The Invisible Hand of Peace

Capitalism, The War Machine, and International Relations Theory

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American Grand Strategy and the Liberal Peace

The United States has a long history of responding to strategic challenges and opportunities by promoting the spread of its own political and economic institutions abroad. Rooted firmly in a political culture defined by its attachment to individual freedom, this penchant often manifests itself in foreign policies supporting democratic transitions and economic liberalization around the world. Democracy and trade are trumpeted for two key reasons: states that possess liberal political and economic institutions do not go to war with each other, and they also tend to share common national interests. As democracy and commerce proliferate around the world, the United States should face fewer enemies while cultivating more political allies.

Many American political leaders over the past two centuries have reaffirmed these principles. Outlining the benefits of annexing Texas in his inaugural address, President Polk (1845) noted, "Foreign Powers do not seem to appreciate the true character of our Government... To enlarge its limits is to extend the dominions of peace over additional territories and increasing millions... While the Chief Magistrate and the popular branch of Congress are elected for short terms by the suffrages of those millions who must in their own persons bear all the burdens and miseries of war, our Government can not be otherwise than pacific." At the Paris Peace Conference of 1919, Woodrow Wilson launched a bold and revolutionary plan to end balance-of-power politics that seemed to lead to war by creating a democratic global political order. Secretary of State Cordell Hull championed free trade in the 1930s as a device to remove the economic causes of conflict that he saw emerging as states shifted toward protectionism in Europe. The Truman administration implemented the Marshall Plan to foster economic recovery and strengthen democracy while preventing the spread of
communism in Western Europe in the larger emerging struggle with the former Soviet Union.

This proclivity to foster the expansion of America's own political and economic institutions has only been strengthened following the implosion of the Soviet Union, which left the United States as the sole superpower in the world. Just as the American triumph over Germany and Japan created an opportunity for presidents Roosevelt and Truman to promote American interests by transforming these political systems into liberal democracies, the collapse of the Soviet Union in 1991 created another opportunity to foster the development of liberal institutions around the world. Referring to American encouragement of democratization, President Clinton's National Security Advisor Anthony Lake (1993) announced that American strategy would shift from "containment to democratic enlargement" in the wake of the Soviet collapse. Clinton defended this policy in his 1994 State of the Union address by evoking the absence of war among democracies. He stated, "Ultimately, the best strategy to ensure our security and to build a durable peace is to support the advance of democracy elsewhere. Democracies don't attack each other."

The peaceful Soviet collapse stands out as more than a chapter in the centuries-old conflict among great powers for global influence that offered another strategic opportunity for the United States to promote liberal institutions. It also marked a watershed in the struggle between governments and decentralized markets to shape the daily choices of individuals and social behavior. The collapse of the Soviet Union emphatically symbolized the defeat of socialism and political authority as a device to control economic activity. This triumph constitutes part of what Francis Fukuyama (1992) has labeled the "End of History" in which no viable alternative economic order exists besides that of free market capitalism. Similarly, Thomas Friedman (2005) describes the fall of the Berlin Wall on November 9, 1989, as the revolution of 11/9 that flattened the world by redistributing power so that economic decision making is driven by the wants of billions of individuals around the world rather than small numbers of political officials in central planning bureaucracies. Propelled by the economic revolutions of Ronald Reagan, Margaret Thatcher, and Deng Xiaoping, governments around the world have increasingly adopted neoliberal economic policies privatizing domestic industry, cutting trade barriers that insulate domestic firms from international competition, eliminating domestic price controls, and substantially reducing the size of Keynesian fiscal outlays.
This book seeks to understand what implications these historic developments in the organization of economic activity have for stability in the international system. When the ability of governments to manipulate the forces of globalization is limited and markets play a large role in the coordination of social behavior, is the international system marked by more or less military conflict among states? Do the domestic institutions often associated with free market capitalism, namely private property and competitive market structures, cause peace?

These questions carry enormous implications for American grand strategy. The attacks on September 11, 2001 (9/11), motivated President George W. Bush to strengthen the American commitment to the liberal vision of transformation, particularly in the nascent struggle with Islamic fundamentalism. His administration made political reform a centerpiece of his strategy to remake the Middle East. In his 2004 State of the Union address, Bush declared, “As long as the Middle East remains a place of tyranny and despair and anger, it will continue to produce men and movements that threaten the safety of America and our friends. So America is pursuing a forward strategy of freedom in the Middle East... We have no desire to dominate, no ambitions of empire. Our aim is a democratic peace.”

Economic reform has more quietly been made the junior partner supporting the cause of liberty in the Middle East. Bush has argued that trade indirectly promotes peace by encouraging individual liberty. In a statement outlining a proposal for a free trade zone with the Middle East, President Bush (2003) observed, “Over time, the expansion of liberty throughout the world is the best guarantee of security throughout the world. Freedom is the way to peace... Across the globe, free markets and trade have helped defeat poverty, and taught men and women the habits of liberty. So I propose the establishment of a U.S.–Middle East free trade area within a decade, to bring the Middle East into an expanding circle of opportunity, to provide hope for the people who live in that region.” Similarly, U.S. Trade Representative Robert Zoellick chided domestic proponents of protectionism for ignoring the capacity of globalization to strengthen the forces of reform and tolerance in the Middle East. He wrote in 2004, “Economic isolationists are too shortsighted to see the full mosaic of America's interests. Their fight to defeat such trade agreements would rob the United States of one of its most powerful tools, just when we should be integrating trade and economic reforms with the struggle for democracy and tolerance that is vital to our security.”

Such references to the social virtues of markets often elicit rejoinders from those who see capitalism not for its capacity to promote economic
opportunity and peace but instead for its tendency to concentrate wealth and expand, often rapaciously, from the economic centers of the developed world. If unfettered markets raised living standards in Western societies and stimulated the fall of the Berlin Wall, they have also left many developing societies trapped in poverty and subject to the demands of a global class of capitalists and their political representatives, like the United States and the International Monetary Fund. Rather than diffusing peacefully throughout the world, the beneficiaries of capitalism have often relied on the sword to secure raw materials and outlets for surplus goods in Latin America, Africa, and the Middle East. If international trade promoted reconciliation between France and Germany during the Cold War, then it also stimulated American intervention in places like Iran, Chile, and Guatemala. Along these lines, current American attempts to transform the Middle East are not viewed for their self-proclaimed goals of promoting freedom and liberty but are instead seen as a device to secure stable access to oil. Contemporary skepticism over the benevolent effects of commerce is reinforced by the legacy of the first era of globalization, which ended in 1914. Even without accepting Leninist arguments tracing the origins of World War I to competition among European powers over the rapidly dwindling supply of colonial outlets for surplus capital, the decisions for war in July 1914 suggest that globalization failed in its most crucial test to prevent war.

REVISING THE FOUNDATIONS OF THE LIBERAL PEACE

This book challenges the intellectual foundations of a series of academic findings, known collectively as the liberal peace, which are intimately tied to this broader national debate over American foreign policy. Perhaps the most prominent in international relations theory over the past two decades, this contemporary research program has utilized insights from such classical scholars as Adam Smith, Baron de Montesquieu, Immanuel Kant, Joseph Schumpeter, and Richard Cobden to refine and affirm two

1 For a recent examination of this tension associated with market development see James (2006).
2 For example, John M. Owen (2005, p. 122) writes of their intimate connection with the policies of George W. Bush: "... [F]ew other presidents – certainly none since Woodrow Wilson, a former president of the American Political Science Association... – have tied their foreign policies more explicitly to the work of social science. The defining act of Bush's presidency was grounded in a theory that the political scientist Jack Levy once declared was 'as close as anything we have to an empirical law in international relations,' namely that democracies do not fight each other."
critical propositions. First, democratic states have created a zone of peace among themselves. Second, high levels of international commerce between states create similar effects, raising the costs of military conflict to unacceptable levels for modern economies.

The relationships among democracy, international trade, and peace are more tenuous than previously thought. The capacity of democracy to promote peace is much weaker than this literature has yet to acknowledge. In addition, the capacity of commerce to constrain war is much stronger than this literature has yet to acknowledge. However, these pacific effects generated by trade depend critically on the presence of liberal economic institutions. I utilize the question of whether market-promoting institutions limit war to advance two central claims. First, liberal economic institutions — namely, the predominance of private property and competitive market structures within domestic economies — promote peace. Second, this liberal economic peace has historically been much stronger than the liberal democratic peace frequently cited by both scholars and policymakers. Together these claims carry important implications for contemporary debates over American grand strategy. They challenge the conventional wisdom about the national security benefits provided from democracy promotion and suggest instead that economic liberalization offers a more robust path to peace.

Democracy and Peace?

The democratic peace debate has extensively studied how regular and competitive elections can empower society to constrain abuses of political authority and generate peace among states. These claims linking democracy to peace generally take one of two forms. The first, which has garnered more

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3 A third finding linking membership in international organizations to peace has received increasing attention. The arguments made here possess fewer implications for this research. For important contributions to this debate, see Oneal, Russett, and Davis (1998), Mansfield, Pevehouse, and Bearce (1999/2000), Mansfield and Pevehouse (2000), Russett and Oneal (2001), Bearce (2003), Boehmer, Gartzke, and Nordstrom (2004), Pevehouse and Russett (2006), and Haftel (2007).


5 There also is a third version of the democratic peace hypothesis that examines how the number of democracies in the international system shapes the aggregate conflict outcomes in the system. For examples of this research see Gleditsch and Hegre (1997), Mitchell et al. (1999), and Gleditsch (2002).
empirical support, is known as the dyadic democratic peace proposition. It restricts the capacity of democracy to promote peace to pairs of democratic states. Democratic governments are only pacific when interacting with fellow democracies. A second hypothesis, known as the monadic version of the democratic peace hypothesis, drops this pairing restriction. It holds that the constraints on war imposed by democracy should operate in interactions with all types of regimes in the international system, democracies and autocracies alike.

Numerous theories have been offered to explain the empirical regularities linking democracy to peace. The literature has developed around three primary variants. Two rely on the institutional qualities of democracy; the third on the normative characteristics that tend to emerge from such regimes. The first institutional explanation points to such features as regular elections; the separation of powers among an executive, legislature, and judiciary; and the rule of law within democracies as sources of peace. The process of holding regular and competitive elections increases the political costs to a leader for going to war. When the segments of society that pay the real costs of war in terms of higher taxation and death in battle are granted the means to punish the government officials by removing them from office, states use force much more cautiously. Democratic states tend to win the wars they fight, suggesting that they only fight when they expect to win (Lake 1992; Bueno de Mesquita et al. 1999, 2003; Reiter and Stam 2002). A second institutional explanation highlights how democracy increases transparency and adjusts informational asymmetries in the bargaining process between states. These traits enhance the credibility of promises to avoid the use of military force made between democracies, reduce the dangers of cheating endemic to anarchy, and increase the probability of reaching a cooperative settlement to a dispute (Fearon 1994; Smith 1998; Schultz 2001; Lipson 2003).

A third set of explanations focuses on the normative aspects of democracy (e.g., Maoz and Russett 1993; Dixon 1994; Owen 1994, 1997a; Risse-Kappen 1996; Rousseau 2005). It argues that the political culture that evolves in democracies helps to promote peace. As the norms of

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conciliation, compromise, and reciprocity shape the resolution of conflicts within democracies, democratic leaders tend to adopt such procedures when negotiating with other democratic states. These norms help to facilitate peaceful dispute resolution.

Despite substantial empirical and theoretical progress, at least three important questions remain for the democratic peace research program. First, numerous scholars have pointed out that democracy, and the threat of electoral punishment in particular, often insufficiently constrains decisions for war (e.g., Gowa 1999; Mansfield and Snyder 1995, 2002a, b, 2005; Rosato 2003). For example, if a ruling political circle wishes to embrace aggressive foreign policies that heighten the risks of war, the choice to oppose such policies can be politically costly for both opposition politicians and members of society. Opposition leaders must weigh the likely consequences, both domestic and international, before going to war. If victory in war generates a policy success, opposition leaders run the risk of being cast as supporting foreign policy weakness by opposing war (Schultz 2001; Levy and Mabe 2004). Similarly, nonmyopic democratic leaders may be able to circumvent electoral constraints and attempt to check their authority by legislators. Given the costs of organizing opposition, active political opposition from society may fail to materialize as individuals choose to free-ride on the protests and threats of electoral punishment by fellow citizens (Gowa 1999). Mansfield and Snyder (2005) show that elected leaders can exploit appeals to nationalism when state institutions regulating political participation are weak, like in the early stages of a democratic transition, to pursue aggressive foreign policies. The failure of recently democratizing states to grant constitutional freedoms and civil liberties that help regulate political participation and constrain the policy outcomes produced by majoritarian institutions like elections casts doubt on their ability to join the “zone of peace” (Zakaria 1997, 2003). In part, these possibilities reflect the legacy of the French Revolution and the subsequent debate within liberal thought throughout the nineteenth century over the role played by nationalism in promoting or constraining individual liberty (Howard 1978). Even democratic leaders can exploit domestic institutional instability and public fears of insecurity to construct broad swaths of public support for war.

Second, an abundance of candidate explanations for the tendency of two democracies to avoid war with each other has failed to yield a consensus on which among these is best. New contributions in this research program have historically been motivated by this theoretical uncertainty. For example, Bueno de Mesquita et al. (1999, p. 791) write, “Although these observations
about democracy and war are part of an important pattern, they lack a coherent explanation. Several possibilities have been put forward, but none has gained broad acceptance.” Similarly, Lipson (2003, pp. 1–2) writes, “That is exactly the question about peace among democratic states. It works well in practice, but there is considerable confusion about how it works in theory. The lack of an answer is no joke, however. Despite extensive research, all we have is a remarkable correlation. We still lack a convincing explanation about why democracies do not fight each other.”

This lack of theoretical consensus is perhaps most damaging to the research program’s central claim when confronting a critical empirical limitation that challenges most existing theoretical explanations of the democratic peace. As will be discussed in Chapter 9, the peace among democratic states does not emerge until after World War I. In both monadic and dyadic research designs, autocrats rather than democrats were more pacific before World War I. This shift in the foreign policy behavior of democracies between the nineteenth and twentieth centuries creates at least two significant problems for most claims linking democracy to peace. The first is simply a new theoretical question that needs to be answered: Why were democratic regimes aggressive in the nineteenth century? The second related problem carries important theoretical implications for most of the existing explanations of a democratic peace because they do not specify that the constraints on war created by democracy are likely to vary over time. Consequently,

7 Although some segments of the democratic peace literature have acknowledged this extreme shift in the relationship between regime type and war, it remains relatively understudied. While arguing that the peace among democratic states does not emerge until the post–World War II era, Gowa (1999) presents some evidence that dyads possessing two democratic states were more likely to engage in low-level military disputes than all other dyads in the period prior to World War I. Cederman (2001) attributes this “initial democratic belligerence” in the nineteenth century to colonial competition among the United States, Britain, and France. Similarly, Blank (2000) argues that the decline of imperialism allowed the democratic peace to emerge after 1945. Although finding that democracy reduced the likelihood of military disputes from 1886 to 1939, Oneal and Russett (1999) and Russett and Oneal (2001) observe that these pacific effects are weaker in the period before World War I. In a sample of politically relevant dyads, they point to the emergence of a democratic peace around 1896 and suggest that a widespread expansion of suffrage occurring around the turn of the twentieth century may account for this shift. This date shifts to 1900 when all dyad are included in the sample.

8 Even time-variant explanations of the democratic peace (e.g., Mitchell et al. 1999, Cederman 2001) insufficiently address this empirical anomaly because they generally begin with the expectation of the null hypothesis positing no relationship between regime type and war. In other words, this hypothesis suggests that democrats were just as likely to go to war as autocrats were in the period before the democratic peace emerged. However, the results presented in Chapter 9 contradict this null finding. Instead, democratic regimes were more likely than autocratic ones to go to war before World War I.
if existing explanations are correct, democratic constraints on war should operate irrespective of the time period under investigation. This dramatic switching relationship between democracy and conflict after World War I thus contradicts most theories claiming that democracy promotes peace and stands out as a critical empirical anomaly yet to be explained.

Third, much of this research program has proceeded by making one of two assumptions. First, democratic institutions are assumed to be exogenous. Often reflected in assertions that political institutions are somehow more fundamental than other social institutions that regulate individual behaviour, this assumption necessarily points to the presence or absence of democracy as the best theoretical vehicle to understand the domestic causes of war and peace. Second, if democratic institutions are instead endogenous, or caused by some larger socioeconomic structure or development, it is assumed that any systematic source of variation in regime type does not simultaneously affect the conflict propensities of governments. The costs of such assumptions loom large in light of multiple claims within classical liberal thought and contemporary research suggesting that political freedom is nested within economic freedom. The emergence of democracy has long been traced to institutions and outcomes normally associated with liberal economic institutions, like respect for private property, the emergence of an educated middle class, and economic development (e.g., Smith 1937; Cobden 1868, 1870; Hayek 1994; Moore 1966; North and Weingast 1989; Pipes 1999; Przeworski et al. 2000; Lipset 1994; Boix 2003). For example, in one of the twentieth century’s classic works of liberal thought, The Road to Serfdom, F. A. Hayek writes, “If ‘capitalism’ means here a competitive system based on free disposal over private property, it is far more important to realize that only within this system is democracy possible” (1944 [1944], pp. 77–8). This possibility suggests that the peace observed among democratic states may be caused by their tendency to possess relatively liberal market institutions rather than their embrace of open political competition in elections.

Even if liberal economic institutions are not responsible for causing the observed peace among democratic states, do they play a larger role in limiting war among states? One of the most prominent contributions to the academic literature argues that a virtuous relationship exists among democracy, commerce, membership in international organizations, and peace, in which each of these traits reinforces the others (Russett and Oneal 2001).

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9 Weede (1995), Gartzke (1998), and Mousseau (2000), are exceptions to this.

10 For a similar critique see Thompson (1996).
Democracy not only promotes peace, it also increases commerce among states, which in turn promotes peace. More recent research critiquing the democratic peace suggests instead that the commercial peace created by capitalism or economic development is stronger than that of democracy (Mousseau 2000; Mousseau, Hegre, and O’Neal 2003; Gartzke, Li, and Boehmer 2001; Gartzke 2007).

The possibility that the democratic peace is weaker than the commercial peace carries important implications for both the central role played by democracy promotion in American grand strategy and for the repeated tendency in policy and academic debates to conflate political and economic freedom. Throughout the Cold War, the United States was cast as engaged in a Manichaean struggle with the totalitarian Soviet Union that controlled all aspects of the political and economic lives of its citizenry. The end of this bifurcation of the world into two vastly different and opposing camps has made it easier to recognize that states often make very different institutional choices with respect to their economic and political institutions. China, for example, stands out as a critical case in which its regime has chosen to sequence political and economic reforms, opting to embrace economic integration before political openness.

The Bush Doctrine suggests that democratic and economic reforms should complement each other, at least as devices to defend American interests around the world. However, a series of recent studies by Mansfield and Snyder (1995, 2002a, b, 2005) caution against overlooking the risks associated with utilizing democracy promotion as an instrument of foreign policy in places like Iraq. They present a wide range of evidence showing that the likelihood of military conflict increases during periods of democratic transition. Similar concerns have arisen in studies of civil war and ethnic conflict (Snyder 2000; Chua 2002). Whereas stable and mature democracies are unlikely to fight each other, the process of transforming an autocratic regime into a democratic regime may be a dangerous one marked by more and not less military strife. If democratization results in a short-term increase in military conflict, American grand strategy should perhaps focus on promoting liberty through markets instead. For example, this possibility suggests that the absence of democratic reform in China may not hinder the building of cooperative ties with the United States that are capable of smoothing any global power transition between the two. Exploring this possibility first necessitates examining whether and how liberal economic institutions have historically influenced decisions for war or peace among governments.
Commercial Liberalism

The commercial peace research program displays perhaps even more variation in explaining the long-hypothesized and more recently confirmed tendency for international commerce to promote peace between states. One segment of this literature focusing on international trade presents up to five potential mechanisms by which commerce promotes peace. The first has been labeled the opportunity cost or deterrence model. Because conflict or even the threat of it tends to disrupt normal trading patterns, potentially large economic costs will deter dependent states from using military force to solve their political conflicts (e.g., Polachek 1980; Russett and Oneal 2001). A second mechanism compares the relative costs of acquiring productive resources. As commerce grows, the incentives for plunder or conquest decrease simply because it is a more costly means of generating economic growth (Rosecrance 1986). Third, a sociological hypothesis concentrates on how trade helps to increase contact and communication across societies. By building a broader cosmopolitan identity across societies, trade enables common interests to emerge while displacing national loyalties and competitive relations among governments that generate military conflict (e.g., Deutsch et al. 1957). Fourth, drawing on bargaining models, some scholars argue that international commerce provides an important signaling mechanism that can help states achieve a negotiated compromise short of war during a crisis (e.g., Morrow 1999; Gartzke, Li, and Boehmer 2001; Reed 2003). A fifth segment focuses on how regional trading arrangements among states promote heightened trade levels and peace (Mansfield, Pevehouse, and Bearce 1999/2000; Mansfield and Pevehouse 2000; Bearce 2003; Haftel 2007).

A second strand of this research focuses instead on domestic economic attributes to explain the absence of military conflict. Mousseau (2000, 2005) and Mousseau, Hegre, and O’Neal (2003) point to the emergence of contractual norms within societies based on exchange as the link between markets and peace. Hegre (2000) claims instead that economic development conditions the relative value of commerce and conquest. Development raises the costs of conquest and increases the returns from international trade.11 Souva (2004) shows that the similarity of domestic economic institutions promotes peace. Defined by the absence of capital controls, common

11 Boehmer and Sobek (2005) find a curvilinear relationship between development and conflict. Extremely poor and wealthy states are both less warlike.
political interests, and economic development, Gartzke (2007) argues that capitalism reduces military conflict by reducing the incentives for conquest and by facilitating communication about resolve in diplomatic crises.

The commercial peace research program faces challenges like those that raise doubts about the capacity of democracy to limit war. Three stand out. They concern the historical capacity of trade to promote peace, the process by which trade causes states to adopt peaceful foreign policies, and the endogeneity question – namely whether the causes of trade also influence decisions for war and peace.

First, the commercial peace literature faces a different version of the historical inconsistency critique. Rather than being bypassed as in the democratic peace literature, it has served as a foundational argument for criticism of any claim that international commerce promotes peace. Even though substantial trading ties helped build cooperative political relationships in Europe following World War II, the abrupt end of a sustained era of globalization caused by the outbreak of World War I stands out as a glaring anomaly for any claim linking international commerce to peace. If substantial trading links failed then to prevent one of the defining military conflicts in human history, why should globalization be able to prevent war in the contemporary period? This empirical weakness looms larger than the single but important case of World War I. European and American competition for colonial markets in Africa, South America, and Asia at the end of the nineteenth century seems to confirm Marxist–Leninist claims associating capitalist development with imperialist expansion and war. These assertions linking international trade and capitalism with conflict in the nineteenth century survive in part because of the absence of systematic research examining the links between trade and conflict during this first era of globalization. The limited data on bilateral trade flows before 1950 have led much of the commercial peace literature to focus on empirical evidence after World War II to validate its claims. When scholars expand their analysis to include cases from the nineteenth century, data across the two periods are aggregated and potential differences between these eras of globalization are obscured.

13 Edward Mansfield and Brian M. Pollins (2003, p. 8) write, “Instead, large-N studies have focused almost exclusively on the past half century and have largely ignored whether and how the effect of interdependence have changed over time.”
14 Barbieri (1996), Oneal and Russett (1999), and Russett and Oneal (2001) examine samples between 1870 and 1939. However, all three studies aggregate data before and after World War I into a single sample.
Second, the mechanisms by which the economic interests of private individuals exposed to international markets get translated into public policies that support either war or peace remain understudied.\textsuperscript{15} For example, one classical hypothesis points to the natural division of resources among societies as generating a mutual need to establish cooperative trading relationships and peace.\textsuperscript{16} This claim associates international trade with the emergence of common interests among governments. Ricardo's principle of comparative advantage reinforces such a link by demonstrating that international trade tends to increase the aggregate income of all countries engaging in it. Accordingly, the economic gains from trade create a joint interest in peace by offering countries a strong material incentive to avoid the severed trading links that accompany war.\textsuperscript{17}

Standard trade theory that has moved beyond Ricardo's key insight illustrates the risks associated with focusing on macro-level propositions to understand how globalization promotes peace. The processes associated with integrating national markets into a single world economy generate intense conflicts within societies by altering the domestic distribution of income. For example, the Heckscher–Ohlin framework shows that trade increases the real income of owners of relatively abundant factors of production in an economy (Flam and Flanders 1991). At the same time, owners of scarce factors of production see their real incomes decline from globalization. This insight carries an important implication. Because international trade redistributes income within society, it simultaneously creates conflicting pressures for and against more open commercial policies. This domestic conflict implies that gains from trade accruing to an economy as a whole will not necessarily translate into uniform lobbying pressures from society for the promotion of trade and peace. Unless the domestic beneficiaries of trade

\textsuperscript{15} For examples of such critiques see Mansfield and Pollins (2001), Barbieri and Schneider (1999) and Schneider and Schulze (2003).

\textsuperscript{16} For a discussion of this variant and its classical roots, see Chapter 1 of Howard (1978).

\textsuperscript{17} Moreover, this straightforward proposition linking high levels of trade with peace is readily testable with the use of modern statistical techniques. Much of the contemporary commercial peace literature has adopted this very approach using broad claims rooted in classical liberal international relations theory to test whether aggregate economic outcomes, like heightened bilateral trade flows, reduce military conflict. More limited attention has been devoted to using alternative empirical techniques, like intense case studies, capable of discriminating among multiple commercial peace hypotheses and moving beyond broad propositions that neglect the process by which economic interests are translated through the domestic institutions to shape decisions for war or peace. For a similar critique see Ripsman and Blanchard (2003) and Rowe (2005).
also possess sufficient political clout to ensure that domestic markets stay open and military conflict is avoided, these uneven effects of globalization cast doubt on the classical insight that international trade always generates a common interest for peace among states. At the very least, these possibilities suggest that the domestic process by which the economic interests derived from international trade get translated into pacific foreign policies is crucial to understanding how globalization limits war. At the same time, the theoretical opportunity created by revising Ricardo’s basic insight necessitates additional empirical research – quantitative and qualitative alike – that moves beyond relying on such aggregate economic indicators like bilateral trade flows to confirm whether and how globalization limits military conflict between states.

Third, economists and political scientists have long recognized that trade flows expand between states for a variety of reasons, including technological innovations that drive down transportation costs, differences in relative factor endowments, and variation in domestic political institutions that influence the scope of regulatory barriers like tariffs. The source of expanding trade flows carries important consequences for the possibility of peaceful relations among states. For example, during the Cold War economic flows within the Soviet bloc were driven by very different mechanisms than those within the Western bloc. In the case of the former, hierarchical political relationships between the Soviet Union and its client states directed trade. In the case of the latter, international trade flows responded instead to the signals created by competitive markets. Today, surging worldwide demand for oil has made economic growth in many Middle Eastern countries completely dependent on a single global integrated market. However, like the conditions in Soviet bloc countries, production decisions and levels of trade in these economies are shaped by government agencies responsible for administering these public assets. Similarly, economic historians agree that the dramatic growth of international commercial flows during the first era of globalization was driven by technological innovations such as the railroad and steamship. Many states even responded to these declining transportation costs by increasing political barriers to trade. Expanding trade flows coexisted with higher tariffs. These brief examples illustrate that the presence of aggregate trade flows, on their own, often tells us little about the causes of this exchange and the political and economic institutions that

18 For a discussion of the role of hierarchical relationships in international relations, see D. Lake (1996, 2007).
underpin it. Consequently, all trade may not be alike in its capacity to promote peace.¹⁹

The empirical and theoretical questions surrounding these two research programs carry important implications for the study here of the relationship between liberal economic institutions and peace. Most important, they underscore the need to expand the range of institutions that regulate state-society interactions within a domestic political system and shape a country's international relationships. As suggested by the arguments of Doyle (1983, 1986, 1997, 2005) and Zakaria (2003), the democratic peace may really be a liberal peace in which the peace is jointly created by multiple domestic institutions that protect civil liberties, ensure competitive markets, and widen political participation. This possibility suggests another theoretical implication. The peace among democratic states may really be caused by liberal economic institutions. Just as respect for private property and relatively laissez faire economic policies promote democracy, they could simultaneously promote peace. At the very least, these possibilities underscore the need to examine the relative capacity of liberal political and economic institutions to promote peace.

THE INVISIBLE HAND OF PEACE

One key thesis runs throughout this book: the domestic institutional foundations of liberal economic systems promote peace between states. This broader claim is rooted in two conceptual shifts from the broader liberal peace literature and decomposed into two constituent parts—one that focuses on the predominance of private ownership in a domestic economy, and another that concentrates on government efforts to limit the capacity of globalization to make domestic markets more competitive. I draw on classical liberal theory, standard trade theory, selectorate theory, the new institutionalism in economics, and the bargaining model of war to explain how these two institutions empower societal actors to prevent war. Just as Adam Smith suggested that an invisible hand facilitated the emergence of collective societal benefits from self-interested actions by individuals interacting within markets, the pursuit of wealth by private individuals interacting in competitive markets reduces the risks of war among states.

¹⁹ For a similar argument see Dorussen (2006) along with the literature cited earlier that examines how preferential trading arrangements promote peace. For example, Mansfield and Pevehouse (2000) show that trade only promotes peace between states that are also members to a common regional economic institution.
The first conceptual shift from the existing literature challenges the central role that the presence or absence of democracy has been accorded as a source of social order within domestic political systems and consequently as a cause of peace. Liberal international relations theory holds that the institutional relationship between a government and its citizenry plays a critical role in shaping the character of a state's foreign policy (Moravcsik 1997). Just as elections have been extolled for their capacity to protect individual liberty, the degree to which markets shape the allocation of scarce resources in an economy reflects government capacity to regulate, shape, and control individual and collective choices within society. In one of the foundational statements of the liberal peace, Michael Doyle (1983, pp. 207–8) points to four sets of domestic institutions that classical liberal theory identifies as advancing or protecting individual freedom: democratic elections, juridical equality among citizens, private property, and the allocation of scarce resources through decentralized markets rather than by bureaucratic authorities. Liberal peace research and policy proclamations associated with its claims have largely focused on the first two of these institutions, while neglecting the role of private property and competitive markets.

The second conceptual shift redirects attention away from such concepts as interdependence and aggregate trade flows that have traditionally been the focus of commercial liberalism and toward such liberal economic institutions, such as private property and competitive market structures, which shape both domestic and international commercial activity. This shift enables an exploration of the limitations and conditions under which international trade promotes peace among states. Although classical liberalism suggests that the material incentives generated by trade facilitate the emergence of common political interests and peace among states, standard trade theory shows how trade can be politically divisive between and within societies. Just as trade increases aggregate consumption possibilities for an economy, it simultaneously shifts the distribution of income within it. These distributional implications suggest that not all commercial flows are alike in their capacity to promote peace. As trade theorists note (e.g., Leamer 1993), commerce can be driven by multiple factors, including consumer tastes, transaction costs, transportation costs, relative factor endowments between countries, and political barriers to trade. Only one of these attributes—political barriers to trade—directly reflects the structure of domestic institutions that enables governments to influence prices within a domestic economy and thus shape individual choices within that political system.

These conceptual shifts facilitate the construction of the two critical component claims of this book—one focusing on how the relative predominance
of private property in an economy promotes peace; the second on how competitive domestic market structures promote peace. Given the centrality of these two institutions in capitalist economies, this twin institutional foci implies a much broader claim: capitalism promotes peace.\(^{20}\)

Large quantities of public property enable government officials to shape the allocation of scarce resources in an economy and simultaneously diminish the role played by decentralized markets in coordinating economic activity. State-owned enterprises act as political firms in which management decisions often reflect political expediency and bureaucratic pressures before profit. Large quantities of public property generate fiscal autonomy for governments and strengthen their hold on the domestic reigns of power. This fiscal autonomy increases the likelihood that governments will engage in military conflict for two reasons. First, it decouples domestic survival from foreign policy performance and decreases the domestic political risk governments face when pursuing aggressive foreign policies. Second, this financial autonomy enables governments to sustain arms races that both reduce the relative military power of adversaries and tempt those adversaries to launch preventive military attacks. Governments possessing access to large quantities of public property are more likely to engage in military conflict than governments overseeing more privatized economies.

Commercial policies shape the extent to which competitive market prices determine the allocation of resources within a domestic economy and the conditions under which globalization promotes peace. By restricting the entry of foreign goods, import tariffs decrease the size of domestic markets and increase the ability of domestic firms to influence prices (Varian 1996, pp. 418–19). The elimination of barriers to trade provides an important mechanism by which more competition can be “imported” into the domestic economy (e.g., Irwin 2002).

The ability of globalization to promote peace depends on the outcome of this crucial domestic political struggle over commercial policy. When free trading interests dominate the domestic political game, governments adopt fewer barriers to international trade and pursue more restrained national interests that create opportunities for cooperation with other states. When protectionist interests enjoy more domestic influence, governments adopt more aggressive foreign policies, including greater control over foreign territories, which raise the risks of military conflict with other states. The capacity

\(^{20}\) The definition of capitalism employed in this book relies on the key domestic institutions, namely private property and the allocation of scarce resources through competitive price signals, which modern economists generally use to define it. For examples of this definition, see Friedman (1962) and Kornai (1992, 2000).
to intervene in the domestic economy and shape this domestic struggle creates opportunities for governments to build coalitions supporting its entire range of policies, including those that heighten the risk of war with other states. These arguments point to the state’s capacity to regulate flows of goods, services, people, and capital across national boundaries as critically shaping the relationship between globalization and peace. Governments that adopt more restrictive policies toward international trade and investment flows are more likely to engage in military conflict.

The empirical sections of the book first test these two primary hypotheses linking private property and liberal commercial policies to peace; and then compare these findings with the existing body of work in the liberal peace literature that focuses on how democracy and economic interdependence promote peace between states. They draw on statistical analysis, archival research, and contemporary fieldwork to generate the following key findings:

1. Governments overseeing economies with high quantities of private property are less likely to engage in military conflict than governments overseeing economies with lower quantities of private property.
2. Governments embracing free-trade policies engage in fewer military conflicts than governments managing more closed economies.
   2a. This link between free-trade policies and peace spans both modern eras of globalization – one from the middle of the nineteenth century until 1914 and another during the post–World War II period.
3. The capacity of liberal economic institutions to promote peace has historically been stronger than that of democracy.
   3a. The democratic peace, or the claim that any two democracies are less likely to engage in military conflict than any other pair of regimes, does not emerge until after World War I.
   3b. Before World War I, democratic states were more likely than autocratic states to engage in all levels of military conflict, including war.
   3c. Moreover, in the twentieth century, the democratic peace holds only among states that also possess substantial quantities of private property.
   3d. Such a restriction does not apply to the peace created by liberal economic institutions. Liberal economic institutions promote peace irrespective of regime type.
3e. Whereas the democratic peace holds only in a dyadic setting (between two democracies), the peace created by liberal economic institutions holds in both dyadic and monadic research designs.

These arguments also create opportunities to rethink important historical cases that have been used both to confirm and challenge the arguments associated with the liberal peace. For example, the evolution of the relationship between the United States and Great Britain over the nineteenth century from one of rivalry and competition to one of cooperation and friendship has been repeatedly examined in the democratic peace debate (Owen 1994, 1997a, b; Layne 1994; Rock 1997; Way 1998; Blank 2000). Rather than reaffirm the capacity of democracy to promote peace, I show how normal democratic processes facilitated the emergence of expansionist foreign policy interests in the United States that heightened political conflict with Great Britain. The conflicts over Oregon and Venezuela in the nineteenth century illustrate that the predominant emphasis on democracy in the literature has obscured a much larger role within these respective countries for economic interests in both starting and stopping these disputes. Although protectionist interests in both countries helped to stimulate and prolong these conflicts, economic interests that were competitive in international markets and their political representatives played a critical role in halting these disputes and thus preventing war.

The conflict over Venezuela in 1895, in particular, carries important implications for larger historical debates over the role played by capitalist development in American foreign policy. Multiple historians have long pointed to economic factors as crucial in America’s transition from a continental to a global power in the 1890s (Williams 1959; LaFeber 1998). Because American territorial expansion during this period relied largely on projecting and using military force, these arguments suggest that commerce promotes conflict rather than peace. My reexamination demonstrates instead that the domestic economic interests most supportive of territorial expansion and conflict in this case were mercantilist and anticapitalist in nature.

Critics of liberal international relations theory have long pointed to the nineteenth-century era of globalization and the outbreak of World War I as powerful evidence contradicting the claim that commerce promotes peace. My arguments focusing on the domestic institutions underpinning economic exchange show why this skeptical conventional wisdom is wrong. Instead of asking why globalization failed to stop war, I examine how political
intervention in markets shaped the decision for war in July 1914. French capital controls and substantial quantities of public property in Russia helped shift the European balance of military power between 1905 and 1914. These market constraints contributed to a disproportionate Russian capacity to finance an arms race on land that precipitated the German decision to launch a preventive war in July 1914. Apart from reaffirming the explanatory strength of liberal international relations theory, these claims challenge the predominant focus in the historiography of World War I on German decision making. The key cause of World War I lies within the domestic institutions of Russia rather than Germany.

Finally, the evolution of the political conflict between China and Taiwan stands out as a critical case to test claims associated with the liberal peace in the contemporary era of globalization. As Taiwan has embraced democratization and liberalized trade with the mainland, the relationship has deteriorated with both periodic military exercises and bold political statements that raise the threat of war. These trends suggest that political and economic liberalization have stimulated, rather than dampened, conflict across the Taiwan Straits. I show that liberal economic institutions, but not liberal political institutions, have helped to stabilize the recent conflict between China and Taiwan. Although democratization has created incentives for some Taiwanese politicians to pursue pro-independence policies that heighten the risk of war, economic reforms are both restraining the mainland’s stance toward Taiwan and shifting Taiwan’s internal balance of power toward groups opposed to independence and the potential war it could bring.

THE STRUCTURE OF THE BOOK

The book is organized into three key sections. The first section, in Chapters 1 through 3, examines how a concentration on the pacific effects generated by liberal economic institutions interacts with existing research on the liberal peace and debates about American grand strategy. Chapter 2 examines the liberal peace debate in the context of contemporary international relations theory and Western philosophy. It shows how a focus on institutions regulating the domestic economy can generate new insights into unanswered questions in these debates. Chapter 3 develops the theoretical explanations linking private property and competitive market structures to peace.

The second section of the book, in Chapters 4 through 8, tests these arguments linking private property and competitive markets to peace by
examining their historical capacity to limit military conflict. For the most part, the liberal peace literature has predominantly drawn on multivariate statistical analysis to check the empirical veracity of various propositions linking either democracy or commerce to peace and then refine them. To ensure comparability of the findings here with this broader literature and to establish that my domestic variant of commercial liberalism has promoted peace across time and in multiple countries, Chapters 4 and 5 adopt a similar research strategy. Chapter 4 tests the capacity of these institutions to promote peace in the twentieth century. Chapter 5 then extends this statistical analysis by looking at the nineteenth-century era of globalization that ended in 1914. Together, the findings of these two chapters illustrate the historical depth of this domestic variant of commercial liberalism, showing that it existed across both modern eras of globalization.

Chapters 6 through 8 deepen this empirical analysis by presenting a series of detailed case studies chosen for their capacity to confront the most critical tests of liberal international relations theory over the past two centuries and to reveal the mechanisms by which an invisible hand pushes governments to adopt more pacific foreign policies. Given the implications of the arguments here for debates over American foreign policy, Chapter 6 examines how struggles over trade, tariff policy, and imperialism in the United States shaped the relationship with its chief rival in the international system during the nineteenth century. Chapter 7 reexamines the Achilles' heel of liberal international relations theory — the outbreak of World War I following more than a fifty-year period of globalization. Chapter 8 investigates the recent evolution of the conflict between China and Taiwan.

The final section, in Chapters 9 and 10, explores the relative capacity of democracy and liberal economic institutions to promote peace and then revisits the policy implications of these conclusions. Chapter 9 draws on a wide range of statistical tests to show that market-based exchange, not democracy, has historically acted as a more significant constraint on war. Chapter 10 presents a summary of the book's key arguments and then returns to where it began. What are the implications of this capitalist peace for American foreign policy in the twenty-first century, when it faces multiple challenges like the rise of China, Islamic fascism, terrorism, and a backlash against globalization in much of the developing world? It argues that the relative emphasis between promoting markets and democracy should be switched in American grand strategy. The United States possesses the largest and most vibrant market in the global economy. American grand strategy can integrate this unique political asset more effectively. A comparison
among British economic statecraft in the 1840s, American attempts to rebuild the European economy following World War II, and contemporary efforts by China to utilize economic incentives to transform its political relationship with Taiwan suggests how similar broad-based economic liberalization strategies by the United States could release the invisible hand to promote development, democracy, and peace in the contemporary world.