of the great powers. A hegemon's foreign commercial policy can range from liberal to imperial, and reflects whether the hegemon will impose an open or closed door commercial policy across its overseas empire and in any region it comes to dominate. The hegemon's foreign commercial policy will shape and constrain its range of security strategies for restoring the balance. Thus, liberal and imperial hegemons will select from a different range of security strategies.

First, the nature of a hegemon's foreign commercial policy will affect how it restores the balance between capabilities and commitments. An imperial hegemon's foreign commercial policy will restrict its foreign policy alternatives to either a strategy of accommodation or extraction. In viewing all rising contenders (liberal and imperial) as threats to its national interests, an imperial hegemon will reject the option of devolution. The rationale is that neither liberal nor imperial contenders will maintain the declining hegemon's exclusive commercial arrangement in the locale, a liberal contender will replace it with an open door order while an imperial contender will replace it with its own exclusive sphere. In both instances, the declining hegemon will lose exclusive access to the locale, while strengthening the future war-making capacity of a rival.

One factor which will influence whether an imperial hegemon will select a security strategy of extraction or accommodation is its domestic flexibility. Unable to increase its rate of domestic resource extraction for military spending or reduce its global

commitments, a domestically constrained imperial hegemon's security options are limited to a strategy of accommodation. In accommodating some or all of the emerging contenders, the declining hegemon's intention is to slow their rate of ascent and lower the costs of hegemony. Any other strategy will accelerate its rate of decline. For a domestically unconstrained imperial hegemon, it can either select a strategy of extraction or accommodation. A strategy of extraction is more attractive because in increasing its rate of military spending it can protect its immediate national security, while a strategy of accommodation will strengthen the war-making capacity of its rivals.

The nature of a liberal hegemon's foreign commercial policy will include the security strategy of devolution (in addition to extraction and accommodation, depending upon its domestic flexibility). In contrast to the tenets of realism, a liberal hegemon will not view all emerging competitors for regional hegemony as threats to its security and commercial interests. Instead, the declining hegemon can differentiate between emerging imperial and liberal contenders; the declining liberal hegemon will view emerging imperial contenders as threats to its national security and commercial interests, and rising liberal contenders as supporters of its liberal commercial arrangement in the locale. The rationale is that an imperial contender will create its own mercantilist position in the locale, whether it is currently an open or closed door regional order, blocking the liberal hegemon's future access to its commercial interests in the locale. In devolving hegemony to an imperial contender, the liberal hegemon will strengthen the war-making capacity of a future rival, undermining its own national security objectives and accelerating its rate of decline. In contrast, an emerging liberal contender will maintain the existing liberal commercial order. In devolving hegemony to liberal contenders, the declining liberal hegemon will retain access to its traditional markets, investments, and sources of raw materials in the locale without any of the costs associated with regional leadership, and

without strengthening the war-making capacity of a future rival. Consequently, a liberal hegemon does not need to prepare to fight all emerging challengers, only emerging imperial contenders. Thus, in contrast to Modelski (1988), Organski (1968), and Gilpin (1981), hegemonic decline does not always result in major war between the rising and declining states.

Second, the nature of a hegemon's foreign commercial policy will affect how long it can remain in the ranks of the great powers. Facing emerging contenders, the dilemma for the declining hegemon is to restore the balance while safeguarding its fiscal strength and its national security. A security strategy which favors either fiscal or security concerns over the other will accelerate the hegemon's fall from the ranks of the great powers. Consequently, I contend that while in the short term, liberal and imperial hegemon can accelerate or decelerate their rate of decline, in the long term, only a liberal hegemon can select a security strategy which will protect both its security and fiscal interests, remaining a player in the great power game longer than an imperial hegemon can.

The realist strategy of managing decline suggests that a declining hegemon should restore the balance by increasing its military capability. In extracting or mobilizing domestic resources, a hegemon increases its military capability in order to keep pace (or out pace) with the combined military buildup of the emerging contenders. The intention is to deter emerging contenders from challenging the hegemon, and in the event that deterrence fails, to launch preventive wars destroying or weakening the rising competitors while the military advantage is still with the declining power. However, one of the main problems of a strategy of extraction (and realism) is that it ignores the fiscal consequences of managing decline; it ignores Britain's Exchequer's claim that financial strength is the third arm of defense. In particular, prolonged and excessive defense

spending to out-pace the combined military spending of several rising contenders will erode the hegemon's political economy, and ultimately its military capability.

Alternatively, a declining hegemon can select a strategy of accommodation. A strategy of accommodation involves concessions and compromises (such as arms limitation agreements) by both the rising and declining states. The declining hegemon's intention is to slow down the emerging contenders' economic/military ascent so that it can defend its global commitments with its existing rate of resource extraction. However, in the long run, a strategy of accommodation will erode its national security, since an emerging contender is unlikely to accept a permanent junior position in the locale, the rising state will cheat on any agreement, leaving the hegemon weak and vulnerable to attack.

Finally, a hegemon can select a strategy of devolution. A strategy of devolution involves ceding leadership to emerging contenders, and perhaps accelerating their ascent, even in strategic locales, in order to lower the costs of hegemony. Depending upon the nature of the declining hegemon's foreign commercial policy, a strategy of devolution can ensure that it remains in the ranks of the great power game longer than if it selects the alternative realist strategy of domestic resource extraction or the strategy of accommodation. The rationale is that devolution will safeguard the hegemon's fiscal strength and national security interests. However, only a liberal hegemon can select a strategy of devolution without eroding its commercial and security interests. First, in retrenching in regions with emerging liberal supporters, the hegemon will be able to defend its remaining commitments without significantly increasing its rate of resource extraction, protecting its fiscal strength. In retrenching, the declining liberal hegemon will retain access to its markets, investments, and resources in the locale without any of the political, military, or economic costs of regional hegemony. The hegemon can

concentrate these freed-up resources in its remaining commitments or redirect the savings to civilian investment, further reducing its defense spending. Second, in retrenching in regions with emerging liberal supporters, the liberal hegemon will not undermine its national security by strengthening the war-making capacity of a future rival. In fact, failure to devolve leadership to a rising liberal supporter, even in a strategic locale, means that the hegemon risks undermining its economic strength by prolonging excessive defense expenditure. Thus, in the long term, only a liberal hegemon can select a security strategy which will protect its fiscal strength and its national security interests, retarding its rate of decline from the ranks of the great powers.

Success and Failure: Managing Decline

One question that needs greater attention is the issue of success and failure in managing decline. What does it mean to manage decline successfully? First, there is a hierarchy among nations in the international system. Hierarchy connotes influence over the behavior of other states in the international system, allowing the great powers to establish the rules of the game which advance or favor their national interests over the other states (Levy 1983). Managing decline successfully involves remaining a player in the great power game or at the top of the hierarchy of states. In contrast, a hegemon fails to manage its decline if it fall from the ranks of the great powers. As a second rank power, its influence will be regional or local in scope, rather than global (shrinking to relative obscurity like Spain). With limited influence, a second-rank power will no longer be able to shape the international system in order to advance its needs or interests. One possible measurement of great power status is involvement in major international conferences, congresses (Concert of Europe), organizations, treaties, or other

participation (formal or informal) which grants the hegemon veto power over other states (see Levy 1983).²¹⁰

Second, managing hegemonic decline successfully involves retarding the rate of decline in the short term and the long term. A hegemon manages its decline successfully if it remains in the ranks of the great powers as long as it can. In the short term, successful management of decline involves selecting the security strategy that will decelerate the hegemon's decline from the ranks of the great powers relative to its alternative security strategies (i.e., the strategy that will allow the hegemon to remain in the ranks of the great powers longer than the alternatives to that state).²¹¹ In the long run, successful management involves selecting the foreign commercial policy that will decelerate its rate of decline over its alternative foreign commercial policy. In the first instance, success is relative to the other alternative security strategies available and in the second case it is relative to the alternative foreign commercial policies. Consequently, a hegemon can accelerate its rate of decline in two ways, (1) in the short run, by selecting a suboptimal security strategy, and (2) in the long run, by selecting a suboptimal foreign commercial policy. In selecting the foreign commercial policy which will ensure that the hegemon remains a key player in the great power game as long as possible, the great power will lengthen the time frame in which it can influence global politics to its advantage. Consequently, hegemons have strategic choice. In the short run, both liberal and imperial hegemons can select strategies which will accelerate or decelerate their rate of decline. If the declining hegemon chooses smartly, it can lengthen its tenure as a great

²¹⁰ It should be noted that there is debate over what characteristics define a great power, especially after the Cold War.

²¹¹ In all three cases discussed in this dissertation, Spain (1621-1648), Britain (1889-1912), and Britain (1932-1939), the hegemon selected the strategy that allowed each to remain a player in the great power game longer than any of its alternative foreign policy options (I intentionally selected such hegemons because they were the only states that could be contenders to manage their decline in the long term).

power over its alternative options. In the long run, hegemonies also have choice. In selecting a liberal foreign commercial policy, the hegemon can decelerate its rate of decline over its alternative option of an imperial foreign commercial policy.²¹² The rationale is that an imperial hegemon can only select from a range of security strategies which risks eroding its fiscal strength or its national security, while a liberal hegemon can select a security strategy which will safeguard its political economy and national security. Thus, a liberal hegemon can remain in the ranks of the great powers longer than if it was an imperial hegemon.

In the short term, both imperial and liberal hegemonies can select security strategies which can accelerate or decelerate its tenure as a great power. For an imperial hegemon, a strategy of devolution will accelerate its immediate rate of decline over its alternative foreign policy options of accommodation or extraction (depending on its domestic flexibility). Devolution will strengthen the war-making capacity of a future rival (liberal and imperial), eroding the hegemon's own immediate commercial and national security interests. For a domestically unconstrained imperial hegemon, a strategy of extraction will allow it to remain in the ranks of the great powers longer than its alternative option of accommodating, ensuring that it has adequate military capability to defend its global commitments. For a domestically constrained imperial hegemon, its only strategy to redress the imbalance between capabilities and commitments is a foreign policy of accommodation. Any other strategy will accelerate its decline from the great power ranks. Consequently, if a constrained imperial hegemon fails to reach an accommodation with any of the emerging contenders in order to slow their ascent, the former will have insufficient military capability to defend its global commitments, leaving it weak and vulnerable to attack everywhere.

²¹² One caveat, there must also be liberal emerging contenders, see discussion in Chapter 2.

For a liberal hegemon, a strategy of devolution will decelerate its rate of decline over its alternative foreign policy options of accommodation or extraction (depending on its domestic flexibility). In devolving hegemony to a liberal contender, the region will be governed in a way amenable to the hegemon's interests; the hegemon will retain access to the locale without any of the costs associated with regional hegemony. Consequently, the hegemon can concentrate these freed-up resources in its remaining commitments or invest this peace dividend at home. This strategy will extend the period in which it can influence the international system.

In the cases examined in this dissertation, the hegemons selected their best alternative strategies for restoring the balance, ensuring that they remained key players in the great power game longer than any of their alternative options. Had these hegemons selected alternative options, they would have accelerated their rate of decline. In the case of imperial Spain, Madrid selected a strategy of increased resource extraction over its alternative option of accommodation, outpacing the combined military spending of an emerging France, Britain, and the Netherlands, protecting Spain's immediate national security. In the case of imperial Britain (1932-1939), unable to increase its rate of extraction or reduce its global commitments, a strategy of accommodation slowed down the military ascent of Germany, Italy, and Japan, safeguarding Britain's fiscal strength in the event of a prolonged conflict. Had Britain failed to reduce the number of threats, they would have overwhelmed England's immediate military capability, leaving it vulnerable to preemptive strikes across its empire. Finally, in the case of liberal Britain (1889-1912), in devolving regional hegemony to the United States and Japan, London was able to concentrate its freed-up resources in its remaining commitments in its homewaters and Central Asia, protecting its fiscal strength and its national security interests.

In the long run, while decline is inevitable, a liberal hegemon can remain a key player in the great power game longer than as an imperial hegemon. An imperial hegemon will fail to manage its decline because it can only select from a range of security strategies which will erode either its fiscal strength or national security, even if it is well aware of what is happening. In particular, a strategy of increased extraction will erode an unconstrained hegemon's fiscal strength (disrupting the processes of investment and economic growth needed to renew its productive base for future military spending), and ultimately its ability to create and maintain a modern military force (higher budgets might also elicit higher spending by the rising contenders). Alternatively, a strategy of accommodation will erode a constrained hegemon's national security interests by strengthening a future adversary's war-making capacity. In falling from the ranks of the great powers to a second tier power, an imperial hegemon's corresponding influence will decline from global to regional or even local. Under this condition, the erstwhile hegemon will have limited ability to advance its interests, especially when they clash with those of the remaining great powers.

In contrast, a liberal hegemon can select a strategy of devolution which will protect its fiscal strength and national security, ensuring that it remain in the ranks of the great powers longer than as an imperial hegemon. First, in concentrating the freed-up resources in its remaining commitments, the hegemon will not need to increase its rate of extraction significantly, thereby safeguarding its fiscal strength. Second, in devolving hegemony only to liberal contenders, the hegemon will not strengthen the war-making capacity of a future rival, thereby safeguarding its national security. However, failure to retrench when the liberal hegemon has the opportunity, even in strategic locales, means that it risks eroding its fiscal health through prolonged high levels of defense expenditure.

While in the short term, both Spain, Britain (1889-1912), and Britain (1889-1912) selected the security strategy which ensured that they remain in the ranks of the great powers longer than their alternative options, in the long term, only Britain (1889-1912) could remain in the ranks of the great powers as long as possible. While Spain and Britain (1889-1912) selected their optimal security strategies, they selected a suboptimal foreign commercial policy. Had they also selected suboptimal security strategies, they would not have been in the running to manage their decline. In the case of Spain, in favoring its national security over its political economy, Spain eroded Castile's industrial base, and ultimately, its ability to construct and maintain a modern military force, leaving it weak and vulnerable to preemptive attacks by France, the Netherlands, and/or England. In the case of Britain (1932-1939), a strategy of accommodation eroded Britain's national security by strengthening the war-making capacity of imperial Germany, Japan, and Italy. In contrast, in the case of Britain (1889-1912), in devolving regional hegemony to the United States and Japan, Britain was able to safeguard both its economic strength and its national security interests. In remaining a key player in the great power game as long as possible, Britain was able to continue to influence the rules of the game for almost another five decades, protecting its national interests.

Regional versus Global Hegemony: Rise and Decline of the United States

How should scholars view hegemonic decline? As discussed above, globalists assume that a hegemon's decline will occur globally, rapidly, and simultaneously across its empire. According to this view, differential rates of growth mean that the emerging contender will capture the declining hegemon's entire empire in a single instance. However the problem with this global or universal view of decline is that it oversimplifies the dilemma that a hegemon faces in restoring the balance between its

capabilities and commitments. In most cases, had the declining hegemon confronted a single emerging contender, it could have concentrated its resources from its remaining commitments, overwhelming the challenger's military capability. Instead, the unit of analysis should be the region, not the globe (for this reason, I define a hegemon as a great power that establishes and enforces the rules of the game over several regions simultaneously). Based on a regionally differentiated view of world politics, a hegemon's decline (and rise) will occur at different rates and in disparate parts of its empire. Once more the hegemon is likely to confront different emerging contenders for regional hegemony across its empire. Even if it confronts the same emerging contender, this competitor is likely to challenge it for leadership earlier in some locales than in others. Such factors as the loss-of-strength gradient and the differentiated nature of power increase the likelihood that the declining hegemon will confront different emerging contenders on the periphery of its empire. In fact, the more extensive its empire, the greater the number of contenders it is likely to confront. Thus, the dilemma for the declining hegemon is how to restore the balance between its capabilities and commitments while protecting its political economy and its national security interests.²¹³

The U.S. experience is no exception to this regional view of rise and decline. The rise of America's informal empire was not global or uniform in nature, but began at the turn of the century with the domination over the Americas. During World War II, American hegemony expanded to include western Europe, the Northern Tier States and the Far East (a crescent stretching from Europe to Asia along the Soviet frontier). By the 1950s, the American sphere included the Middle East, and in the mid-1970s, the United States started to make in-roads into Africa. While America's formal and informal empire

²¹³ Since no power is likely to dominate all of the regions of the globe simultaneously, this regional view of the international system allows for more than one hegemon at any point in time.

was extensive, it was never global in nature. Certain regions such as Eastern Europe remained outside of the American sphere, while Britain and France continue to be the dominant actors in most of Africa (one author titled his chapter on Africa "'Non-Benign Neglect', the United States and Black Africa in the Twentieth Century").²¹⁴

Similarly, during the Cold War the United States (and the Soviet Union) encountered different emerging contenders in disparate parts of its informal empire. In the aftermath of the war, the initial competition took place along the Soviet frontier, stretching from Europe to central Asia to the Far East (Eastern Europe, Iran, Turkey, Greece, Manchuria; Schaller 1982; Gallicchio 1988; Gardner 1993; Hess 1987; Kuniholm 1980).²¹⁵ By the 1950s, beginning with support for Egypt, Syria, and Iraq, the Soviet Union challenged American hegemony over the Middle East, pushing its influence into the region (Campbell 1960; after the Suez Crisis, the Soviets engaged in a rapid buildup of conventional land and sea forces). In the 1960s and 1970s, the Soviet Union challenged American leadership in its own homewaters, including the Caribbean, Central America, and Latin America (Nicaragua, 1979). As well, Soviet conventional (Soviet

²¹⁴ During World War II, informally, the United States recognized that Eastern Europe fell in the Soviet sphere of interests. Churchill and Stalin worked out an agreement whereby Russia would exercise control in southeastern Europe and Great Britain in Greece, and the allies would share responsibility in Yugoslavia. Stalin traded American predominance in China (and Japan) for Manchuria. In the Far East, in exchange for Russia's pledge to enter the Asian war against Japan, Stalin received territorial concessions: the lease of Port Arthur, joint Sino-Soviet operation of the Chinese -Easter and South Manchurian railroads, possession of the southern Sakhalin and Kurile Islands, and a plebiscite to be held in Outer Mongolia; Gardner 1993)

Noer notes that Washington has historically neglected Africa and that as late as 1958, the U.S. had more diplomats in West Germany than in all of Africa (1981). In this context, it is interesting to note that in a bibliographic index on the origins of the Cold War, there is not a single citation on Africa (Black 1986). As former Assistant Secretary of State for African Affairs stated, "The U.S. policy was very explicit, giving major responsibility for Africa in global terms to the major metropolitan powers" (*New York Times*, 28 February 1995).

²¹⁵ In the aftermath of the war, the Soviet Union refused to evacuate its troops (by early 1946 most of the British and American forces had withdrawn). In Turkey, early in 1945, the Soviet Government made outright demands for joint control of the Straits and for a sizable part of Turkish territory (joint control over the strategic Dardanelles Straits). In neighboring Greece, the government was losing to Communist guerrilla forces believed to be supported by the Soviet Union.

fleet sailed in the Mediterranean, Indian Ocean, and even Caribbean areas) and nuclear buildup forced the United States to acknowledge Moscow as an equal in nuclear military capabilities.

During this same period, the rising economic and political powers of Germany and Japan were beginning to challenge America's predominant economic position in Europe and the Far East (overtaking the Soviet Union), respectively. Finally, by the mid-1970s, while not dominating Africa, the Soviet Union challenged the United States and its allies in Angola, Ethiopia, Somalia, and in the Persian Gulf region. New challenges to American hegemony came from the Third World, such as OPEC and the Group of 77 (New International Economic Order) demanding a reputation of world economic wealth and function within the world system. Thus, facing these emerging contenders on disparate fronts, the dilemma for the United States (and the Soviet Union) was how to restore the balance between its capabilities and commitments, while safeguarding fiscal strength and national security interests. In focusing solely on the Soviet challenge in a single region (or the American challenge from the Soviet perspective), scholars oversimplify the predicament that the United States faced in restoring this balance. Had the U.S. confronted only the Soviet Union in Europe, Washington could have concentrated its resources in the locale, overwhelming Soviet capability.

The United States and the Soviet Union during the Cold War: "Different Strokes for Different Folks"

During the Cold War, in facing emerging contenders for regional leadership, on disparate fronts, including each other, the United States and the Soviet Union had a number of alternative foreign policy options for restoring the balance between their military (and economic) capabilities and global commitments. Facing similar international pressures, why did American and Soviet leaders select different security

strategies and what lessons can one learn for the United States in the coming decades? As a first cut at this question, I suggest that due to differences in the nature of their foreign commercial policies, the United States *could* select a strategy of devolution and limited containment (however it did not always do so), while the Soviet Union *had* to pursue a strategy of extraction or risk accelerating its rate of decline.

In the case of the United States, as a liberal hegemon, it differentiated among emerging contenders, devolving leadership in regions with emerging liberal supporters and standing firm in regions with emerging imperial challengers (i.e., the Soviet Union and China). In devolving regional hegemony, the United States would retain access to its interests, markets, and resources in the locale without bearing any of the costs of hegemony. In fact, in contrast to realism, the United States assisted the ascent of liberal contenders (such as Germany and Japan), even in strategic locales such as Europe and Asia (the problem was that the United States was unwilling to retrench from these locales). In contrast, the Soviet Union, as an imperial hegemon, viewed all emerging contenders (liberal and imperial) as future rivals. Consequently, the Soviets could only select a strategy of extraction or risk undermining its immediate national security through the alternative strategies of devolution or accommodation, accelerating its rate of decline from the great powers. The rationale is that in devolving hegemony the Soviets could strengthen the war-making capacity of a future rival, eroding its own national security interests.

In the short run, both the United States and the Soviet Union were able to restore the balance between their capabilities and commitments. However, in the long run, even though the Soviet Union collapsed, the United States was not successful in managing its decline. For the United States, as a liberal hegemon, a strategy of devolution would slow its rate of descent over its alternative options of extraction or accommodation. The

rationale is that only a strategy of devolution can safeguard its fiscal strength and its national security interests. Properly pursued, in the long term, the United States could have concentrated these freed-up resources in its remaining commitments or invested this peace dividend at home, further strengthening its fiscal strength, and without strengthening the war-making capacity of a future rival. However, as discussed below, the United States initiated a policy of devolution but was unwilling to follow through with it completely. In particular, after assisting in the rise of Japan and Germany, under the Nixon administration, the United States was unwilling to devolve hegemony to these supporters. Beginning with the Carter administration, and especially under Reagan, the United States rejected a strategy of devolution, choosing a policy of extraction. However, a strategy of extraction accelerated America's relative decline over the alternative policy of devolution. Had the Soviet Union not collapsed as rapidly as it did, the United States risked greatly weakening its fiscal strength. In this sense, the United States failed to manage its decline by selecting a suboptimal security strategy of extraction.

In contrast, in the case of the Soviet Union, as a domestically unconstrained imperial hegemon, it selected a strategy of increased domestic extraction for military spending. In the short term, the Soviet Union kept pace with the combined military buildup of the United States, its allies, and China (liberal and imperial contenders). While extraction ensured that the Soviet Union remained in the great power game longer than its alternative options, in the long run, this strategy ignored the fiscal consequences of managing decline, eroding the Soviet Union's productive strength and ultimately its military capability, contributing to the dissolution of the Soviet empire (Bialer 1976). In particular, during the Cold War, a large share of Soviet wealth went to nonproductive military budgets. Up until the mid-1970s, Brezhnev built up his military by spending as much as 15 percent of the GNP on it, at the expense of domestic investment (LaFeber

1991a, 316). Consequently, the economy's growth rate fell to a zero percent increase. Ultimately, deindustrialization undermined the Soviet Union's ability to create and finance a modern military force. In late 1988, no longer able to afford the cost of empire, Gorbachev replaced the Brezhnev doctrine with the "Sinatra Doctrine" allowing the East Europeans to do things their way, contributing to the disintegration of the Soviet empire.

Ironically, one might argue that the Soviet Union managed its decline more successfully than the United States. The rationale is that the Soviet Union selected a security strategy that ensured it remain in the great power game longer than under any of its alternative options. In contrast, the United States chose a strategy of extraction, accelerating its decline quicker than under the alternative option of devolution. However, in the long run, the Soviet Union failed to manage its decline because of the nature of its foreign commercial policy, and the United States failed because it selected a sub-optimal foreign policy.

The United States: Global versus Selective Containment

How and based on what factors do declining great powers rank their global commitments and strategic interests? How do statesmen identify whether an emerging state is a potential ally (and acceptable regional successor) or a future adversary? How do leaders decide what proportion of the nation's resources to devote to defense? One historic debate in American foreign policy has been centered on how to prioritize America's global commitments. As early as the 1890s, with the closing of the American frontier, statesmen debated whether America's foreign policy orientation should be towards the Far East or Europe. The debate between the Asia Firsters and the Europe Firsters continued during the interwar period and even during the early stages of the Cold War.

As part of this discussion, during the 1950s and 1960s, one debate over the direction of American grand strategy centered on whether the United States should pursue a strategy of global or selective containment (strongpoint versus perimeter). Incorporated into this debate was how to rank or prioritize American interests and how to restore the balance between capabilities and commitments. A strategy of global containment entailed a strategy of resource extraction, while selective containment included devolution to rising contenders or regional surrogates. Hard-liners, such as Harry Truman, Dean Acheson, and Paul Nitze, advocated a policy of global anti-Communist containment, calling for an active U.S. policy throughout the globe, including the Third World. They warned of the dangers of falling dominoes and the damage to America's reputation in core regions such as Europe and Japan if the U.S. failed to defend its commitments in peripheral areas. This strategy was the source of the Truman Doctrine and the massive increases in the defense budget called for in NSC-68 (Gaddis 1982). A proliferation of foreign interests meant an increase in defense expenditures (costing \$50 billion annually or three and a half times the President's existing \$13.5 billion on defense). Since all interests were equally vital, the assumption was that the country could bear this massive military spending, protecting its national security.

In opposition, policy-makers and scholars like Walter Lippmann, George Kennan, Hans Morgenthau, and Norman Graebner opposed this strategy of global containment (so called soft-line realists).²¹⁶ Recognizing the reality of limited resources they rejected the universal commitment of the Truman Doctrine which called for the U.S. to defend any state threatened by communist invasion wherever it appeared. They criticized Acheson for containment beyond the capabilities of Western preparedness. They believed that

²¹⁶ Ironically, several of Waltz's students have adopted a differentiated view of international relations, such as Walt (1989) and Van Evera (1989). On the evolution of Norman Graebner's writing towards a soft-line realist position, see Combs (1987).

unrestrained military spending would set off either unacceptable inflation through persistent peacetime budget deficits or confiscatory taxes and economic controls.²¹⁷

Instead, they emphasized the need to differentiate among overseas commitments based on the region's strategic worth or value. In particular, they called for American intervention in strategic locales such as the Eurasian landmass and restraint throughout most of the non-vital Third World.

For instance, Kennan argued that there were only five centers of industrial and military power in the world which were important to the U.S. These regions were the United States, Great Britain, Germany and central Europe, the Soviet Union, and Japan. Since only one region was in hostile hands, Kennan's policy of containment was intended to ensure that no other regions fell into Soviet control. His rationale was that only by conquering some or all of these vital power centers could the Soviet Union, or any other challenger to the U.S., shift the balance of power in its favor. For Kennan, not all parts of the world were equally vital to American security (1951; Gaddis 1982, 25-88). Kennan strongly objected to the notion that the U.S. had to resist Communism everywhere. In particular, there was no need to contain the Soviets in the Third World since even substantial Soviet conquest would not alter the global balance of power.

An alternative way to prioritize America's global commitments is based on the nature of the emerging contenders' foreign commercial policy, not the strategic value of the locale. In differentiating among contenders, the United States could retreat from locales with rising liberal supporters (even in strategic regions and stand firm in regions with emerging imperial contenders (even in peripheral or less strategic areas). It should be stressed that in contrast to soft-line realists (who also differentiated across regions), in

²¹⁷ As well, election of an economy minded Republican Congress in 1946 resulted in the rapid decline in defense spending (\$81.6 billion in 1945 to 13.1 billion in 1947).

prioritizing commitments based on the nature of the emerging contender, the United States might retrench from vital locales, such as Europe, while standing firm in peripheral areas, depending upon the nature of the rising contenders. Soft-line realists would oppose this strategy because it might allow a single state to accumulate power that would dwarf American capabilities, even if the successor was a liberal hegemon.

The problem with the soft-line realist strategy of disengagement is that it ignores the dilemma of balancing capabilities and commitments. In particular, a declining U.S. had to consider both its political economy and its national security interests. In selecting to stand firm in regions with emerging liberal contenders, even in strategic locales, the United States risked eroding its fiscal strength through prolonging its military spending. Instead, in devolving hegemony to emerging liberal contenders, a declining United States could concentrate the freed up resources in its remaining commitments, safeguarding its fiscal strength, without strengthening the war-making capacity of a future rival.

In this context, one must ask why did the United States buildup Germany and Japan after World War II, accelerating their rate of ascent, but reject devolving regional hegemony to either state? In particular, did the United States intend for these states to be future regional successors? Finally, why did the U.S. reject devolution for a policy of accommodation of the Soviet Union (Nixon's *Détente*), and later a costly (and suboptimal) strategy of extraction under Carter and Reagan? Had the United States completely followed-through with this strategy of devolution, it would have protected its fiscal strength (and national security). Instead, the rapid decline of the Soviet Union saved it from eroding its political economy through excessive defense spending.

As a liberal hegemon, the United States established a liberal international commercial system. Coming on the heels of the great depression, many policy-makers feared a return to the depression, or at least economic crisis, following the end of World

War II (demobilization and reduced government spending would trigger unemployment). The danger was that a return to the beggar-thy-neighbor protectionist policies of the 1930s threatened America's fiscal strength (as LeFaber argues, the ghost of depression past and depression future shaped American foreign policy; 1991).²¹⁸ By creating liberalizing trade and monetary regimes (the Bretton Woods system established stable exchange rates, the International Monetary Fund, and the General Agreement on Trade and Tariffs or GATT, provided the economic basis for a freer trading system, emphasizing non-discrimination) the United States would ensure access to foreign markets for its surplus goods (LaFeber 1991a; Williams 1972). As a consequence, the United States opposed any state that espoused economic nationalism, exclusive trading practices, and autarky, fearing that a closed door arrangement would undermine America's political economy. Dependent on foreign markets and overseas investment opportunities as an outlet for its domestic production, the United States feared that the loss of access to markets and resources to all would have a detrimental effect on its economy.

In the aftermath of World War II, the United States rebuilt the economies of Germany and Japan, accelerating their rate of ascent. The United States transferred huge resources through the Marshall Plan, bilateral trade discrimination, and military rearmament programs. In the Far East, originally China (under Chiang Kai-shek), not Japan was viewed as the cornerstone to stability in the Far East.²¹⁹ However, by 1948, the United States had built-up Japan as the cornerstone of U.S. containment policy in the Far East, and part of a larger "crescent" of American security arrangement stretching to Iran

²¹⁸ Having an advanced economy, the United States could compete with less efficient producers in an open market competition.

²¹⁹ Asia firsters such as MacArthur argued that Asia, not Europe, had become the decisive theater of operation in the Cold War.

and in 1951 signed a security pact with Japan (Leffler 1984; Schaller 1982, 1985). The U.S. occupation of Japan served this purpose in two ways, (1) militarily, the creation of permanent American bases served as a possible staging ground for U.S. intervention in East Asia and as a constant threat of a second front in a war with the Soviet Union, (2) economically, Japan's industrial expansion served to integrate the Far East into the western economic order and to energize the sagging global economy.

In the case of Germany, beginning in 1946, the United States moved quickly to revive Germany in order to serve as the engine for Europe's recovery.²²⁰ Truman used the Marshall Plan to prevent a collapse of the European (and American) economy. In 1950, following the Korean outbreak, the United States initiated German rearmament. As part of this agreement, four to six American divisions were placed in Europe (to serve as a tripwire against Soviet invasion and to calm Western European fears of German rearmament). In 1955, the German army entered NATO.

By the 1970s, the United States was suffering from military and economic overstretch due to the costs associated with hegemony. Militarily, the United States was

²²⁰ In Britain, the business community embraced protectionism, favoring the advantages of the preference system over the uncertain advantages of freer trade. However, the United States opposed Britain's imperial preference system created at the Ottawa Conference (1932). During the war, through Article VII of the Lend-Lease Agreement and the Atlantic Charter, Britain pledged to dismantle the discriminatory commercial aspects of the imperial preference system. After the war, the United States made its aid conditional upon the acceptance of the open door principle. The Anglo-American Financial Agreement (1945) extracted a number of painful concessions from the British, including British commitment to end the sterling area dollar pool and quantitative import controls on American goods. In addition, Britain was required to restore sterling convertibility in mid-1947, allowing countries enjoying export surpluses with the UK to exchange sterling for scarce dollars. In return Britain received a low-interest 3.75 billion loan. A devastated England had no choice but to retreat from its imperial preference system.

In becoming a liberal contender, the United States encouraged Britain to retain its empire to defray costs for the United States. This accounts for why Britain did not fall further from the ranks of the great powers following World War II. One can speculate that had Britain remained an imperial power, the United States would have viewed it as a challenger, and not encouraged it to reclaim its overseas empire.

France received the same treatment from the United States. De Gaulle fought American calls for decolonization. In 1945, de Gaulle received a billion dollar loans from the United States in exchange for his promise to curtail government subsidies and currency manipulation which had give advantages to its exporters in the world markets (LaFeber 1991a).

committed in all parts of the globe. In order to fight on several fronts simultaneously (core and periphery), the United States maintained a two-and-a-half war standard used since the Kennedy administration to calculate conventional force requirements. Despite massive military spending, the United States acknowledged Moscow as an equal in nuclear capabilities (Soviet naval buildup further extended the rivalry into the periphery). Economically, declining American relative competitiveness and productivity contributed to Japan and Germany's encroachment (they had overtaken the Soviet Union).²²¹ American Presidents since Eisenhower gave little consideration to the fiscal consequences of a strategy of extraction for increased defense spending abroad (and increased entitlement programs at home; Friedberg 1989a). Consequently, the United States confronted a fragile economy, resulting in the collapse of the Bretton Woods system (ending the fixed exchange rate system based on the dollar for a floating system), high inflation and an overvalued dollar which undermined American exports and contributed to a growing trade deficit (U.S. ran its first trade deficit in 1971 since 1883), and a growing budget deficit due to increased spending on guns and butter (the U.S. paid for the war in Vietnam through deficit financing, unwilling to increase taxes).

Nixon's response to restore the balance was a mixed strategy of devolution (Nixon Doctrine) and accommodation of the Soviet Union (détente) in order to lower the costs of hegemony. The Nixon-Kissinger approach reflected an unwillingness to assume the sole responsibility for securing global equilibrium. Nixon wrote in 1968 that "no country can act wisely simultaneously in every part of the globe at every moment of time" (Gaddis 1982, 279). One of Kissinger's earliest priorities was to shift official thinking from

²²¹ Calleo argues that in the 1960s, the United States shifted the cost of Vietnam and the Great Society programs to its allies (1982).

"superiority" to "sufficiency," recognizing that the quest for global superiority would be costly and self-defeating.

The ideas of Kennan and Lippmann were embraced in the Nixon Doctrine. In a statement delivered in Guam in July, 1969, Nixon called for the United States to retreat from the Third World while reaffirming the primacy of Western Europe and Japan. In the core regions, U.S. allies would carry more of the burden of their defense, while the U.S. would maintain its presence of troops as well as its nuclear umbrella. In the Third World, Nixon argued that if a country cannot save itself with American economic and military support, American troops will not be able to save it at an acceptable cost. As part of a strategy of devolution, Nixon called for the buildup of regional surrogates in the periphery, hastening America's retreat, further reducing the costs of hegemony. The Nixon Doctrine meant that the United States would rely on regional powers for the maintenance of regional stability, supporting them with military and economic assistance. Kissinger generalized "that the U.S. will participate in the defense and development of allies and friends, but that America cannot-and will not-conceive all the plans, design all the programs, execute all the decisions and undertake all the defense of the free nations of the world.

Broadly, the Nixon Doctrine built-up a number of regional surrogates in the periphery (Osgood 1973). Vietnamization involved the building up of South Vietnam's army so it could replace the departing American troops. Other regional surrogates included Zaire, Angola, Iran, and Israel (Organski 1990; LaFeber 1991). In Europe, Nixon and Kissinger favored a united but independent Europe. Unlike most Atlanticists in the Kennedy and Johnson administrations, Nixon had sympathized with General De Gaulle's insistence on achieving unity by reconciling the sovereign interests of European states, rather than by subordinating them to an integrationist "grand design" devised in

Washington (Gaddis 1983). One "trilateral" institution intended to augment the role of Germany and Japan on the world stage was the G-7 summits.²²² By stressing their economic strength, Japan and Western Europe could play a role in the world out of proportion of their military power. However, Nixon never called for complete U.S. withdrawal from either locale.

Simultaneously, the Nixon administration pursued a strategy of accommodation with the Soviets, known as *détente*. The purpose of *détente* was to slow down the Soviet Union's rate of military ascent. Through arms control agreements with the Russians, Washington would constrain Soviet military buildup, without significantly restricting measures the U.S. might take in the future to upgrade its own capabilities. Through extension of Most Favored Nation (MFN), Export-Import Bank credits, and a policy known as "linkage," Nixon and Kissinger tried to integrate the Soviet economy with that of the West to such an extent that the Russians would have few motives for upsetting the international status quo. However, Nixon and Kissinger failed to see the degree to which the Russians would stretch the limits of the Strategic Arms Limitation Talks (SALT) (Gaddis 1982, 325). In particular, Soviet decision-makers were unlikely to respect any agreement that condemned them to a permanent position of inferiority in the locale. Consequently, the Soviet Union shifted their emphasis from quantitative to qualitative improvements, including the deployment of their own MIRVs, and building a new generation of heavy ICBMs.

Why was the United States unwilling to devolve leadership over Europe and/or the Far East to Germany and/or Japan? In particular, the Nixon Doctrine was intended to narrow the growing gap between capabilities and commitments, but it targeted the wrong

²²² The Trilateral Commission was founded in 1973 by David Rockefeller and Zbigniew Brzezinski. Its purpose was to broaden an existing "Atlanticist" consistency to include Japan.

countries. Instead of retrenching in peripheral regions, the United States should have devolved greater hegemony to Europe and Japan. In other words, Nixon's trilateralism did not go far enough (as Wallerstein argues, it was meant to preserve U.S. hegemony despite America's weakening base in the 1970s; 1993). In devolving hegemony to liberal contenders, the United States would have retained access to its commercial interests in the locales, without any of the costs associated with hegemony. These resources could have been concentrated in its remaining commitments and/or invested at home as a peace dividend, without strengthening the war-making capacity of future rivals. There are several explanations why the United States rejected this foreign policy option for alternatives which risked accelerating America's fall from the ranks of the great powers. These include the fear that devolution would erode America's reputation/credibility to defend its remaining commitments, encouraging Europe/Japan to bandwagon with the Soviet threat, and the fear that burden sharing implies "influence sharing" and a relatively diminished position in international affairs for the U.S.

The Carter administration rejected devolution, returning to a policy of extraction (and global containment). President Carter's increased military spending was the beginning of a massive military spending program undertaken by the Reagan administration. In 1980, the Carter Doctrine called for full U.S. intervention in the Persian Gulf if the Soviets threatened Western interests in the region. Carter's National Security Adviser, Zbigniew Brzezinski wanted to use the Soviet invasion of Afghanistan to implement earlier plans for a new American led security framework and military presence in the Persian Gulf-Middle East region. According to some scholars, such as Melvyn Leffler, the Carter Doctrine's intent was similar to the Truman Doctrine's (1983). As a policy of global containment, both doctrines projected American interests everywhere, calling for the defense of American commitments, even in areas of

peripheral interest and strategic value. Like the Truman Doctrine, once American interests were defined in global terms, a gap emerged between interests/commitments and capabilities, requiring a massive buildup at home and abroad (increased defense spending by 5 percent in real terms; LaFeber 1991a, 299). The consequence was indiscriminate and costly efforts to limit Soviet influence.

The Reagan administration greatly accelerated the defense buildup initiated by the Carter Administration, fully embracing the global containment of the Soviet Union everywhere (The Reagan Doctrine, 1985, called for rollback in the third world; where Carter called for 1.2 billion over five years, Reagan called for 1.6 billion; LaFeber 1991a, 303). According to Secretary of Defense Casper Weinberger, U.S. defense capabilities must be able to respond to direct and indirect Soviet aggression around the globe. In 1986, the U.S. arms budget approached 300 billion (the Soviets spent 250 billion). Weinberger called for the United States to prepare to fight 3 1/2 wars around the globe (Nixon prepared for 1 1/2 wars, down from 2 1/2).

Ronald Reagan contends that "peace through strength" forced the Soviet Union to increase their military spending, contributing to the collapse of the Soviet Union and the break of its empire.²²³ However, like Spain in the 1640s and even the Soviet Union during the Cold War, Reagan's military expenditure risked undermining America's fiscal strength. In the late 1980s, as the U.S. arms budget approached \$300 billion (1986), its trade deficits hit record highs (\$171 billion) and the United States became the world's largest debtor. In absorbing more than half of all national savings, government spending contributed to rising interest rates and "crowded out" domestic investment, eroding its undisputed preeminence in technology, manufacturing, and finance (Gilpin 1987). The

²²³ There is an interesting debate on this point. On the left, it is argued that America's military buildup accelerated its own relative decline. On the right, it is argued that America's military buildup forced Moscow to increase its rate of military spending, contributing to the economic collapse of the Soviet Union.

consequence of this decreased accumulation was lower productivity and an accelerated deindustrialization of the American economy.

In summary, by the 1970s, the United States confronted different emerging contenders for regional hegemony in disparate parts of its empire. While the United States initially selected a strategy of devolution and accommodation, it ultimately chose a policy of extraction. In selecting a strategy of extraction, the United States accelerated its rate of decline in relation to its alternative foreign policy option of devolution. In favoring its national security over its political economy, had the Cold War continued, the United States risked eroding its fiscal strength through prolonged military spending.²²⁴

Coming Decades

In the late 1980s, American policy-makers and scholars were greatly concerned about the decline of the United States and its loss of global primacy. America's decline even became an issue in the 1988 presidential campaign. However, only a few years later, with the collapse of the Soviet Union, many spoke of America's economic renewal and the emergence of a unipolar world. Yet, the underlying fiscal and security problems persist. In the coming decades, with the diffusion of power, rising contenders such as Germany (or a united Europe), China, Japan, Russia, and perhaps India and Brazil, will increase the cost for the United States of leadership over Europe, Asia, Central and Latin America, and the Middle East. There is currently a debate in the United States among scholars and policy-makers on how to narrow the growing gap between America's military capabilities and its global commitments.²²⁵ Some policy-makers argue that the

²²⁴ On this point, compare Kennedy (1987); Calleo (1982); and Huntington (1988).

²²⁵ On whether the U.S. should retreat from Europe and especially from NATO, and whether the Third World "matters" for U.S. national security, see Johnson (1985/86); Layne (1988); David (1989); Van Evera (1989); Desch (1989); Valeries Hudson, Robert Ford, David Pack, and Erik Giordano (1991).

United States is currently overstretched and needs to reduce its global commitments, especially in Europe (NATO) and Asia. They fear that prolonged increases in societal resource extraction to keep pace with the military spending of several rising contenders will erode its fiscal strength (i.e., productive base) and ultimately its military capability. In contrast, others argue that the United States is currently undertaxed and can bear the increased government expenditure needed to raise the military budget. Maintaining America's global commitments without increasing its rate of defense spending will weaken its relative military power, tempting rising competitors to challenge it for regional hegemony. Finally, a third group argues that the United States should abandon its global role, focusing on its own domestic woes, including increasing American saving rates, encouraging domestic investment, promoting commercial research and development, better training for its work force, tax incentives (reduction in capital gains taxes for long term investments), lowering interests rates, reducing the federal debt and deficit, (by reducing entitlement programs and defense spending), and lowering the trade debt.

The dilemma for the United States is how to restore the balance between its capabilities and commitments while safeguarding its economic staying power and its national security objectives. A foreign policy strategy that favors either fiscal or security concerns to the exclusion of the other will accelerate its fall from the ranks of the great powers. Based on the experience of previous hegemon, the lessons for the United States in the coming decades are several-fold. (1) First, in managing its decline, the United States must consider both its political economy and its national security interests. For the United States, as a liberal hegemon, failure to reduce its global commitments when it has the opportunity, even in strategic locales, means that it risks eroding its fiscal strength by prolonging its military spending, and ultimately its military power. This risk is especially

relevant for the debate on NATO's eastward expansion. (2) Second, as the United States becomes less competitive (or as other states continue to encroach on its lead), there will be domestic pressures to adopt an imperial foreign commercial policy. Protectionists will argue that an imperial commercial policy will slow-down and perhaps even reverse America's rate of decline. However, the danger of an imperial strategy is that it will restrict America's options for managing its decline, accelerating its fall from the ranks of the great powers.

Declining from undisputed leader to confronting emerging competitors for regional leadership, the United States will have three alternative foreign policy strategies for restoring the balance between its capabilities and commitments. The first strategy is to increase its military capability by extracting or mobilizing domestic resources. Increased military expenditure can be used to deter emerging contenders, and in the event that deterrence fails, to launch preventive wars destroying or weakening the rising competitors while the United States still has the military advantage in the locale. Second, the United States can reach an accommodation with some or all of the rising contenders. A strategy of accommodation involves concessions and compromises (such as arms limitation agreements) by both the rising and declining states. The intention is to slow down the emerging contenders' economic/military ascent so that the United States can defend its global commitments with its existing rate of resource extraction. Finally, the United States can devolve regional hegemony to an emerging contender in order to reduce its global commitments. Under this condition, the United States will not bear any of the political, economic, or military costs of regional hegemony. Thus, while a strategy of extraction restores the balance by increasing America's military capability, both a strategy of accommodation and devolution restore the balance by lowering the costs of hegemony.

Both a strategy of extraction and accommodation will accelerate America's fall from the ranks of the great powers over its alternative option of devolution. In accommodating some or all of the rising challengers the United States risks eroding its national security. First, decision-makers in a rising contender are likely to cheat on any agreement which condemns them to a permanent position of inferiority, leaving the U.S. with insufficient capabilities to defend its imperial commitments, and ultimately weak and vulnerable to attack everywhere (a challenger might agree to such an accord in the short term in order to buy time to buildup its forces without the threat of a preventive attack). Second, accommodation might signal the U.S.' weakness, encouraging other rising states to challenge its leadership position or damage its credibility to defend its remaining foreign commitments.

Alternatively, in increasing its rate of societal resource extraction in preparation for a preventive war against several rising states, the United States risks undermining its fiscal strength. First, excessive and sustained peacetime defense spending will divert resources from domestic investment, limit the scope of future economic growth, and ultimately weaken the productive strength of the U.S. to construct and maintain a modern military to defend its global commitments. Second, prolonged peacetime defense spending will drain the America's war chest, which it will need to mobilize during wartime.

A strategy of devolution of regional leadership will allow the United States to remain in the ranks of the great powers longer than its alternative options (and longer than imperial hegemonies). The rationale is that devolution will safeguard America's fiscal strength and its national security interests. As a liberal hegemon (a powerful state that will create and maintain a liberal economic arrangement), the United States can differentiate among emerging liberal and imperial contenders for regional hegemony (an

emerging liberal contender is a state that prefers a liberal regional commercial order and an emerging imperial contender is a state that will create its own mercantilist position in the region, whether it is currently an open or closed door regional order). In viewing liberal contenders as future allies (and potential regional successors) and imperial contenders as future adversaries, the United States can devolve hegemony in regions with emerging liberal contenders, such as Europe and perhaps the Far East (Japan), rather than discouraging these rising contenders, while standing firm in regions with rising imperial challengers such as the Middle East.²²⁶ In devolving hegemony, the United States can, (1) defend its remaining global commitments while further cutting its rate of resource extraction for defense; (2) retain access to its traditional interests in the locale without the economic, military, and political costs associated with regional hegemony. In both instances the United States can concentrate these freed-up military and foreign-policy resources in its remaining commitments (enabling the United States to implement the "Bottom-Up Review" which calls for fighting two major regional wars nearly simultaneously) or invest this peace dividend at home. However, failure to retrench when the United States has the opportunity, even in strategic locales such as Europe or the Far East, means that America risks undermining its fiscal staying power by prolonging

²²⁶ There is wide disagreement on Japan's future role and on America's willingness to let it assume hegemony (Gilpin 1989; Sakamoto 1989). Rosecrance and Taw (1990) note that Japan has taken on some hegemonic functions, such as a leading creditor, and anticipate that Japan will assume the role of hegemon. In contrast, Huntington argues that "Japan has neither the size, natural resources, military strength, diplomatic affiliates nor, most important, the ideological appeal to be a twentieth century superpower" (1988, 92). Taira (1991) argues that Japan is unwilling to assume hegemony, while Rapkin (1990) argues that there are domestic and foreign constraints on its ability to do so. According to Rapkin, one foreign constraint includes the United States, which has resisted Japan's military ascendancy (also see the Pentagon's 1992 Defense Planning Guidance for 1994-99, *New York Times*, 8 March 1992).

In Europe, there are similar debates on the future of America's commitment to the region. While Van Evera (1989) and Walt (1989) emphasize the primacy of Europe, Calleo argues that the United States should "assume the role of ally rather than of hegemonic protector managing Europe's defense" (1989, 20). This would involve some combination of European nuclear forces and larger number of conventional forces. He concludes that Europeans have not taken on this role because the U.S. has been willing to do so. Wallerstein argues that America's real interest in continuing NATO is to prevent France and Germany from creating a European army, which would reduce U.S. influence in the region (1993).

excessive military spending. Thus, in making itself more secure, the United States cannot ignore the fiscal consequences of managing decline.

This strategy for managing decline contradicts the expectations of realism. According to realists (and the Pentagon's 1992 Defense Planning Guidance for Fiscal Years 1994-1999), the United States should retain the bulk of its global commitments, trimming them only in the periphery. The underlying assumptions are two-fold, (1) since today's ally might be tomorrow's enemy, the United States must remain in strategic locales in order to discourage its allies, especially Germany and Japan, from developing their own defense capabilities or assuming regional hegemony; (2) losses or gains in the Third World will not upset the global balance of power. However, the realist strategy of managing decline focuses exclusively on national security concerns, ignoring the fiscal consequences of balancing capabilities and commitments. In particular, in retaining its global empire the United States risks eroding its long run economic staying power through excessive and prolonged defense spending (while insufficient defense spending will threaten its national security by tempting rising contenders to challenge America's regional hegemony everywhere). Thus, in contrast to the realists and the Pentagon, the best strategy for the United States to manage its decline might include retrenching in more valuable locales, while standing firm in less strategic areas.

Just as important are the linkages between economic and security policies. Recent calls for the United States to adopt a protectionist economic policy will hasten America's relative decline rather than slow it down or reverse it (i.e., on the left by organized labor and the right by isolationists such as Pat Buchanan). As an imperial hegemon, the United States will impose an exclusive economic order in any region it dominates, preferring a commercial policy of economic self-sufficiency or economic autarky (and excluding more efficient producers). In viewing all emerging contenders (both liberal and imperial)

as threats to its national interests, the United States will restrict its range of security strategies for restoring the balancing between capabilities and commitments to either a security strategy of accommodation or increased resource extraction. An imperial U.S. will reject a strategy of devolution since it will undermine its national security by strengthening the war-making capacity of a future rival. However, in the long run, both extraction and accommodation will accelerate the United States' fall from the ranks of the great powers due to either excessive defense spending, accommodating an incompatible rising challenger, or insufficient defense spending. In contrast, as a liberal hegemon, the U.S. can differentiate between emerging contenders, including among its range of foreign policy options the strategy of devolution. In the long run, in devolving hegemony, the United States can safeguard its fiscal strength and its national security interests, remaining a key player in the great power game longer than any of its alternative security options and longer than as an imperial hegemon.

APPENDIX

By administrative custom, the Treasury is responsible for ensuring that government revenues and expenditures are balanced.²²⁷ The Treasury controls government expenditure through a process known as "Treasury control." According to this historical precedent, the Exchequer must approve any changes or increases in a department's expenditure for the ensuing year (known as Votes). No piece of legislation calling for increased expenditure can proceed to Parliament until a Treasury Minister has consented. The intention of this oversight is to ensure that a department's estimate is both economical and sufficient.

By December of each year every department prepares detailed estimates of proposed expenditure for the following year. The Estimates fall into four categories: Navy, Army and Ordnance, Civil Service, and Revenue Department (Customs and Excise, Inland Revenue, and Post Office) (later Air Force Estimates were added). A department's Estimates are divided into Votes, representing different aspects of its budget. For instance, in the Admiralty's Vote 1 covered wages, Vote 2 covered clothing. New expenditure and variations in the scope of existing services leading to increased expenditure must be submitted separately to the Treasury for approval. Subsequent increases in the original Estimates are submitted by means of Supplementary Estimates, which must also be approved by the Treasury.

²²⁷ This discussion is based on Peden (1979a); Beer (1956); Bridges (1964); Heath (1927); Roseveare (1969); French (1982); Burton (1966).

Intense argument and consultation often occurs between the Treasury and the Departments over Estimates. It is not uncommon for the Treasury to modify the Estimates either by addition or by reduction. The Chancellor can criticize a department's proposal either on the ground that finance was not available or on the merits of the proposals themselves. While Treasury control could be used by the Exchequer to hinder individual items, lacking a technical knowledge (especially for military matters), the preferred method of exercising control is to set overall financial limits, allowing individual departments to prioritize their programs. In the event the Chancellor and the minister responsible for a department are unable to agree to a limit to that department's expenditure, the matter is referred to the Cabinet for arbitration.

Once estimates are approved by the Treasury, they are sent to the House of Commons. Estimates are discussed in the Committee of Supply (consisting of the entire house) and agreed to by the whole House. Each Vote can be discussed at length in the Supply Committee, and any item in the Vote can be rejected or reduced, but the House of Commons can not add to the vote. However, as Peden notes, "Defence expenditure always required Cabinet approval in principle and Treasury approval in detail" (1979, 15). Since all proposals included in the estimates cannot be reviewed before the estimates were submitted to the Supply Committee, the Treasury reserves the right for further consideration, and if the Treasury later finds that it cannot approve these proposals, the money allocated to cover them can not be spent. In addition, savings on Votes can be transferred to meet excesses on another vote only with the approval of the Treasury (known as virement). Finally, to exceed its Estimates for the current year (new commitments not approved in time for inclusion in the original Estimates or increases in costs which have arisen since the original Estimates were accepted), a department must

submit to the Treasury a Supplementary Estimate which is submitted to Parliament for approval.

There are slight differences between the Civil Estimates and the Service Estimates (Navy, Army and Ordnance, Airforce), which grant the latter certain advantages (see Heath, 1927).²²⁸ First, the Admiralty and the War Office have large financial Departments of their own. Lacking technical knowledge of the development and production of new weapons, when the approximate total figures of expenditure are agreed for each service, the *Board of Admiralty* and the *Army Council* settle their detailed programs accordingly. In practice, the consequence is that the Treasury departmental examination is less scrutinizing than in the case of Civil Estimates. Second, the estimates by Civil and Revenue Departments are presented to the House of Commons by the Treasury, while Estimates of the Services are presented to the House of Commons by the Admiralty and War Office.

²²⁸ Since there was no over-arching Department of Defense (Ministry of Defense), each service minister prepared an annual Estimate of their expenditure (inter-service coordination was handled by the Committee on Imperial Defense, or C.I.D.).

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