

# THE TOBACCO TAX IN LATE COLONIAL SPANISH AMERICA:

## THE MAKING OF THE ROYAL TOBACCO MONOPOLY \*

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### ABSTRACT

This paper examines the relationship between the state and the tobacco industry in late colonial Spanish America. The 18<sup>th</sup> century Bourbon monarchs increased regulation and control over the tobacco industry, from tobacco cultivation to cigarette and cigar manufacture. The paramount goal was to increase fiscal revenues. The paper gives a new perspective on the rationale for vertical integration. It argues that vertical integration was perceived as a mean to reduce monitoring efforts in the control of illegal trade. The Bourbon strategy, however, reflected a great deal of flexibility and pragmatism. Monopoly policies were critically affected by political considerations, which caused the relative decline of the monopoly in the last decades of the empire. In addition to offering an overview of the basic trends of monopoly policies, the paper shows that the *Estanco* was effective in the extraction of rents.

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The tobacco industry was an economic activity of extraordinary importance for the Spanish crown. In the Iberian Peninsula the industry was monopolized in the late seventeenth century. Soon after, the Spanish monopoly became a critical source of income yielding around 25% of fiscal revenues.<sup>2</sup> The economic significance of the industry was certainly critical for the establishment of the *Estanco*, but there were other considerations that made tobacco an ideal source of government income. Given that tobacco was not a necessary commodity a tax on tobacco was perceived as a “voluntary” contribution, which was consistent with the Bourbon view that in order to build a prosperous empire the crown had to promote the well being of the population at large.<sup>3</sup>

In Spanish America, the tobacco industry became increasingly important under Bourbon rule. Tobacco was the second most important export industry in Spanish America at the time, only behind silver.<sup>4</sup> The tobacco monopoly was an important component of the Bourbon plan throughout Spanish America. It was instituted in Cuba in 1717, in Peru in 1752, in Chile and La Plata in 1753, in New Spain in 1764, in Costa Rica in 1766, and in most other areas of Spanish America including New Granada, Paraguay and Venezuela in the 1770s.<sup>5</sup> The most interesting and comprehensive works on the tobacco enterprise have been published for Mexico, although there are studies that

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<sup>2</sup> Agustín González Enciso, “En torno al contrabando de tabaco en el siglo XVIII,” in *Estudios de Historia Moderna y Contemporánea*. Homenaje a Federico Suarez Verdeguer, 1991, p.199.

<sup>3</sup> See Colin MacLachlan, *Spain's Empire in the New World: the Role of Ideas in Institutional and Social Change*, 1988, pp. 68-80.

<sup>4</sup> Total tobacco exports were 13.6% of the total during the “free-trade” period 1782-1796. Tobacco was followed by *cacao* with 7.8% and sugar with 5.5%. See John Fisher, *The Economic Aspects of Spanish Imperialism in America, 1492-1810*, 1997, p.168.

<sup>5</sup> The La Plata and Chile monopolies were in the administrative jurisdiction of Peru until 1776 and 1785 respectively.

contribute to the understanding of the monopoly in other areas.<sup>6</sup> Overall, most of these works are focused on the institutional evolution of the *Estanco* and pay little attention to its economic and social aspects.<sup>7</sup>

This article contributes to the literature through a discussion of the rationale of monopoly policies and an evaluation of the overall economic performance of the monopoly in the region. In so doing the paper provides a survey of the literature together with new data on the Peruvian experience.<sup>8</sup>

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<sup>6</sup> Among the most important studies of the Mexican tobacco monopoly are: Susan Deans-Smith, *Bureaucrats, Planters and Workers. The Making of the Tobacco Monopoly in Bourbon Mexico*, 1992, which is to this day the most comprehensive and thoughtful study on the Mexican monopoly. Other sources are: Guillermo Céspedes del Castillo, *El tabaco en Nueva España*, 1992; David Lorne McWatters, "The Royal Tobacco Monopoly in Bourbon Mexico 1764-1810," Ph.D. diss., University of Florida, 1977, and Maria Amparo Ros, "La real fábrica de tabaco, un embrión de capitalismo?" *Historias* 10 (1985). For other areas see Jerry W. Cooney, "La Dirección General de la Renta de Tabacos and the Decline of the Royal Tobacco Monopoly in Paraguay, 1779-1800," *Colonial Latin American Historical Review* 1 (1992); Thomas L. Whigham, "Agriculture and the Upper Plata: The Tobacco Trade, 1780-1865," *Business History Review* 59 (1985); René de la Pedraja Tomán, "Los cosecheros de Ambalema: un esbozo preliminar," in *Anuario Colombiano de Historia Social y de la Cultura* 9 (1979); Eduardo Arcila Farias, *Historia de un monopolio. El estanco del tabaco en Venezuela (1779-1833)*, 1977; Juan Carlos Arias Divito, "Dificultades para establecer la Renta del Tabaco en Paraguay," *Anuario de Estudios Americanos* 33 (1976); Margarita Murillo Gonzales, "El Estanco colonial del tabaco," *Cuadernos Colombianos* 2 (1975); Eduardo Arcila Farias, "La Administracion de la Renta del tabaco en Venezuela," *Anuario de Estudios Americanos* 31 (1974); Marco Antonio Fallas, *La factoría de tabacos de Costa Rica*, 1972; Agnes Stapff, "La Renta del tabaco en el Chile de la época virreinal. Un ejemplo de la política económica mercantilista," *Anuario de Estudios Americanos* 18 (1961); John Harrison, "The evolution of the Colombian Tobacco Trade to 1875," *Hispanic American Historical Review* 32 (1952) and "The Colombian Tobacco Industry from Government Monopoly to Free Trade, 1778-1876," Ph.D. thesis; 1951; José Rivero Muñoz, *Tabaco: Su historia en Cuba*, 2 vols, 1964-1965; Fernando Ortiz, *Cuban Counterpoint. Tobacco and Sugar*, 1995.

<sup>7</sup> Deans-Smith's work on the Mexican experience and Catalina Vizcarra's Ph. D. dissertation "Markets and Hierarchies in Late Colonial Spanish America: The Royal Tobacco Monopoly in the Viceroyalty of Peru," are the exception.

<sup>8</sup> The literature on the Peruvian monopoly is relatively limited. The most important published works are: John Fisher, "El estanco del tabaco en el Perú borbonico," In González Enciso and Rafael Torres Sánchez (eds.), *Tabaco y economía en el siglo XVIII*, 1999; Guillermo Céspedes del Castillo, "La renta del tabaco en el virreinato del Perú," *Revista Historica* 21 (1954), pp. 138-163, and Christine Hunefeldt, "Etapa final del monopolio en el virreinato del Perú: el tabaco en Chachapoyas," in Nils Jacobsen and Hans-Jurgen Puhle (eds.), *The Economies of Mexico and Peru During the Late Colonial Period*, 1986. In addition, the first comprehensive work on the Peruvian monopoly could be found in Catalina Vizcarra, "Markets and Hierarchies in Late Colonial Spanish America: The Royal Tobacco Monopoly in the Viceroyalty of Peru," Ph.D. Diss, University of Illinois at Urbana-Champaign, 2001. Also see Catalina Vizcarra and Richard Sicotte, "El control del contrabando en el Perú colonial: el caso del monopolio del tabaco, 1752-1813," in Carlos Contreras and Manuel Glave (eds.), *Estado y mercado en la historia del Perú*, 2002, pp.184-211.

The first section of the paper discusses the rationale behind the monopolization of the tobacco industry. In particular, it discusses why the tax on tobacco took the form of a vertically integrated enterprise that controlled not only production and distribution of the tobacco leaf, but also the manufacture of cigars and cigarettes. Centralization of manufacture did not imply any technological innovations or significant economies of scale in the manufacture of tobacco products. Nonetheless, as the Peruvian case illustrates, factory organization was successfully used as an instrument in the control of contraband.

The economic success of the tobacco monopoly was inextricably linked to the establishment of the tobacco factories. In both areas for which we have in depth studies available, New Spain and Peru, the tobacco monopoly yielded its highest revenues under full vertical integration. Interestingly, the analysis of the evolution of the *Estanco* suggests that political constraints influenced considerably the course of monopoly policies. Even though there were well documented economic restrictions to the expansion of monopoly revenues in certain areas in the late 1780s and beyond, such as bottlenecks in the supply of raw materials, the paper suggests that the relative downfall that the monopoly experienced in the last decades of the empire was a function of political rather than economic constraints.

In particular, in the years that followed Charles III death, the *Estanco* was evaluated in most areas, and its regulations were adjusted to the changing attitudes in Madrid. In the early 1790s the Crown took a number of measures that illustrated its concerns with the security of the empire and its fears of upheavals in the colonies. In spite of their good economic results, the Peruvian tobacco factories were closed after only

ten years of operation due to Crown mandates that emphasized security and precaution rather than efficiency.

#### BOURBON RATIONALE

The early state intervention in the tobacco industry was shaped by the experience of the Royal tobacco monopoly in the Peninsula. In particular, the Cuban industry, with the tobacco of best quality, was monopolized early on in the eighteenth century with the explicit goal of assuring enough imports of Cuban tobacco leaf for the factories in Seville.<sup>9</sup> In all other areas, the tobacco monopoly was instituted decades later as a critical component of the Bourbon plan to increase fiscal revenues.<sup>10</sup>

The crown manifested interest in extending the monopoly beyond Cuba to other colonies in the 1740s. The enthusiastic response of the Peruvian viceroy led to the early establishment of the Peruvian *Estanco* in 1752.<sup>11</sup> Later on, in the 1760s, it was instituted in Mexico under the guidance of José de Gálvez in his capacity of *visitador* of New Spain.<sup>12</sup>

The monopoly was instituted in the rest of Spanish America during Gálvez' tenure as Minister of the Indies (1776-1787). The Gálvez' years brought major changes in the structure and administration of monopoly operations. The reforms, however, were

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<sup>9</sup> The paper does not include an in depth discussion of the Cuban case due to its marked differences with the monopoly administration in the rest of the region. See Doria González Fernández, "Tabaco y poder. La primera factoría de la Habana," in *Tabaco y Economía en el siglo XVIII*, 1999, p. 110. Also, see Laura Nater, "El negocio colonial del tabaco en el Imperio Español," unpublished manuscript.

<sup>10</sup> The Bourbons sought to transform the relatively weak colonial state of the Habsburg period into a stronger centralized state. One of the principal goals was the increase of fiscal resources. For an interesting analysis of this transition see, John Lynch, "The Institutional Framework of Colonial Spanish America," *Journal of Latin American Studies*, 24, Quincentenary Supplement: The Colonial and Post Colonial Experience. Five Centuries of Spanish and Portuguese America. (1992), pp. 69-81.

<sup>11</sup> See Vizcarra, "Markets and Hierarchies," p.26.

<sup>12</sup> José de Gálvez took over the *Dirección* of the *Estanco* shortly after his arrival in Mexico. See Deans-Smith, "Bureaucrats, Planters and Workers," chp. 1, for an in depth discussion of Gálvez' role in the establishment of the Mexican tobacco monopoly.

the result of a clearer commitment and political will to expand the control of the industry and enforce monopoly regulations, not a new vision.

Monopoly regulations followed a *path influenced* trend. The *Estanco's* experience in the Peninsula was the main guidance to the administration of the Spanish American monopolies. They were for the most part conceived of as vertically integrated enterprises.<sup>13</sup> We have studies on the rationale and on the process of centralization of manufacture in New Spain and Peru.<sup>14</sup> There is also evidence that factories for the production of cigars and cigarettes were established in other areas, such as Colombia and Venezuela, but no works are available on the rationale or on the organization of the factories in these areas.<sup>15</sup> Nonetheless, based on documentary evidence and secondary sources on New Spain and Peru, we can learn several aspects of the organizational methods, strategy, and rationale of the monopoly enterprise.

### *The Mexican Experience*

The Mexican domestic tobacco industry was the largest in Spanish America during the Bourbon period. Deans-Smith describes it as a vibrant industry dominated by petty producers, and artisans. The most popular consumption habit was smoking cigars and cigarettes, which was widespread not only in the urban areas, but also in the country side. In contrast to Peru, tobacco consumption played an important cultural role among the indigenous Mexican communities.<sup>16</sup>

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<sup>13</sup> The crown's control over the tobacco industry in the Iberian Peninsula varied considerably throughout the years. Only well into the eighteenth century crown policies stabilized adopting a definite shape of a vertically integrated enterprise. See José Pérez Vidal, *España en la historia del tabaco*, 1959.

<sup>14</sup> See Deans-Smith, "*Bureaucrats, Planters and Workers*," chps. 1, 6 and 7. For Peru see Vizcarra, "Markets and Hierarchies," chp. 4, and "Imperialists as Managers."

<sup>15</sup> See the works of Arcila Farias, "*Historia de un Monopolio*," and John Harrison, "The Colombian Tobacco Industry from Government Monopoly to Free Trade." I will expand on this point in a future version of the paper.

<sup>16</sup> Deans-Smith, "*Bureaucrats, Planters and Workers*," p. 11-14.

Before the institution of the monopoly, the tobacco industry was not dominated by powerful economic groups. Indeed, as Deans-Smith suggests “...no powerful merchant lobby existed which could challenge the monopolization of the tobacco trade, and the region where tobacco was on the rise as a major commercial crop in Veracruz was not hindered by the monopoly but was incorporated into its operations.”<sup>17</sup> The author adds that in the early period, resistance came from the bureaucracy itself.<sup>18</sup>

Soon after the establishment of the *Estanco*, the colonial state heavily regulated production and distribution of the tobacco leaf. The two most important production areas were Orizaba and Cordoba.<sup>19</sup> Royal orders, however, stated early on that the *Estanco* should include the monopolization of manufacture.<sup>20</sup> The implementation of this measure took several years. According to Deans-Smith, this was by far the most controversial Royal mandate. Opponents to the establishment of state tobacco factories cited major riots in the city of Puebla as evidence of major discontent. They claimed that this was just the prelude to potential widespread protest against the monopoly if it were to carry out this measure.<sup>21</sup>

Nonetheless, José de Gálvez, *visitador* of New Spain at the time, was committed to the establishment of the tobacco factories. He dismissed these reports and pushed successfully for their final institution.<sup>22</sup> Gálvez’ approach was based not on coercion but cooptation of vested interests. The private workshops were progressively banned and the state absorbed into its operations workshops owners and artisans. By 1770, five large

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<sup>17</sup> Deans-Smith, “Bureaucrats, Planters and Workers,” p.14.

<sup>18</sup> *Idem*.

<sup>19</sup> For an interesting discussion on the production areas and the cooptation of vested interests among the *cosecheros*, see Deans-Smith, *Ibid.* chp.4.

<sup>20</sup> *Idem*.

<sup>21</sup> The director of the monopoly, Espinoza, and Viceroy Cruillas were among the most radical opponents of the centralization of manufacture. Deans-Smith, *Ibid.* p.21.

<sup>22</sup> Deans-Smith, *Ibid.* p. 22.

factories had been instituted in Mexico city, Guadalajara, Puebla, Queretaro, and Orizaba. Their size and importance were impressive, the Mexican factories eventually employed over 13,000 workers.<sup>23</sup>

Susan Deans-Smith, in her work on the Mexican monopoly, argues that according to public officials' reports, there were two reasons for the centralization of manufacture: 1) Profitability, and 2) The expansion of opportunities of employment for the urban poor. Deans-Smith argues that the Bourbons had a perspective close to a "maximization of revenues" approach. As she puts it:

"With regard to profit, the bureaucrats adopted an opportunity costs approach to determine which method used tobacco resources more profitably, sales of tobacco leaf or of manufactured products. As Jon Cohen has argued for the economic rationale of early mill production in England, their owners 'implicitly or explicitly were compelled to do their sums; they had to estimate the expected return on various options open to them and select the one that brought the highest pay-off.' This is precisely what the monopoly bureaucrats, under José de Gálvez's guidance, did."<sup>24</sup>

Documentary evidence on the Peruvian monopoly is somewhat consistent with Deans-Smith findings, although it gives an additional dimension to the vertical integration rationale. In particular, according to documentary evidence the centralization of manufacture in Peru was perceived as a critical step in the battle against contraband.<sup>25</sup>

It is worth noting that the officials' calculations described in the citation above (also present in the Peruvian records) were not accurate. In particular, economic theory

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<sup>23</sup> Deans-Smith, *Ibid.* p.159.

<sup>24</sup> Deans-Smith, *Ibid.* p.144.

<sup>25</sup> The argument for the creation of jobs for the urban poor is absent from Peruvian documents. See Vizcarra, "Markets and Hierarchies, chp. 4."

has shown that the monopolist of an input used in fixed proportions with other inputs could obtain full monopoly rents without vertically integrating.<sup>26</sup> In other words, the centralization of manufacture was not a necessary condition for the maximization of monopoly revenues. There is overwhelmingly evidence that there were no technological improvements nor were there major economies of scale brought by factory organization in either Mexico or Peru.<sup>27</sup> It seems that the major impact that factory organization had on monopoly performance was related to its role in the fight against contraband, as the Peruvian case illustrates.

#### *Factory Discipline and the Control of Contraband in the Peruvian Viceroyalty*

Before state control, the tobacco industry in Peru was relatively modest. As a consequence, monopoly officials had great degrees of freedom in the design of monopoly policies. Only a few years after the establishment of the *Estanco*, the colonial state took complete control of tobacco production and distribution, heavily regulating its cultivation by private planters, including the determination of quotas of production and prices. The production areas were restricted to two: Saña, along the northern Peruvian coast, and Chachapoyas, in the northern Andes. Only in 1780, under the direction of Gálvez, the

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<sup>26</sup> Vernon and Graham demonstrated that the monopolist of an input used in fixed proportions with other inputs could obtain full monopoly rents without vertically integrating. This situation corresponds to that of the tobacco leaf in the production of cigars and cigarettes. Nevertheless, Quirmbach showed that integration might be profitable in such scenario if there are “scale distortions.” Scale distortions can occur if downstream firms face U-shaped average costs, because the monopoly price of the intermediate good will induce firms to adopt a scale that is not equal to the lowest possible unit cost. The main point here is that the upstream monopolist can increase total profits through integration by lowering industry costs. Therefore, the discussion of the existence of scale effects is critical to evaluate changes in transformation costs that could have occurred when the colonial state integrated into the manufacture of tobacco products. See John Vernon and Daniel Graham, “Profitability of Monopolization by Vertical Integration,” *Journal of Political Economy*, 79 (1971); also see Herman Quirmbach, “Vertical Integration: Scale Distorsions, Partial Integration, and the Direction of Price Change,” *Quarterly Journal of Economics* 100 (1986).

<sup>27</sup> See Deans-Smith, “Bureaucrats, Planters and Workers,” p. 152 ; and Vizcarra, “Imperialists as Managers: The Making of the Peruvian Tobacco Factories, 1780-1791 (unpublished manuscript) and “Markets and Hierarchies,” chp.4.

*Estanco* centralized the manufacture of cigars and cigarettes, which was previously in the hands of artisans (see Table 1 for a synthesis of this evolution).

The centralization of manufacture was sanctioned early on in the Peruvian ordinances of 1759. But it was only under the direction of Gálvez that artisanal production was banned and the state installed factories for the production of cigars and cigarettes. In Peru, in contrast with the Mexican case, there was no major opposition to the institution of the tobacco factories. Indeed, most former tobacco workers and the owners of tobacco workshops were easily co-opted by the monopoly, and hired as factory's employees.<sup>28</sup>

Interestingly, the centralization of manufacture was viewed as a critical step in the battle against contraband. Transaction cost economizing arguments supported a number of the new regulations and the rationale for vertical integration. According to documentary evidence, under the system that pre-dated centralization, the *Estanco* faced high monitoring and enforcement costs. Licensed workshop managers (artisans) and licensed retailers were heavily regulated and were required to buy the tobacco leaf at the monopoly warehouses. Monopoly supervisors, who visited regularly the workshops and retailer stores were responsible for contrasting their accounts and inventories with the monopoly warehouses' books (which recorded all sales). Monitoring costs were high because it was impossible to distinguish between legal and illegal tobacco at the workshops and retailer stores.<sup>29</sup>

With centralization the monopoly banned all final sales of tobacco leaf, which was a policy oriented to help control fraud. Under the new system, the private workshops

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<sup>28</sup> See Vizcarra, "Imperialists as Managers," p. 15.

<sup>29</sup> Vizcarra, *Ibid.* p. 7.

were not allowed to operate and the retailers only sold monopoly manufactured products, which had a seal of origin stamped at the state manufactures. Thus, illegal manufacturers faced a higher risk of detection. Smugglers could yet attempt to disguise their products, but this would be neither easy nor free.<sup>30</sup>

Elsewhere I have shown that the centralization of manufacture and additional anti-contraband measures passed under Gálvez were successful in curbing contraband, which makes it difficult to understand Viceroy Gil's decision to close the tobacco factories in 1791.<sup>31</sup> The paper discusses below how this decision was a result of political rather than economic constraints. But first, it offers a brief overview of the evolution of the monopoly performance.

#### MONOPOLY POLICIES AND FISCAL REVENUES<sup>32</sup>

The historiography on the efficacy of the Bourbon reforms has paid particular attention to their achievements in tax collection. According to most scholars, the Bourbon state was quite successful in the extraction of resources.<sup>33</sup> The latest findings on the tobacco enterprise confirm this view. Revenues from the tobacco industry were an important part of the fiscal burden in all areas in Spanish America where the *Estanco* was established.<sup>34</sup>

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<sup>30</sup> See Vizcarra, *Idem*.

<sup>31</sup> See Vizcarra, "Markets and Hierarchies," chp.4 and Vizcarra and Sicotte, "El control del contrabando en el Perú colonial."

<sup>32</sup> I will expand on this in a future version of the paper.

<sup>33</sup> For an overview of the royal treasury in Spanish America see Herbert Klein, *The American Finances of the Spanish Empire. Royal Income and Expenditures in Colonial Mexico, Peru, and Bolivia, 1680-1809*, 1998. For a general assessment of the reforms in Peru see John R. Fisher, *El Perú borbónico, 1750-1824*, 2000. For an analysis of the treasury in New Spain see Carlos Marichal, *La bancarrota del virreinato. Nueva España y las finanzas del imperio español, 1780-1810*, 1999. Also see John Coatsworth, "Límites del absolutismo colonial," in *Los orígenes del atraso. Nueve ensayos de historia económica de México en los siglos XVIII y XIX*, 1990.

<sup>34</sup> The literature on the Andean region, in particular, the work of Christine Hunefeldt on the Peruvian monopoly had a much grimmer view of the monopoly performance. Only recent work based on a complete data set has proposed a more positive view. See Catalina Vizcarra, "Markets and Hierarchies."

The economic importance of the tobacco industry in the region could not be overstated. In Nueva Granada, according to Harrison, the monopoly was the most important source of income in the thirty years before independence.<sup>35</sup> In Venezuela, the monopoly yielded a total gross of 1,946,393 pesos in 1798. This was an extraordinary year, however, for in the two following ones it yielded a gross average of 1,026,000 pesos.<sup>36</sup> Other areas for which we have some data are Costa Rica, where the monopoly produced around 520,000 pesos a year in the late 1780s,<sup>37</sup> and Paraguay where the *Real Estanco* produced around 250,000 pesos a year in the same decade.<sup>38</sup>

In Peru, as Table 2 illustrates, monopoly revenues were substantial relative to other sources of revenues. Tobacco was the second source of gross income since the 1770s.<sup>39</sup> Interestingly, we can infer from contemporary documents the portion of the value added from the industry captured by the *Estanco* in its early years.<sup>40</sup> Net monopoly revenues in the early 1750s, which were on the average approximately 140,000 pesos, were equivalent to around 40% of the estimated value added of the industry.<sup>41</sup> Thus, even in the early monopoly period (1752-1780), which was, as Table 2 shows, the least profitable for the colonial state, the monopoly was quite effective in the extraction of rents. The Peruvian monopoly achieved its largest revenues during the factory period

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<sup>35</sup> John P. Harrison, "The Colombian Tobacco Industry from Government Monopoly to Free Trade: 1778-1876," p. vii.

<sup>36</sup> Arcila Farías, "*Historia de un monopolio*," p. 68. Farías only provides scattered data on revenues.

<sup>37</sup> This estimation is based on the final price and total tobacco production given by Fallas, "*La factoría de tabacos*," pp. 60-61. The figure given should be taken only as an upperbound.

<sup>38</sup> This estimation is based on data on production and final prices from Cooney, "La Dirección General de la Renta de tabacos."

<sup>39</sup> Revenues from mining, trade, and *tributo* are gross figures.

<sup>40</sup> My estimates are based on Thomas Chavaque's report; AGI, Lima, 1229.

<sup>41</sup> According to contemporary documents, in the 1740s, the value of total consumption for the tobacco industry was around 700,000 annual pesos, and the industry's value added was about 336,400 pesos.

(1781-1792). Average net revenues were of around 132,000 in the pre-factory period, 340,000 in the factory years and of around 256,000 in the last decades of the monopoly.<sup>42</sup>

The monopoly in New Spain yielded the largest revenues of all areas. In Table 2 we see the annual averages since the 1760s. In Mexico, tobacco was the second most important commodity in the production of government income surpassing silver in the first decade of the 1800s. Net revenues in New Spain also increased substantially with the institution of the tobacco factories and the prohibition of artisanal production (which became absolute in 1780). In the 1780s, average net revenues were twice as large than in the previous decade.

### *The Evolution of Monopoly Revenues*

The historiography has discussed only sparingly the evolution of monopoly revenues. Based on secondary sources and on data for the Peruvian enterprise we can conclude that the tobacco monopoly grew more rapidly under the Gálvez administration than in any other period. In Peru, Costa Rica, and Paraguay, these were the years of maximum expansion.<sup>43</sup> In Mexico monopoly revenues peaked in the 1790s. In Venezuela they increased until the wars of independence but at a lower rate.<sup>44</sup>

Nonetheless, there were several challenges faced by the *Estanco*. Beyond those related to the administration of the monopoly, i.e. monitoring and enforcements costs, there were other economic constraints.<sup>45</sup> For the Mexican monopoly, for example, Deans-Smith suggests that the critical economic problem faced by monopoly officials

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<sup>42</sup> Vizcarra and Sicotte, “El control del contrabando en el Perú colonial: El caso del monopolio del tabaco, 1752-1813,” in *Estado y Mercado en la Historia del Perú*, 2002, p.190.

<sup>43</sup> For Costa Rica, see Fallas, “*La factoría de tabacos*,” p. 98. For Paraguay, see Cooney, “La Dirección General de la Renta de tabacos.”

<sup>44</sup> For Venezuela, see Arcila Farias, “*Historia de un monopolio*,” p. 68.

<sup>45</sup> Given the state of the literature we are not in a position to evaluate the impact of monitoring costs.

was related to the supply of raw materials. According to the author, limits on the supply of paper were reached after 1790.<sup>46</sup> The Peruvian monopoly faced similar challenges. In the 1780s, during the factory period, the poor management of the warehouse facilities together with the scarcity of tobacco supplies of good quality i.e. Cuban tobacco due to the wars of American independence, critically affected the sales of cigars and cigarettes.<sup>47</sup>

The evolution of tobacco monopoly revenues throughout the region, however, was inextricably linked with the political events of the late 1780s. Gálvez died in 1787 and Charles III shortly after in 1788. As a consequence, the *Estanco* was re-evaluated in most areas, and in many of them its policies were adjusted according to the more cautious prescriptions from Madrid. Vested interests seemed to have played a key role in the assessment and modification of monopoly policies. In some areas, monopoly policies were relaxed and monopoly revenues decreased accordingly, while in others the monopoly continued functioning nearly unaffected.

#### THE FINAL YEARS

“Being the will of your Majesty [Charles IV] that the *Estanco* be administrated with economy and good order, so that the well served and treated public, far from perceiving it as a heavy tax burden, receive it as a much more lenient one...in order to provide a happy sense of security to the individuals that compose it [the state].”<sup>48</sup>

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<sup>46</sup> See Deans-smith, “*Bureaucrats, Planters and Workers*,” p. xiv and p. xix.

<sup>47</sup> Vizcarra, “Markets and Hierarchies,” chp. 4.

<sup>48</sup> Superior Decree, signed by viceroy Gil; Lima, Dec. 26, 1791; AGI, Lima 1232.

The Crown's needs and views on the appropriate course of action for monopoly policies was only one among multiple variables that shaped the evolution of the *Estanco*. As Acemoglu, Johnson and Robinson argue, institutional change is not separable from distributional issues.<sup>49</sup> In other words, efficiency considerations are often not the ultimate factor explaining the course of institutional change. Interest groups and vested interests in the industry had a major role to play in the course of monopoly policies.

In the years that followed the death of Gálvez, the Crown took a number of measures that illustrated its concerns with the security of the empire, especially its fears of upheavals in the colonies. The *Estanco* was evaluated in most areas, and its regulations were adjusted to the changes in policies prescriptions from Madrid. However, the divergent outcomes in the different areas where the *Estanco* operated suggest that vested interests played an important role in the course of institutional change. Documentary sources and the secondary literature suggest that the Crown relaxed monopoly policies in those areas where conflicts with local elites related to monopoly operations were most apparent. The monopoly in Paraguay, for example, experienced a relaxation in its policies. As Cooney puts it:

“...shortly before the death of the Minister of the Indies, José de Gálvez, and the subsequent termination of his ‘revenue-producing reforms,’ Paula Sanz was removed from the *Superintendencia* of Buenos Aires...Now with a greater willingness among officials to appease the local elites and with less zeal displayed for law enforcement, the war against contraband on the rivers noticeably slackened. Thus by 1790 those former obstacles to the contraband traffic had disappeared. In 1790-91 the apprehension

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<sup>49</sup> Acemoglu, Johnson and Robinson, “Institutions as the Fundamental Cause of Long-Run Growth,” forthcoming in the *Handbook of Economic Growth*, Philippe Aghion and Steve Durlauf (eds.).

of downriver smugglers by the Resguardo (revenue police) had vanished...”<sup>50</sup>

Charles IV ordered the abolition of the *Estanco* in Venezuela, in October of 1792, conceding that since its institution several demands for its termination were introduced before the Crown, and that, “in all justice,” the monopoly should be brought to an end. The royal order stated that the *Ayuntamiento* (local government) had to commit to taxing the tobacco industry either through the *encabezamiento* (head tax to be paid by tobacco producers) or through any other system that the local authorities deemed appropriate. According to Arcila Farias, a heated argument following the royal order, between those farmers excluded from the state enterprise and those who wanted to keep their privileges ensued. In the end, those lobbying for the status quo won the battle and the *Estanco* continued functioning, mostly unchanged, until the wars of independence.<sup>51</sup>

In New Spain, the monopoly lost its relative autonomy with respect to the *Tribunal de Cuentas*, although no other major administrative changes followed. As Deans-Smith argues, from the early 1790s, attempts to reform the monopoly to adjust to economic and political changes were silenced. Although this is merely speculative, it is likely that what laid behind the relative rigidity of Mexican regulations was the important economic role of the monopoly as collateral for government loans (the monopoly in New Spain was mortgaged for 15 million pesos by 1797). The latter generated the support that the monopoly enjoyed from leading merchants and miners.<sup>52</sup>

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<sup>50</sup> Jerry Cooney, “La Dirección General de la Renta de tabacos,” p.108.

<sup>51</sup> For an interesting discussion of vested interests in the distinct provinces involved in tobacco production, and their role opposing the royal order, see Arcila Farias, “*Historia de un monopolio*,”\_chp. 12.

<sup>52</sup> See Susan Deans-Smith, “*Bureaucrats, Planters and Workers*,” p. 52 and p. 65.

The Peruvian case illustrates well the politics behind the modifications of the *Estanco* under Charles IV. The arrival, in 1790, of Viceroy Gil de Taboada y Lemos (1790-1796) was crucial for the course of monopoly policies. Viceroy Gil had strong ties with newly appointed officials in Madrid, especially, with Antonio Valdés, who was in charge of the Ministry of Finance.<sup>53</sup> He was appointed first as viceroy of New Granada in 1788, and shortly after, as viceroy of Peru.

As Allan Kuethe explains in his article on the culmination of the Bourbon reforms, Gil fought the huge financial crisis in New Granada with the same views he would apply in Peru a few months later: reducing expenditures instead of increasing taxes and expanding the bureaucracy. Kuethe finds Viceroy Gil's policies to be consistent with Barbier's interpretation of the new regime: The crown became more cautious under Charles IV, advancing the Bourbon program as long as it did not threaten local vested interests.<sup>54</sup> Gil, for example, as viceroy of New Granada, supported the policy towards modernization of the mining industry, whereas in Lima, where opposition from Lima's mercantile oligarchy was apparent, Gil visibly opposed those same policies.

Viceroy's Gil stand on the tobacco industry, is consistent with this interpretation. Soon after his arrival to Lima, honoring his duties as maximum authority of the royal

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<sup>53</sup> In 1787 the Ministry of the Indies was divided into two offices. One in charge of war, finance and commerce, under Antonio Valdés, the other one in charge of grace and justice under Antonio Porlier. In 1790, a *Junta de Estado* was formed to oversee policies in Spain and America. The colonial portfolios were abolished and the newly nominated peninsular ministers gained authority over the Indies in their own sphere. The *Junta de Estado* was composed of five offices: Florida Blanca was in charge of the Ministry of State, Campo Alange of war, Valdés of the navy, Lerena of finance, and Porlier of justice. This evolution, according to Barbier, was "the logical culmination of nearly nine decades of administrative development," whose principal problem was the coordination of policies. The *Junta de Estado* was meant to guarantee "union and equality" between Spain and America. See Barbier, "Culmination of the Bourbon Reforms."

<sup>54</sup> See Allan Kuethe, "More on the Culmination of the Bourbon Reforms: A Perspective from New Granada," *Hispanic American Historical Review*, 57 (1978).

treasury, Viceroy Gil sent a letter to Madrid discussing the performance of the *Estanco*.<sup>55</sup> He informed the crown of pervasive consumers' complaints about the quality of manufactured products, and sustained that the monopoly had enormous bureaucratic expenses, which had to be reduced to improve performance.<sup>56</sup> The colonial elite shared this view. Hipólito Unanue, writing for the *Mercurio Peruano*, a magazine published by the *Sociedad de Amantes del País*, an enlightened and progressive organization in Peru composed mostly of members of the local elite, strongly criticized the poor quality of the state manufactures.<sup>57</sup>

Gil's diagnosis of the *Estanco's* performance was consistent with the crown decrees of 1787, which "...implicitly condemned some of Minister's Gálvez policies by stressing the need to economize..."<sup>58</sup> The Viceroy manifested his views more extensively in a subsequent letter to the crown:

"...selling the leaf cheaply and thereby increasing the quantity sold is the most advantageous step for the people and it is that which Your Majesty should take throughout the entire monopoly if Your Majesty wishes it to

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<sup>55</sup> In 1787, as part of the administrative changes that followed the death of Gálvez, the office of the viceroy regained power over economic matters, which had been taken away from the viceroys in the early part of the 1780s. Thus, the position of *Superintendente de la Real Hacienda* was terminated. Jorge Escobedo, who served as *Superintendente* in the Peruvian viceroyalty, and had supervised monopoly policies throughout most of the decade, left Peru in that year.

<sup>56</sup> Opposition to the state manufactories thrived in spite of the fact that the state did not change the prices of manufactured products. Prices of packs of cigarettes (of twenty four) and cigars (of six, eight or twelve, depending on quality) were set at a half real, which was the price at which artisans used to sell tobacco products. Nonetheless, the tobacco content of the state manufactures was lower than the typical artisanal production. Thus, in real terms, prices increased. Nominal prices were maintained throughout the decade. In letter Areche to Gálvez, No. 230, Lima, September 20, 1780; AGI, Lima 1230.

<sup>57</sup> Several additional sources confirm the poor quality of manufactured products in the late 1780s. Their bad quality was not only discussed in many of the viceroy's reports (and his assistants'), but was also documented by officials like accountant Trujillo who was a supporter of the state manufactories. See Hipólito Unanue, "Disertación sobre la naturaleza y efecto del tabaco, origen y progresos del Real Estanco de Lima," 1792.

<sup>58</sup> Barbier, "The culmination of the Bourbon Reforms, 1787-1792," *Hispanic American Historical Review* 57 (1977), p.59.

flourish without the need of hiring as many monopoly police. In order to successfully accomplish this, it is indispensable to achieve economy, good order, and simplicity.”<sup>59</sup>

Viceroy Gil ordered a *visita* (audit and investigation) of the monopoly in April 1790.<sup>60</sup> Soon after, in July of the same year, he reported to the crown that the *visita*, which was conducted by former director of the monopoly Feijoo de Sosa (1767-1774), was not favorable to the *Estanco*. According to Feijoo de Sosa, the main problem was the excess of inventories that caused the deterioration of a great quantity of tobacco in the factory’s warehouse, which, he argued, explained the inferior quality of tobacco manufactures. Tobacco leaf was accumulating at a high pace in the warehouse as a result of the monopoly’s relative success in the control of contraband in the production areas.<sup>61</sup> According to Feijoo’s report, there were other problems among which was the relatively low weight of the *mazos* of bracamoro tobacco.<sup>62</sup>

But Feijoo’s report overlooked a key issue that was at the heart of consumers’ complaints against the state manufactories. The inadequate quality of manufactured products was not only related to the excessive inventories of tobacco leaf at the factory’s warehouse, but also, and principally, to the substitution of domestic tobacco for imports.

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<sup>59</sup> Letter Gil to the Crown, June 1790; AGI, Lima 1243.

<sup>60</sup> Letter from Viceroy Gil to the Crown, April 30, 1790; AGI, Lima 1243.

<sup>61</sup> The excessive accumulation of tobacco leaf in the factory’s warehouse is consistent with S.R.H. Jones’ view on the relatively poor responsiveness attributes to changes in market conditions of the factory -as opposed to the putting-out system. Jones’ work focuses on British entrepreneurs in the eighteenth and nineteenth centuries. We should not expect any better from a state controlled monopoly. See S.R.H. Jones, “The Organization of Work,” p.127.

<sup>62</sup> “*Indice de los extractos que por la intervencion de visita del Real Estanco de Tabacos de Lima, se han deducido de las actuaciones originales de ella por lo respectivo a cuenta y razon y se pasan al excelentissimo sr. virrey de estos reynos. Anexo 3: Resumen de las sumarias informaciones recibidas por los señores intendentes de Tarma, Cuzco, Huamanga, Huancavelica y Trujillo, acerca del estado calidad peso y precio de los tabacos que se expenden en las capitales de sus distritos y en sus subdelegaciones, con arreglo a la comision conferida por este superior gobierno en 27 Diciembre, 1790. Habiendo obrado iguales actuaciones en las de Ica, Cañete y Chancay, subalternas de Lima,*” AGI, Lima 704. Also see *extracto no.5*.

The colonial state had engaged in an “import substitution” strategy experimenting with new tobacco fields that tried to reproduce Guayaquil and Havana tobacco as a result of the disruption of commerce during the crown’s involvement in the wars of American Independence. According to documentary evidence, the Peruvian *Estanco* failed to produce tobacco that could compete with the best quality imports. This fact explains, to a great extent, the relative decline in sales of cigars in the second half of the 1780s (see Graph 1).<sup>63</sup> The quality of cigars was badly affected for cigars used to be manufactured with imported tobacco from Guayaquil and Havana only, whereas cigarettes were commonly manufactured with domestic tobacco.<sup>64</sup>

As discussed above, in spite of consumers’ complaints against the state manufactures, the factory years yielded higher revenues than the period that pre-dated centralization. Nonetheless, the reports on the monopoly accounts given by the monopoly accountant, Fernando Trujillo, and Diego de la Vega (accountant of the *tribunal de cuentas*, who assisted Feijoo at the time of the *visita*) were inconsistent. Diego de la Vega’s report was far less supportive of the factories’ performance than Trujillo’s.<sup>65</sup> Based on the *visita*’s report, and arguing that the public outcry was for the closure, viceroy Gil abolished the tobacco factories. The Crown approved the judgment of the *visita*, the closure of the factories, and the destitution of Director Otermín in May

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<sup>63</sup> Vizcarra, “Markets and Hierarchies,” chp. 6.

<sup>64</sup> See Vizcarra, *Idem*.

<sup>65</sup> The analysis and discussion of the monopoly accounts lasted for a long time after the factories were abolished. In fact, the *tribunal de cuentas* and several high-ranking officials participated in the debate. Eventually, Trujillo’s accounts were vindicated. Among other documents: Letter Otermín to Gardoqui, Lima, October 23, 1793. Appendix: “*Documento esclareciendo...los errores y equivocados principios con que se pretende cubrir el lamentable estado de decadencia en que se halla la real renta del tabaco del reyno del peru de resultas del nuebo sistema que se ha adoptado para su manejo y gobierno,*” AGI, Lima 766.

24th, 1791.<sup>66</sup> This decision marked the relative downfall of the monopoly enterprise in the Peruvian realm.

## CONCLUSION<sup>67</sup>

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<sup>66</sup> Letter Crown to Viceroy Gil, May 24, 1791; AGI, Lima 1243.

<sup>67</sup> Forthcoming.

TABLE 1

## Level of Government Intervention in the Peruvian Tobacco Industry

	1752-1779	1780-1792 (Gálvez' Reform)	1792- Indep.
Planters	Planters needed license for production  Prices and quotas fixed by the colonial state, which became the only buyer	State keeps monopsony, it determines prices and quantities  Greater vertical control  Heavy regulations over planting and cultivation	Saña: Regulations back to original conditions (pre-factory)  Chachapoyas: Regulations for the most those of the factory period
Transport	State arranges transport with private carriers ( <i>arrieros</i> ) from factorías to government warehouses in urban centers	Same as in previous period	Saña: Producers arrange transport from factorías  Chachapoyas: Regulations of the factory period
Sales of Tobacco Leaf	The state monopolized the sales of tobacco leaf only  Leaf tobacco prices fixed by the state	All sales of tobacco leaf were restricted. Small quantities were sold at prices fixed by the colonial state	The state monopolized the sales of tobacco leaf only  Prices fixed by the state
Manufacture	Private licensed workshops	Centralization of manufacture, state factories produce cigars and cigarettes	Same as in the period 1752-1779
Sales of Cigars and Cigarettes	Sales by licensed stores	Final prices fixed by the state. Sales only by licensed stores	Same as in the period 1752-1779

\*Saña's planters arranged transportation to Lima until 1769. Vizcarra, "Markets and Hierarchies," p.14.

TABLE 2

Fiscal Revenues Viceroyalties of Peru and New Spain  
Annual Averages  
(Pesos)

Peru

Decade	Mining	Trade	<i>Tributo</i>	Tobacco Monopoly Revenues	Tobacco Monopoly Net Revenues
1750-59	178,438	453,722	350,210	325,164	141,246
1760-69	260,612	838,813	496,327	400,000	163,797
1770-79	309,843	794,619	278,895	410,000	186,989
1780-89	562,924	798,014	983,030	968,205	365,851
1790-99	867,219		1,076,197	906,113	368,271
1800-09	771,127		980,769	763,764	331,512

New Spain

Decade	Mining	Trade	<i>Tributo</i>	Tobacco Monopoly Revenues	Tobacco Monopoly Net Revenues
1760-69	2,506,034	1,535,808	782,210	1,560,261	611,493
1770-79	3,813,004	2,306,846	938,644	3,605,011	1,490,095
1780-89	4,305,094	4,775,696	1,103,705	6,221,068	2,839,445
1790-99	4,288,153	5,673,504	1,638,373	7,383,335	3,669,569
1800-09	3,359,589	4,906,414	1,986,223	7,766,753	3,454,758

Sources: Data for the Peruvian tobacco monopoly from Vizcarra, "Markets and Hierarchies," p.12. The rest from Klein, "The American Finances," and Deans-Smith, "Bureaucrats, Planters and Workers., Appendix I."

Graph 1



Source: Vizcarra, "Imperialists as Managers," p.23.

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