AN EMPIRE LOST: SPANISH INDUSTRY AND THE EFFECT OF COLONIAL MARKETS AND TRADE ON INNOVATION

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Job Market Paper

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Abstract. I study the effect of access to new (international) markets on innovation direction using two historical experiments on the textile industry in Spain at the end of the 19th century. I provide causal evidence on how trade structure enhanced biased technical improvements. Although each shock meant access to new markets to Spanish cotton textiles, their effect on innovation differed because the change on demand characteristics differed. First, after Spain effectively forced their colonies to buy manufactured cotton goods in 1891, I observe an increase in innovation destined to create cotton textiles. Second, after the Spanish-American war and the unexpected loss of these captive markets, I find a change inside the cotton industry towards weaving innovation. After the 1898 war, and with an already installed capacity, cotton industrialists were forced to enter and compete in the international markets that demanded more sophisticated fabrics. Using novel archive data from a big cotton firm, I evaluate the mechanism that explains my results. I show that changes in intermediate goods relative prices explain the type of innovation developed. Finally, I show that these new incentives on innovation translated directly into the adoption of new mechanized tools in the sector. In particular, I find evidence of increased industrial technology with a rise in mechanized cotton looms used in Spain after 1900.

JEL Codes: F15, F63, L16, N73, O24, O32

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"***Opening a new and inexhaustible market*** to all the commodities in Europe, it gave occasion to new division of labour and ***improvements of art***, which, in the narrow circle of the ancient commerce, could never have taken place for want of a market to take off the greater part of their product" - Adam Smith (1776), *An Inquiry into the Nature and Causes of the Wealth of Nations*

1. Introduction

Trade can affect in different ways economic development on those countries that gain access to international markets. For instance at the firm level, several mechanism would explain an observed positive relation between an exporting expansion and firm's productivity. In one hand, since trade might represent a transfer of knowledge from buyers to firms, exporting itself explains an increase on productivity of exporting firms (e.g. Clerides, Lach, and Tybout, 1998; De Loecker, 2007; Atkin, Khandelwal, and Osman, 2017). In the other, there is evidence that firms normally experience technological upgrading when they start to produce for international markets (e.g. Lileeva and Trefler, 2010; Garcia-Marin and Voigtländer, 2019). However, and despite the channel that explains the increase on productivity, there is few evidence on how the access to new markets changes the incentives that firms face to adopt and implement these technologies. In this paper, I argue that the opening and closing of foreign markets affects in several dimensions the incentives to develop new technology and the direction that firms follows when producing for those external markets.

International trade might not only affect the rate of technological change (see Rivera-Batiz and Romer, 1991; Grossman and Helpman, 1991) but also the type of technology that is going to be developed (see Acemoglu, 2002; Gancia and Zilibotti, 2009; Gancia and Bonfiglioli, 2008). In this paper, I document how access to different types of markets shaped the direction of progress. In the same way that input shocks (e.g. Hanlon, 2015), new markets affect the internal incentives for innovators. They choose among several possibilities the most profitable sectors to introduce new machines, and with sector differential access to new markets, those decisions might change. To do so, I exploit two unique historical experiments and the Spanish colonial context that vastly changed international trade patterns in the Spanish textile industry at the end of the

19th century. First, the extensive market integration between Spain and its colonies that effectively forced the latter to buy cotton textiles from Spain mainly. Second, the American-Spanish war that ended with the Spanish captive colonial markets and forced cotton producers to enter into new markets with different and more sophisticated tastes. Although both shocks gave access to new markets to Spanish cotton textiles, the nature of each one was different, and so were their implications on the adopted technology.

In 1891 Spain introduced an imperial protective tariff forcing colonies to buy cotton textiles exclusively from them. This policy had several implications. It reduced available cloth in the internal market when a shared of the production was oriented to the colonial markets. It also induced an increase in prices of cotton textile products relative to other fibers textiles. Jointly, the policy implied a change in innovators' incentives to develop new technology for the cotton industry relative to other textile industries. I document this behavior using patent data, and I show that the colonial trade induced innovation on technologies that augmented cotton fibers in all production stages. Moreover, I provide evidence that the change in relative finished textiles prices is the mechanism that explains the movements towards cotton innovation.

However, these conditions lasted only a few years, and they changed after the colonies' independence. With a significant installed production capacity and without a strong internal market, industrialists were forced to find new external markets after 1898. These new markets had different needs, and they demanded more sophisticated fabrics that required more effective weavers' use. In line with literature findings, Spain increase fabric quality after exporting textiles to richer countries (Schott, 2004; Hallak, 2006). Those new conditions implied an increase in the cost of producing at weaving stages that translated into a more considerable price per unfinished piece. That is a more significant innovations incentives to develop technologies at this production stage in contrast to other stages. Those new international consumers were more willing to pay for product quality than Spanish consumers, and this effect pushed innovation forces. Even more, those incentives did not vanish after considering the concerns of producing at a costly production section. Using patent data inside the cotton industry, I documented an increase in weaving technology patents after Spain lost its colonies. Also, I provide evidence that the change in relative prices of fabrics to other cotton products is the main trigger of this change. I use data from a big cotton firm (*La España Industrial*) to show that the prices of unfinished cotton fabrics increased relative to cotton threads. Finally, I show how relative wages inside the cotton industry changed in the presence of this biased technology upgrading. Because weavers and other workers in the production of textiles are complements, the increase of weavers cost did not fully translate in a reduction of weavers' relative demand. Therefore it meant a rise in the weavers' wages. I find consistent evidence of this hypothesis using wage information from this company. After 1903 I document a positive trend in the weavers payments in relation to spinners payments.

One caveat is necessary when interpreting these results. Spanish regulation allowed two types of patents. A patent of invention that protected new ideas and procedures, and patents of introduction that protected ideas never implemented in the country despite being developed and used in other countries. This system was not exceptional, and many peripheral countries adopted it during the 19th century aiming to facilitate technological transfers.(see Saíz, 2014). I use patent law to show that my results are motivated by real innovation and not just copying foreign technology. When I only analyze patents of innovation behavior, I reached the same conclusion when analyzing the whole patent sample. Therefore, I conclude that changes produced by trade structures affected incentives to create new production structures and ideas.

My results relate to many works on trade and development that analyze the behavior of exporting firms, mainly technological upgrading. Although I will not be able to document heterogeneous effects in firms after they got access to new markets (e.g. Clerides, Lach, and Tybout, 1998; Bernard and Bradford Jensen, 1999; De Loecker, 2007), I provide evidence on the internal forces the generate the incentives to create and adopt new technology. This literature did not answer how trade encourages innovation in firms and how new markets are important in the technology transfers. I strengthen my result by studying how these innovation incentives translated into technology adoption of textile firms. Previous literature have documented positive effects on new technologies' adoption due to trade agreements (Bustos, 2011; Lileeva and Trefler, 2010) or temporary trade protection (Juhász, 2018). I complement this literature suggesting that general trade competition also produced a change in the machinery levels of the industry. I find an increase in installed mechanized looms in the short run. Using local tax data, I find an increase in cotton weaving machines compared with other textile industries after Spain lost its colonial captive markets. I hypothesize that this change is related to the increase in weaving innovation observed during the same period.

Also, my findings relate to the literature on directed technical change. In particular, the empirical works that document the behavior of innovation under different shock types (Popp, 2002; Hanlon, 2015; Aghion et al., 2016). I contribute by looking at another kind of shock. While this literature has well documented the effect of input shocks on innovation, this paper studies a shock on the output market. Even though the shocks are analyzed under the same theoretical background, their nature and implication are not the same. I show that even two changes that meant access to new markets to cotton textiles, they translated into different movements on the technology directions. Following previous literature, I use a clean historical experiment, and I take advantage of the exogenous and surprising shock that both the increase in tariffs and the war represented.

Finally, to my knowledge, this is the first paper showing how imperial possessions' presence influenced technical direction. I review how Spain responded to exogenous changes to the trade relations with its colonies. I draw on the extensive literature on Western European colonialism that searches for the effects of this policy on both the colonized territories and the societies that did the colonizing. In particular, I build on the previous literature that asks how European extracted benefits from their colonial empires (e.g. O'Brien and Escosura, 1998; Findlay, 1990; Butel and Crouzet, 1998). It has been suggested that the interaction between slave trade profits (Williams, 1944) and the expansion of colonial commerce (Inikori, 2002) helps to explain the rise of Western European societies during the 17th and 18th centuries. However, and despite the interest in the relation between North Atlantic trade and growth (Davis, 1973), there has been little empirical evidence on the actual process of how trade affected economic development in western societies. Following Davis and Huttenback (1982, 1986), I show that the benefits of the imperial enterprise were not equally distributed along with all economics sectors. I provide formal empirical support of a channel that has not been studied before: trade's effects on innovation incentives. According to this literature, commerce created a unique price and wage structure that modified incentives and allowed the technological breakthroughs of the 18th century in Britain (Allen, 2009, 2011). I contribute to this literature by studying the related mechanisms and broadening the study beyond the British empire. I look at the effects of trade and innovation on the technological periphery. In this work, I suggest that even in the presence of not the best institutional environment (Acemoglu, Johnson, and Robinson, 2005) colonial trade was able to induce the growth of some economic sectors

2. Background

2.1. **Spanish cotton industry.** Cotton has been one of the most important industries in the world. Indeed, during the 18th century, European empires used cotton as a platform to create new industries, a launching pad for the Industrial Revolution (Beckert, 2015, pp.xiv). Spain was not the exception, and the cotton textile industry was one of the few modern industries with relative success in the country. During the second part of the 19th century, it was one of the first industrialized sectors in a period characterized by industrial productivity growth due to the incorporation of new ideas and technologies (Carreras, 2006). Textile industry represented 1.7%[1] of the entire country's tax value (compared with 4% of industrial values) and the cotton textile employment was around 4% of total employment (29% of the total employment on the main industries)[2].

After the shock on raw input global markets produced by the American Civil War, the Spanish cotton industry had several distinct features. First, the sector relayed completely on raw material imports[3]. Second, although with the presence in different areas, the industry was concentrated in Catalonia due to geographic advantages and historical changes one century before[4]. Third, most of the production was performed on vertically integrated firms in which both spinning and weaving mills were under the control of the same firm[5]. Fourth, although the market was dominated by large firms[6], relatively to other countries in Europe, the size of the industry was small. Finally, firms used piece payment on both spinning and weaving production. Like in technological leaders such as England or the American North, those payments remained unchanged during the last part of the 19th century. When facing external shocks, firms adjusted on output, hours of work, or employment (Domenech, 2008).

Those characteristics were direct results of the internal market characteristics the industry faced. The heavily protected agricultural output sustained internal demand, and therefore it was small and volatile. Unable to support more prominent firms and more considerable savings through economies of scale, the cost structure remained high

[1]Based on the payments on industrial taxes Nadal (1987) in 1856. This value was not bigger than any other individual industry. The comparable industries were just a half of the value.

[2]Based on the Giménez y Guited (1862)'s study for the main industries in Spain in the most relevant provinces in 1860. The whole textile employment represented more than a half of industrial employment, including wool industry (14% employment), silk industry (4.8%), and linen industry (3.5%).

[3]There were some minimal experiences in raw cotton production, such as in Motril (Granada). Still, they were unable to fulfill the industry demand, and they disappeared during the second half of the century (Martín, 2018).

[4]An agrarian crisis in Catalonia between 1770-1775 forced capital to move into the production of cotton textiles due to the increase on agricultural wages and reduction of rents. Moreover, the presence of rivers and mountains provided industrialists with a valuable power source to move mills without relaying into other external sources such coal (Nadal, 1975).

[5]According Rosés (2009), in 1860, 60% of spinning production and 69% weaving production was made in integrated firms.

[6]Rosés (2009) estimated that in 1860 both spinning and weaving were dominated in more than 60% by firms producing more than 100 output tons per year.

in comparison to the global market leaders (Nadal and Sudrià, 1993). To survive, firms followed a different strategy: protecting the internal market and capturing external markets.

2.2. **Colonial markets, tariffs and the war.** After losing all the continental possessions in America during the first half of the 19th century, Spain accomplished, although with hardship, to maintain some territories such as Cuba, the Philippines, and Puerto Rico (besides some other small possessions in Africa and the Pacific). After the first Cuban independence war (1868-1878), there was a renewed need to formulate the relation between the metropolis and the colonies. There was a tension between the Cuban sugar entrepreneurs' need for free trade and Catalan cotton industrialists' need for colonial market protection. The solution was a middle position. Despite the textiles lobbies did not achieve a high protective tariff, they reached a change in the trade policy toward the colonies[7]: the Antillean colonial markets and the metropolis started to be considered as a single market. The *Ley de Relaciones Comerciales con las Antillas* in 1882 established a gradual yearly reduction of tariffs between the colonies and Spain for ten years that would end with the complete elimination of trade barriers between the two territories[8] Even imperfect, after this change, Spanish textiles found a market to overcome the internal market limitations.

The real protection and market capture came in 1891 with the rise of a protectionist tariff (known as *Canovas Tariff)*. Original though as a starting point to future negation to reduce French tariffs to Spanish wine, high tariffs for industrial products remained high when negotiations failed (Sabeté-Sort, 1995). In practice, there was an effective market integration with both the reduction of the barriers between the colonies and the extremely high tariffs after 1891. In this system, colonies were forced to buy the overpriced metropolis' products (Nadal and Sudrià, 1993)[9]. However, the benefit did not last much. In 1895 Cuban independence movement gained force after a general

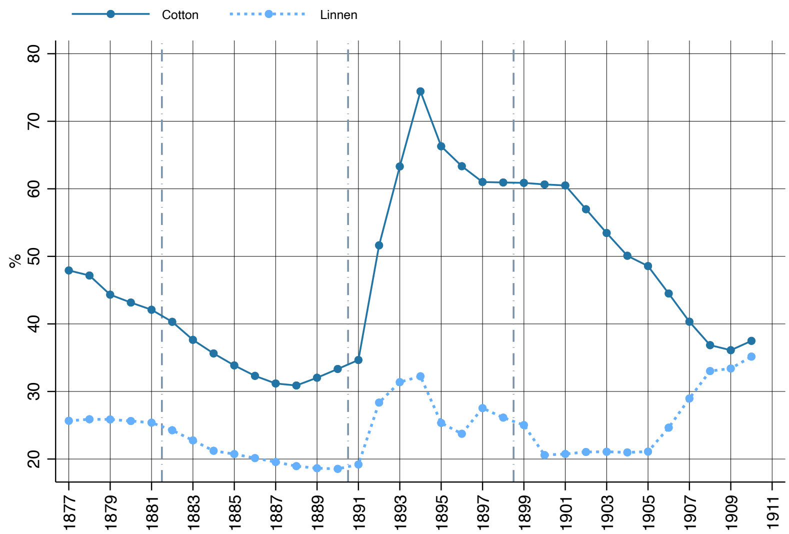
[7]The tariff system did not include a protective tariff to industrial products. The system was a result of negotiation with other European powers in exchange for low tariffs to Spanish agricultural output such as wine and flour (Nadal and Sudrià, 1993).

[8]The law established a yearly reduction in the original tariffs of 5% during the first three years, then a reduction of the 10% in the following four years and then a reduction of 15% in the remaining three years until 1891.

[9]This is not a particularity of Spanish colonial policy. Beckert (2015) reports several cases in which the industrial policy was the use of colonies as a captured market for textile industrial outputs. For instance, England used this strategy to displace Indian textiles from global markets during the late 17th century. Belgium had a boost on the industry during the Great Netherlands period thanks to the access of Dutch colonial markets on the pacific.

disappointment with Spanish policies (Zanetti, 2013)[10]. This movement ended in 1898, with the loss of the colonies and therefore the loss of protected markets for Spanish cotton textiles[11].

FIGURE 1. **Textile tariffs**



Source: Dirección General de Aduanas (1876-1898, 1899-1911)
Notes: Tariff measure as the fraction of total tariff revenues on import value. Cotton tariff is measured as a weighted average on tariff on plain-woven and twilled woven fabrics either unbleached, bleached, or dyed on 2 different quality grades. After 1906 the cotton categories also include different fabric weights, and I have ten other quality groups. Linen tariff was measured as a weighted average on tariffs on plain-woven and twilled weave fabrics on three different quality grades (4 after 1906). Imports' weight in each category is used to assess the importance of each category when constructing the series. In both cases, I show the two years moving average of the raw numbers.

Figure 1 shows the tariff evolution of basic textiles in Spain between 1878 to 1910. I include two of the fibers that, due to their characteristics, can fit the colonial market's necessities: cotton and linen[12]. Cotton textiles in all the period had greater protection than linen textiles. Before the introduction of the protective tariff in 1891, there was

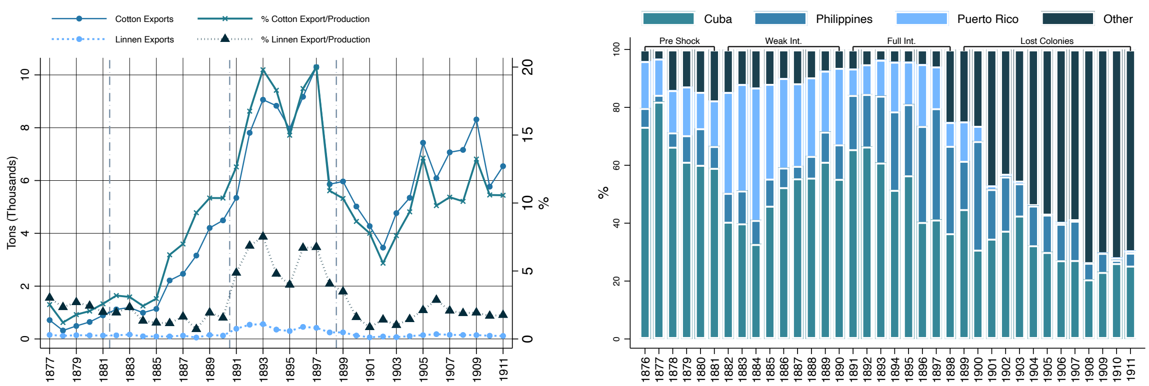
[10]For instance, trade policy was not reciprocal. Spanish exported a considerable amount of products to the colonies, while the colonies' main market was not the metropolis. According to Zanetti (1998) in 1978, United States were 82.5% of Cuba's exports destination

[11]Despite some proposals of autonomy (that found opposition among the textile sector), after the United States quick intervention, Spain lost its last colonial possession in America and the Pacific. See Heraclides and Dialla (2017) for a detailed explanation of United States intervention in Cuban and Philippine independence movement.

[12]Due to the tropical location of the colonies, the need is for breathable summer fabrics. Other fabrics like those made of wool and silk do not fulfill this requirement completely. For instance, in 1895, Cuba imported a minimal amount of wool and silk manufactures. In that year, Cuba received 11,796 tons

a reduction trend on textile tariffs[13]. However, this pattern changed with the new protective tariff system. Cotton tariff doubled in the period and remained around 60% while the linen tariff increased by a half and remained around 30%[14]. I exploit this fact in my analysis, and I use linen and other fibers as "control" group to get a sense of the behavior of textiles without an extensive market capture.

FIGURE 2. **Cotton textiles export**



A. Cotton textile production and exports **B.** Cotton textile destination

Source: Same as figure 1 and Ministerio de Agricultura, Pesca y Alimentación (1929-1935)
Notes: In Panel A, I estimate available raw materials' weight adding average yearly cultivation yields between 1929 and 1935 to total raw imports weights for each year. I estimate textile production based on this raw material weight following Sudrià (1983). I calculate available raw material two years average and assume a 25% weight reduction during all production stages. I show the two years moving average of the raw numbers. Panel B shows the destination market share, highlighting the share of main colonies. Figure D.2 in the appendix, Panel A shows detailed desegregation of cotton textile export destinations besides Caribbean and Pacific colonies.

Figure 2 shows how the tariff regimen translated to exports volume and destinations. Cotton production and exports were very similar to their linen counterparts before 1982. Cotton production and the share destined to exports started to grow similarly after the trade barriers reduction in that year. With the protective system in 1891, the share of production destined for exports in both sectors significantly increased. For cotton, it reached a maximum of 20%, while for linen, this value was around 8%. However, the behavior of the export was different between the two types of fibers. In

of linen textiles and 4,932 tons of cotton textiles, 312 tons of wool textiles, and 19 tons of silk textiles (Dirección General de Hacienda, 1894-1895).

[13]This in line with the literature that emphasized that the protection aim on this period was to protect the agricultural sector.

[14]This is even less than the cotton protection before 1891.

the cotton case, the exports growth had a similar pattern to the share of exports. It shows an increasing capture of the colonial market with new production[15]. In terms of destination, even before 1891 (and 1882), colonial markets represented more than 90% of the total exports markets (Figure 2 Panel B)[16]. This market got lost, and the exports to those markets decreased dramatically. In 1898 they represented more than 90% while ten years later those values fell to around 20%[17]. This confirms my decision to use other textiles industries as control groups since they were not highly affected by the trade policies in comparison to cotton[18].

2.3. **Market lost.** Colonies gained back the trade freedom they lost to the metropolis, and Spain industry had to compensate for this loss. According to Nadal and Sudrià (1993) some characteristics were the constant of the industry during the first decade of the century: the significant presence of female and child labor and the wide variety of produced fabrics. Both were strategies to reduce costs and to gain access to new markets. First, women and children were a cheaper labor source, and according to Smith (1991) it was a deliberate strategy on weaving sections to reduce costs. Second, the wide range of fabrics types allowed the firms to reach a greater amount of buyers despite the cost on productivity that it represented[19].

The final strategy adopted in Spain was the increased protection of the internal market, although it came late in 1906. This tariff system extended the classification categories, which according to (Sabeté-Sort, 1995), in practice, represented a relative increase in the tariff for high-quality textiles against low-quality textiles. Figure 1 shows this pattern. After the 1898 war, cotton textile protection decreased while linen protection increased. Nonetheless, this only policy cannot explain the industry recovery that started before this tariff system change. This is the argument of this work; an

[15]Contrary to linen exports that did not increase in the same proportion, showing relative constant production levels and a replacement of the internal market. Even more, in 1895, according to Dirección General de Hacienda (1894-1895) the cotton imports in Cuba from Spain represented around 70% of the total imports weight while the linen imports from Spain represented only 31% of the total import weights.

[16]The only change that 1891 tariff reform represented was a change in the internal compositions. After 1891 there was an increase in the exports to the Philippines.

[17]This is contrary to linen textile markets. Market share of colonial markets returned to the previous values around 40% (See. Panel B appendix figure D.1).

[18]Actually, figure D.1 (Panel A) shows that non of the other textiles sectors were comparable with any cotton product type when looking exports to colonial markets. Colonial trade of silk, wool, or linen was minimal in value, and they were far below any category of cotton textiles.

[19]Without specialization, large economies of scale were impossible. Moreover, the constant change in machines and techniques required more number of loom workers (Nadal and Sudrià, 1993).

insertion on global markets requiring new technologies to produce new fabric types explains the industry's recovery.

Jointly with this internal work, firms began a fight for international markets to replace the ones lost after the war. Figure 2 shows that despite the small reduction in exports during the first years after the war[20] this variable grew and it remained on the general values after 1891. Two facts explained this behavior. First, the search for alternative markets that found a good replacement market for cotton textile products in the American republics (Pane A appendix figure D.2) and other European powers (on less degree). Second, the change in exported fabrics' quality. Spain completely stopped the exports of white textiles. It increased the production and exports on more valued-added fabrics[21] like dyed, printed, double fabrics and knitted fabrics[22] (Pane B appendix figure D.2). That is, even on a small scale, Spanish industrialists looked to compete on the global market on more specialized products[23].

3. Theoretical Framework

Several authors have built theories of international trade and the effects on innovation (see Acemoglu, 2002; Gancia and Zilibotti, 2009; Gancia and Bonfiglioli, 2008). When directed technical change is endogenous trade and international markets affects the direction in which technology is developed. These are some of the key features of the theory (see appendix section A for a complete review of the model). The theory focus on two sectors that can represent cotton textiles (Z) and other fibers textiles (X). Intermediate goods and machines combined produced each one of the textiles. Both machines and intermediate goods (raw fibers are transformed into those goods using an independently cost structure) are specific to each sector. I am interested on the machines since they represent the available technology in each sector and the number of them (A_i for the numbers of machine in the secotr i) measures each sector's innovation degree. Machines developers hold an infinite patent on the machine and sell them on a monopolistic market to textile makers after producing it at a marginal cost. Developers must pay a fixed cost to enter into the market and decide then in which sector invest taking into account the whole discounted profit stream of producing each

[20]This despite the peseta's value lost after the instability produced by the war.

[21]Appendix D.1 also showed that imports to colonial markets did not disappear completely. Export values of sophisticated fabrics remained high at the same value before the market integration periods.

[22]In 1895, most of the cotton textiles entering Cuba were textiles of low quality (around 50%). This included textiles with a low number of threads and without any additional processing.

[23]This was not a unique Spanish feature. Beckert (2015) account recorded evidence in several countries with similar experiences. For instance, the Ottoman industry took advantage of cheap input products and catered a highly differentiated weaving output markets (p. 331 Beckert, 2015).

machine type. Their profit is then affected by market structure of each sector and the demand for their machines from textile producers. Then the innovators when deciding in which sector introduce a new machine will choose the sector that gives them more returns. I will analyzes then how each particular trade shock affect the market structure and therefore the incentives to expand the machines in each sector, through changes on the profits that innovators can make on each sector.

Spain patent law allowed the introduction of innovations already patented in other countries. That is, it allowed imitation of foreign ideas. Under this framework the ideas developers have to include into their consideration technology overseas. Gancia and Bonfiglioli (2008) show that even in this case local conditions determine the technological levels adopted on the non-technological leader country. I argue then that the conclusions an expectation I develop in this section apply since there were not perfect replication of foreign technology in Spain. Although there were not total barriers to overseas technological adoption, the Spanish markets conditions were still affecting the decision of local innovators when they decide the type of innovation to develop.

In the case of the market integration I am assuming that the change in innovation incentives is trough prices of the intermediate goods. When Spain forced their colonies to buy cotton textiles the prices of these manufacture goods increase after the production leave the country to the colonies. That is, raw cotton relative to other fibers was scarcer in the integrated market than in Spain. Since innovators are selling on a monopolistic markets their machines, the increase on prices in the cotton sector is also translated on increase on the profits they can make selling the machines to this sector. This leave the following prediction

Prediction **1.** *When technology is fixed, cotton textiles relative price increased after the protective tax and the market integration. Due to this increase on cotton relative prices, there were an increase on patented machines to process cotton (A_z) relative to the machines to process other fibers (A_x).*

The case of Spanish textiles entrance into the competitive global markets is more complicate. There are two sectors inside the cotton industry, producing intermediate goods using two different types of labor: weavers (L) and other type of workers (H). In this case innovators are choosing between introducing machines into the weaving sector that uses weavers or other sectors of production. With the entrance to the new markets and with different tastes the cost to use weavers to produce intermediate goods increased. Under these new conditions firms needed to expand their variety range and it represented an increase on the cost to use a weaver that have to work on more sophisticated fabrics[24]. This change translated directed on prices of fabrics that became more expensive to produce. This meant more incentives to the innovators to develop machinery for this more costly sector. However, since weavers are costly to use the producers of these goods are now less willing to produce in this sector, or what is the same, there were less space for innovators to develop technology for the weaving sector. I have then two contradictory forces that produce an ambiguous conclusion on the direction of the expected innovation. However, these two sectors are complements in the production of a single product (cotton textiles) and the reduction of the willingness to produce in the weaving sector are not a big concern and the positive effect on incentives due to the increase on prices remained. This leave the following prediction

PREDICTION **2.** *When technology is fixed, after the entry to a new market, where tastes were different, weavers got relative scarcer and the price of fabrics also increased. Since weaving and the other stages of production are complements the increase on the fabric relative prices motivates innovators to introduce machines to weaving. Then, there were, an increase on patented machines for weaving (A_l) relative to machines needed in other sectors (A_h).*

4. DATA

4.1. ***Patents.*** I use patent data to study the central concept I want to study in this paper: innovation. The patent data I use comes from the work made by Saíz et al. (2008). These authors worked directly on the original documents containing historical patent applications[25]. The source is the government office in charge of patents historical archives, Oficina Española de Patentes y Marcas (or OEPM, for its Spanish acronym). I work with all patents registered in Spain[26] in the period between 1978 and 1911[27]. I scraped the OEPM website to get access to the basic characteristics

[24]With more varieties to be produced weavers cannot specialized and the same machine must be used on the production of several type of fabrics. This requires more time on the preparation and to stop productionin order to change the arrangements when producing each different fabric.

[25]In some cases, these authors only worked with administrative records since some inventors used to retire more detail descriptive documents at the expiration period of their patents.

[26]I exclude from my analysis any addition made to previously registered patents.

[27]During this period, there were no significant changes in patent legislation. Actually, the Spanish patent system changed significantly in 1878. A law in this year modified 1826 law. It introduced, among other things: a new payment system based on progressive quotas, the possibility of patents protection to foreign inventors that have already patented the invention overseas, and a more rigorous procedure to verify that the protected idea was implemented. Besides some complementary laws orientated to regulated specific matters, there was a new significant law in 1902. However, this law did not change the previous regulation spirit significantly, and it only modified minor issues to manage

of the patents: application's date[28], patent's description, applicant's name, place of residence and occupation, patent duration and type patent[29] and information whether the applicant implemented patented idea.

This dataset classifies patents according to the International Patent Classification (IPC). This hierarchical classification allows me to identify to some degree the technology behind each patent. The table in appendix E.1 presents the technology classification of textile patents, showing all technological subcategories in which there was at least one application between 1878 and 1911[30]. In the main analysis, I use two patent features. The first characteristic I exploit is the ability to use the patent on the production of cotton textiles. I reviewed all the registered patents and divided the patents categories into those machines and ideas applicable for cotton and those that are only applicable to other materials. I label a patent as cotton related if the patent description mentions as its main purpose the process of either general fibers and fabrics or cotton and fabrics made with this fiber. A non-cotton-related patent is a patent designed for different fibers and fabrics made exclusively with those fibers. The second characteristic I exploit is the use of the patent at the weaving production stage. For that, I use the three subcategories under the "Weave" IPC classification, adding the knitting subcategory[31]. In my analysis, I compare the behavior of the cotton patents in these four categories with the remaining 27 categories. Therefore, I use 62 technology-material categories to compare the number of cotton-related textile patents against textile patents related to other materials besides cotton in the market integration period against the pre and post periods.

4.2. ***Textiles wages and prices.*** I evaluate the effect of innovation on relative wages and textile prices using data I collected from a big cotton textile firm located in Barcelona: *La España Industrial*. I gathered price information from inventory ledgers. I included different industrial products such as thread, unfinished fabrics (output after

the system according to new realities. See Saíz (1995) for a detailed history of the Spanish patent system.

[28]I follow (Hanlon, 2015) using applications date since, as highlighted by this author, it allows me to focus on patents at the early stage of patenting and without any concern for differential speed during the granting process.

[29]That is if the patent was a patent of invention or patents of introduction

[30]Since the classification was created in 1970, some patents do not fit in a single category or concept in the classification. I assigned the patent as a textile patent to solve this problem if one of these classifications was related to textile production. In the case of a textile patent categorized with several divisions, I assigned it to the classification of the patent's primary purpose after reading the patent's description.

[31]I included knitted fabrics since those were a significant proportion of textile export after 1898 representing the shift towards high quality-value textiles I want to study.

being woven), and finished fabrics. The firm produced several different fabrics and threads, so I recorded information on several types of qualities that the firm constantly produced for a long time. I gathered the information for three types of threads: warp thread without size, warp thread with size, and weft thread. For each of these cotton thread varieties, I recorded the price for the different product qualities available in the inventories. Also I gathered information for two type of unfinished fabrics: *molesquin* and *madras*. As in the thread case, I recorded the price for all the products qualities of these two fabric types available in the inventory. I chose these two types of fabrics since those were the only ones that the firm constantly kept on the inventories during my period of interest (1880-1910). Finally, I gathered the information for a single type of finished fabric: *percalina superior lisa*. I needed comparable information through the years, and this type of cloth offered me the longest available series since the firm kept them on the inventories between 1877 and 1907. For wages, I use information from payroll ledgers. I collected information from weekly payments on spinning and weaving mills between 1880 and 1910 for four weeks in the year (weeks 1, 14, 27 and 40)[32]. The information includes, besides the total amount of wages paid during the week, the total number of workers on each section and the total number of pieces (for fabrics) or kilograms (for threads) produced. It is important to note that I do not have information on spinning mills during 1888-1890 since the firm completely stopped thread production during those dates.

4.3. ***Machines.*** I also look at the impact of innovation on mechanization and machines acquisition using data I gathered from industry and business taxes reports payments (see Dirección General de Contriuciones, 1879, 1893-1894, 1895-1896, 1900-1909). I expect that the change in innovation would be reflected in shifts of mechanization patterns in different Spanish regions. Even imperfect, this is the best available measure of machines used in several textile industries. First, the reports do not entirely cover my period of interest, and sometimes they cover two years of contributions. I recovered information for the following years: 1879, 1893-94, 1895-96, and yearly from 1900 to 1909. Second, tax evasion and fraud was an extended problem in Spain during the 19th and 20th centuries; therefore, the number of machines and taxes paid over them represent only a fraction of the real capital employed on those industries[33]. Therefore, the analysis using this data is only a lower bound of the real effect, and it is valid

[32]When the information was not available because the firm stopped production on that week, I extracted information from the closest available week that has production information.

[33]Moreno Lázaro (2015) identified an extended fraud in flour mills. He estimates, on average, revenue losses around 40% to 60%. See Comín (2018) for detailed information about this practice in Spain.

if there were no differential changes on evasion across industries. From this source, I collect information about different machines (such as mechanical and manual looms and spindles) used in three different textile industries: cotton, wool, and linen (hemp) industry[34]. In my analysis, I compare the patterns of mechanization on 45 provinces[35] between different fibers industries and on a different stage of production. While in 1879 most of the provinces had the presence of linen and wool industries (only three did not report any machine working with these fibers), cotton machines were located in 20 provinces and most of them on the coast (see appendix figure D.3)[36]. This situation changed, and the industry grew beyond these natural borders. Many provinces recorded the presence of cotton machinery after 1900 (only three provinces did not report the presence of cotton machines).

4.4. ***Other data.*** I complement this data with a large dataset on provincial demographic characteristics recovered from the 1877 census (Derección General del Insituto Geográfico y Estadśtico, 1877). I use the information on population, number of men, number of regular residents, number of single and married individuals, number of people identified as catholic, number of illiterate people, number of the population born in the same province, and the number of regular residents in the same municipality. The goal of this data is to control for characteristics that might affect the development of textile industries. Table E.2 in the appendix shows that the presence of the cotton industry in 1879 was not related with most of the province characteristics except with a lower proportion of the illiterate population.

5. Technical Change

5.1. ***Empirical Strategy.*** The first main idea I investigate in the empirical work is the effects of colonial-metropolis market integration on the cotton industry innovation. I exploit two variation dimensions: the existence of textile industries that colonial market integration did not affect and the timing in which the integration took place

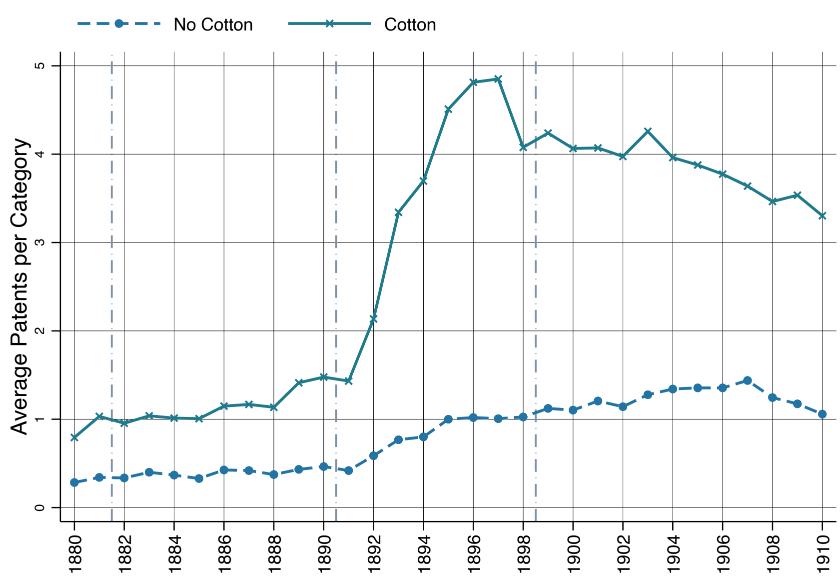
[34]I do not include information about machines used on mixed-material fabrics and stages in which it is not possible to identify the type of textile such as textile bleaching.

[35]*Privincia* is an administrative division of Spain territory. The system had its origins in 1833, and it did not have any significant change during the analysis period. The tax payment reports did not cover some territorial regions, such as the provinces belonging to the Basque Country (Vizcaya, Álava and Guipúzcoa) and Navarra that were under a different tax system during my period of interest. Also, I do not include Canarian Islands regions since they never reported a machine on textile industries during these years.

[36]The strong international orientation of cotton textiles and the lack of good communication roads help to explain this location decision close to ports.

between 1891 and 1898. My strategy is then based on a *difference-in-difference* approach. I use data on patents in 31 technology categories on all textile production stages and two material categories (i.e., whether the patent is related to cotton or not).

Figure 3. **Cotton related and no-cotton related textile patents**



Notes: This graph shows the evolution of textile patents for both cotton and non-cotton-related patents. In both cases, I show the two years moving average of the raw numbers.

Figure 3 shows the average number for both cotton and non-cotton-related patents per technology category in all production stages between 1878 and 1911. During this period, there were more cotton-related patents registered in Spain compared with non-cotton-related patents. Before market integration between Spain and its colonies in 1891, both patent categories had similar behaviors, and both counts did not significantly increase. However, cotton-related categories had a sharp increase after 1891. This increase was constant, and in 1897 the number of cotton-related patents reached a value five times greater than in the period before the market integration. After the American-Spanish war and the loss of the colonial markets, this patent count began to decrease, although it never reached previous market integration levels. This is consistent with theory predictions since it shows that there was a change towards technologies related to cotton textiles production during the market integration period.

Formally, I estimated the following equation after aggregating the data into eight periods of 4 years each one[37], where subindex j denotes technology-material category and subindex t denotes period.

$$Pat_{jt} = \sum_{k \neq [1879-82]} \beta_k (\text{Period}_k \times \text{Cotton}_j) + \alpha_t + \alpha_j + \varepsilon_{jt} \tag{5.1}$$

where Pat_{jt} is the count of patents and Cotton_j is a dummy that takes the value of one for technology categories related to cotton. α_t and α_j are time and technology-material fixed effects that capture any time-invariant category characteristics and any aggregate time shock, and ε_{jt} is the error term. The key coefficients are β_k that capture the differential change between each period k[38] and the baseline period (1879-82) in the number of cotton related patents relative to the change of non-cotton related patents. The identification assumption is that the number of cotton-related patents would have behaved similarly to the number of non-cotton-related patents in the absence of market integration. I provide evidence that this assumption is plausible using the comparison with weak integration periods. I expect a zero effect since there was a gradual reduction in tariffs between the colonies and metropolis but not an effective integration because colonies were still allowed to trade with other foreign powers.

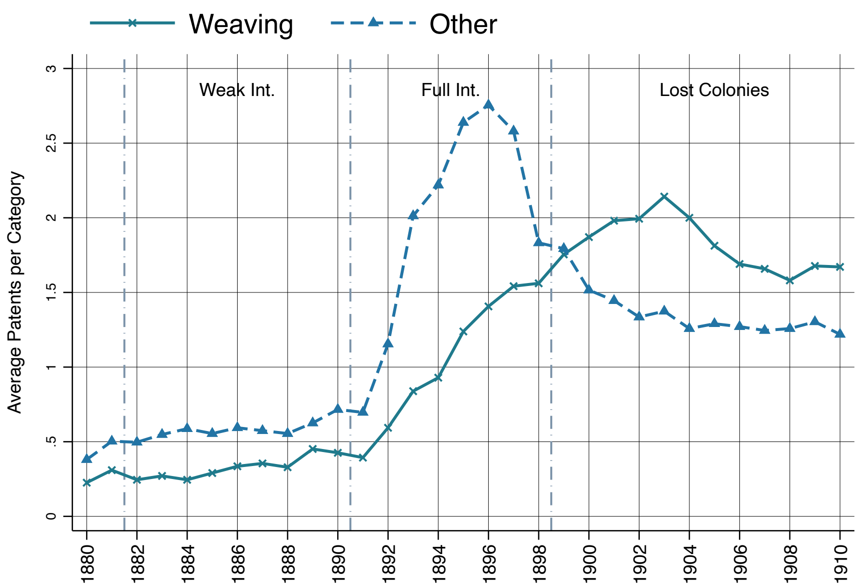
The inference is an additional challenge when conducting this analysis. Due to the small number of observations and panel units, I cannot rely on standard inference approaches that use asymptotic and model assumptions. I use a randomized test to derive significant conclusions. First, I randomly take one group in each technology category pair and treat it as a cotton-related technology. Second, I randomly shuffle

[37]To analyze the data formally, I have a panel of 32 years for 62 technology-material categories. However, this panel structure arises several challenges when applying standard econometric methods (see Hanlon, 2015, p. 83 for more details on these issues). Then following this author, I use a similar aggregation strategy. With this strategy, I deal with truncation problems in some technology series that show zero patents in different years (although I am not able to eliminate all zero counts) and serial correlation errors that generate bias on the standard errors estimation (Bertrand, Duflo, and Mullainathan, 2004). Actually, according to the table in appendix E.3 panel B, there is evidence of serial correlation presence in the data that is partially solved when using this strategy. When applying a Q-stat Born and Breitung (2016) biased corrected test to a yearly model similar to equation 5.1 (column 1), I can reject the null hypothesis of no serial correlation of order 1 or 2. In contrast, I cannot reject the hypothesis using the 4-year aggregated data (column 2). However, the evidence is ambiguous. Using the LM portmanteau test for serial correlation developed by Inoue and Solon (2006) there is some evidence of serial correlation on my model. With four years of aggregated data, I can eliminate some zeros in the series yet preserve time structure that I can use to test dynamics effects.

[38]The periods are:weak integration (1883-86) and (1887-90); full integration (1891-94) and (1895-98); and lost colonies (1899-1902), (1903-06) and (1907-10).

the periods and treat them as the period assigned. I use 20,000 different realizations combination of these randomizations and estimated placebo coefficients. Under the null distribution of no effect on cotton-related pattern and same time effect on both material categories, how treatment and time are assigned does not matter. Any of these randomization assignments would not change the outcomes observed[39]. I construct both p-values and confidence intervals to derive conclusions. To calculate confidence intervals, I follow Garthwaite (1996) using an efficient search algorithm[40].

Figure 4. **Cotton textile patents per category by stage production**



Notes: This graph shows the evolution of cotton related textile patents for weaving and other production stages: thread, spinning and yarn treatments and textile finishing. I show the 2 years moving average of the raw numbers for each series.

[39]This is a similar approach used by Hanlon (2015). However, I also randomized over the period. This allows me to test the hypothesis that differences in the pre-shock periods do not drive the effects estimated.

[40]Randomization tests have the advantage of relying on few distributional assumptions, however finding CI is computationally costly. In theory, the calculation involves searching over a grid of possible treatment effects using the randomization distributions to calculate a p-value under the null hypothesis that the treatment is equal to each value in the grid. Then the calculation involves choosing the lowest and highest value in the grid with a p-value of 0.05. (Garthwaite, 1996) proposed an efficient search process independently for each endpoint of the confidence interval. This procedure reduces the search dimensionality. Instead of using the whole randomization distribution for every single possible effect, the algorithm uses a single randomization in each search step. I follow the author's suggestions regarding the starting point and the length of the search.

The second main idea I investigate is the effect of colonial markets lost and further competition on international markets on cotton industry innovation at the weaving stage. In this case, I exploit three variation dimensions: the existence of textile industries that colonial market integration did not affect, the timing in which competition on international markets started after 1899, and the presence of 4 out of 31 technology categories classified as weaving and looms. The approach is then a triple difference model in which, besides the previous comparison, I exploit in the *difference-in-difference* approach; I compare the additional effect on cotton-related textile patents at the weaving stage with other cotton-related patents at different stages.

Figure 4 shows the average number of cotton-related patents per technology category desegregated by textile production stage between 1878 and 1911. The number of patents in each one of the production stages remained relatively unchanged before the market integration period, and the patents in all the categories started to grow after 1891. However, after the colony lost in the 1898 war, the patents number began to decrease in all production stages except for weaving. After the loss, patents at this stage continued growing, and the numbers never reduced below the level reached during the market integration period[41]. This is again consistent with theory predictions. It shows that the effect observed during the market integration period on cotton-related patents is exclusive to this period. During the lost colonies period, competition positively affected international markets on cotton patents at the weaving stage.

I follow the same strategy as in the *difference-in-difference* model and aggregate the data in 8 periods of 4 years[42], and I estimate the following equation:

$$\begin{aligned} Pat_{jt} = & \sum_{k \neq [1879-82]} \gamma_k^1 (\text{Period}_k \times \text{Cotton}_j) + \sum_{k \neq [1879-82]} \gamma_k^2 (\text{Period}_k \times \text{Weave}_j) \\ & + \sum_{k \neq [1879-82]} \gamma_k^3 (\text{Period}_k \times \text{Weave}_j \times \text{Cotton}_j) + \alpha_t + \alpha_j + \varepsilon_{jt} \end{aligned} \tag{5.2}$$

Weave_j is a dummy that takes the value of one for technology categories at the weaving stage of production. In this case, the key coefficients are γ_k^1 that capture the same effect

[41]Figure D.4 shows this same desegregation for non-cotton related patents. The behavior in these industries is different. The number of patents did not decrease after the American-Spanish war, and they remained at the same levels after the colonies' independence.

[42]Table E.4 shows that this aggregation seems to solve serial correlation found in the yearly model. When applying a Q-stat Born and Breitung (2016) biased corrected test to an annual model similar to equation 5.2 (column 1), I can reject the null hypothesis of no serial correlation of order 1 or 2. In contrast, I cannot reject at the 95% of confidence the hypothesis using the 4-year aggregated data (column 2). Using the LM portmanteau test for serial correlation developed by Inoue and Solon (2006) I achieve the same conclusion. I cannot reject at any level the hypothesis of no serial correlation.

as β_k^1 in equation 5.1 and γ_k^3 that capture the differential change between the period k and the baseline period in the cotton related patents at the weaving production stage in comparison with the other cotton production stages. The identification assumption is that without the insertion on international markets of Spanish fabrics after the American-Spanish war, the behavior of the difference between cotton patents and non-cotton patents for weaving would have behaved in a similar way to the patents at different stages[43]. I evaluate the plausibility of this assumption by looking at the coefficients for triple difference on the periods before 1998. I expect that without competition on the international market motivated by the loss of colonial markets, there is no effect on cotton patents used on weaving technologies. Finally, for inference, I use the same approach as in the previous model estimation. However, I add a third randomization. I randomly chose four technology groups out of the 31 technology groups and treated them as weaving technologies. Under the null distribution of no differential effect on weaving technologies, the assignation of these placebo categories is not relevant to the observed outcome.

5.2. ***Results.*** I present equation 5.1 estimation in figure 5. The results confirm the observation in figure 3: there was an increase in the number of cotton patents during the market integration period in comparison with patents related to other fibers. During the period of not a complete market integration, before the protectionist tariff, the point estimates move very close around zero. This result is in line with the theory where only under the complete integration are there enough incentives to change the direction of the technology employed towards more expensive cotton textiles. The results are significant at the 95% confidence after the second half of the market integration period[44]. According to these results, during the 1895-1898 period, there were on average 13.5 more cotton-related patents per technology category when compared with no cotton-related patents. The effect begins to decrease, yet it remains significant during the three periods after the American-Spanish war and the colonies' loss[45].

Figure 6 shows equation 5.2 estimation. Panel A shows the difference between cotton and non-cotton-related patents. This estimated difference is similar to the one observer

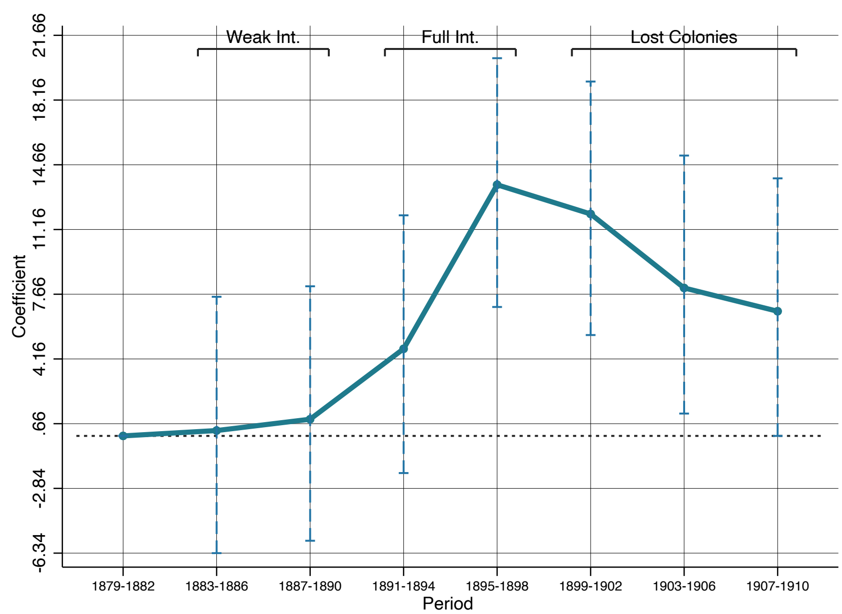
[43] Olden and Møen (2020) formalized the identification assumption for triple differences model and show that only one parallel trend assumption must hold to have a causal interpretation of the coefficients.

[44] Figure D.5 in the appendix shows the convergence path for the confidence interval estimation and the distribution of placebo coefficients for each one of the coefficients plotted on figure 3.

[45] This pattern would be evidence of path dependence on innovation (like the one theorized on Acemoglu et al. (2012)) however, in the next section, I am going to evaluate this theory against the presence of additional effect due to the insertion of Spanish textiles on international markets.

in the previous results. Before the full integration period, the estimated difference is very close to zero and nonsignificant. During the market integration period, there is an increase in the number of cotton related patents, and this is significant at the 95%[46]. Actually, this point estimate is similar to the one found before: during the 1895-1898 period, there were on average 11 more cotton-related patents per technology category when compared with no cotton-related patents. However, contrary to the previous results, differences after the war are not significant and approaching zero. These results are against the theory of a strong path dependence on cotton textile innovation, at least in this setting.

Figure 5. **Event study: Effect market integration on cotton patents**



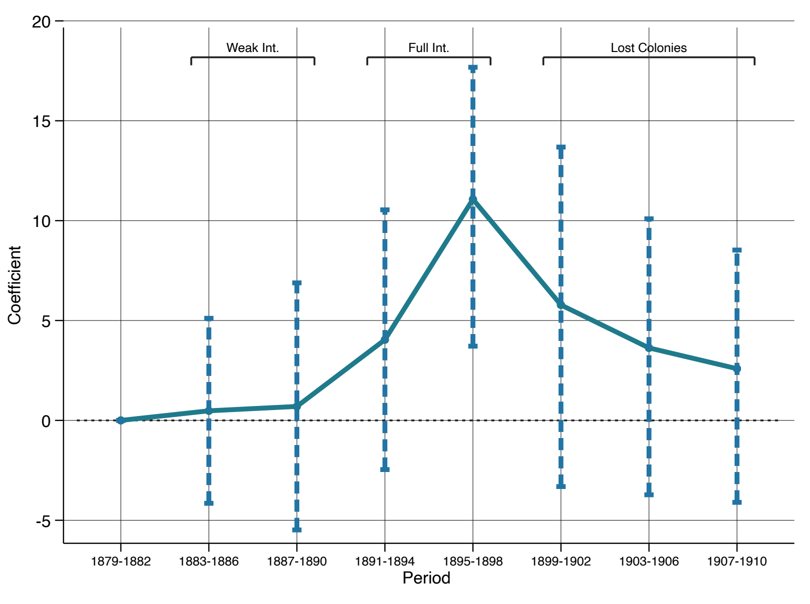
Notes: This figure shows coefficients β_k from regression 5.1. 95% Confidence Intervals using randomized inference. I followed the algorithm proposed by Garthwaite (1996) using 20.000 randomization allocations. Total number of observations 496.

Panel B shows the additional difference in cotton-related patents between patents at weaving production and other stages. The results confirm the observation in figure 4: The number of cotton patents designed for the weaving production stage increased after the war. Even more, there is no evidence of significant differences in cotton weaving patents prior to 1898. The coefficients are close to zero and non-significant (although in period 1896-1898 has a considerable magnitude yet it is not significant). 4 years

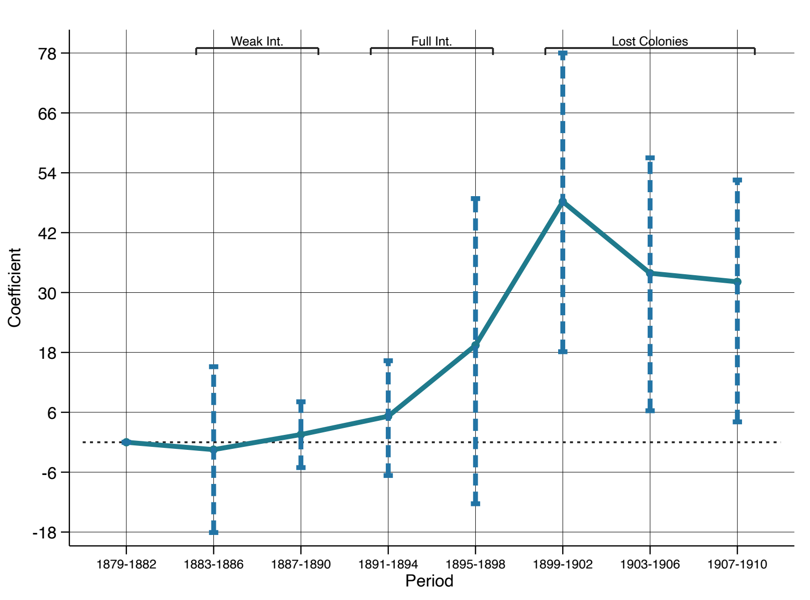
[46]See figure D.6 in the appendix for the detail of the placebo coefficients distribution and the confidence intervals estimation's convergence path.

after the 1898 crisis, there were, on average, 48 more patents used on cotton weaving process. The effect in the next period maintained around the same levels (additional 33 patents), and it was significant. Protection of local markets for high-quality textiles cannot explain this behavior since the policy was introduced much later. My argument is that the insertion on international markets explains these results. With the entry to new markets, skilled weavers got scarcer, and firms needed to adopt technologies in the weaving sector.

FIGURE 6. **Event study: Effect market integration and colonies lost on cotton and weaving patents**



A. Cotton x ....



B. Cotton x Weaving x ....

Notes: This figure presents the regression results from equation 5.2. Panel A shows γ_k^1 coefficients and panel B shows γ_k^3 coefficients 95% Confidence Intervals using randomized inference. I followed the algorithm proposed by Garthwaite (1996) using 20.000 randomization allocations. Total number of observations 496.

5.3. **Robustness.** The previous results use a 4-year aggregation; however, my results are not driven by this specific estimation. I estimate a yearly panel form 1878-1911 of the equation 5.2 in appendix figure D.7. In this case, due to the number of years i estimate a more restrictive form including differential trends by technology category[47]. Finally due to the presence of serial correlation I a calculate Newey–West standard errors with a lag length of 3, based on Greene's rule-of-thumb lag length of $T^{1/4}$ rounded upwards. Also because of the presence of cross sectional dependence[48] I include an estimation with double cluster standard errors at group and year level.

Results do not change significantly. The estimated difference between cotton and non-cotton patents is very close to zero before 1891. After this period, there was a significant increase in the estimated difference until 1898, when the difference started to decrease. However, the difference remained significant during some years after the colonial markets lost. This is evidence of some small path dependence in innovation. When analyzing the additional effect on weaving patents, the estimated difference moves around to zero before 1895. After that year, the number of weaving cotton patents increased. This is evidence of some anticipation effects, perhaps due to the disruptions in Cuba with the reactivation of the independence movement. This is consistent with the historical evidence that accounts for growing concerns in Spain about the possible US intervention, and the view of a foretold lost (Heraclides and Dialla, 2017). Overall, this is reassuring on the previous analysis conclusions. First, the market integration motivated an increase in innovation on all cotton patents due to changing towards a price determined by the relative endowment of cotton on the integrated market. Second, the insertion on global markets (forced by the colonial markets lost) motivated an increase in weaving innovation to face the relative cost of use weavers.

The previous results might not capture changes that industry faced due to Spain-colonies market integration or to the entrance of Spanish cotton manufactures into the international markets. In particular, the effects captured after 1898 might be related to external forces on the international markets. First, the changes could be related to shocks on external innovating countries that tried to allocated production outside their national frontiers. To rule out this type of off-shoring shock (theorized by Acemoglu, Gancia, and Zilibotti (2015)) I evaluate my results using patents registered only by

[47]Exactly I estimate the following equation: $Pat_{jt} = \sum_{k\neq[1881]} \gamma_k^{01}(\text{Year}_k \times \text{Cotton}_j) + \sum_{k\neq[1881]} \gamma_k^{02}(\text{Year}_k \times \text{Weave}_j) + \sum_{k\neq[1881]} \gamma_k^{03}(\text{Year}_k \times \text{Weave} \times \text{Cotton}_j) + \sum_{g\in\text{Tech}} \alpha_g \times t + \alpha_t + \alpha_j + \varepsilon_{jt}$ where $\alpha_g \times t$ are the technology group differential trends

[48]Table E.4 shows the presence of some cross sectional dependence between units. Pesaran's test with a statistic of 5.3 and p-value of 0.

Spanish residents (i.e. leaving out all patents registered by foreign residents). Spanish patent law allowed ideas protection of non resident individuals if they plan to insert in the country the technology. Figure in appendix D.10 shows the results when I estimate equation 5.2 using as dependent variable the patents originated in Spanish. The graphs show that my main results are not driven by any type of shock that motivated capital reallocation since this new estimation do not change the conclusions I arrived before. Second, it might the case that my results capture the forces of new countries demanding new textiles after 1898. Indeed during this same period Argentina experienced an economic boom that translated into a bigger demand for industrial goods[49]. To formally rule out the possibility that Argentina's conditions explain my results I estimate equation 5.2 controlling by Argentina exports. I include a new set variable that interact the material-technology fixed effects with the total yearly import values in Argentina[50]. Appendix figure D.9 shows the results of this exercise. Again the results' behavior is the same to the original results. There is a positive increase on cotton weaving innovation that is significant during all the periods after 1898 . Then, I conclude that there are few possibilities that my results are contaminated by external shock that occurred during the periods of the market integration or after the colonial lost.

Finally, my results are nor driven by any patent quality difference. I use two approaches to control for the differential quality on the patent application. First, Spanish law required an inspection to corroborate that the patent was actually used during the first 2 years after the application process. Figure D.11 in appendix shows the results when I use only the counts of this high quality patents. That is patents that were used in the production of new goods. During the integration market period (and especially during 1895-1898) the high quality cotton patents increased in contrast to non-cotton patents. However the change on high-quality patents destined to cotton weaving started

[49]Argentina became one of the most important markets for Spanish cotton fabrics. Between 1905 and 1910 Argentinean market represented 15% of total cotton exports far above other important markets such as France (6.9%), Turkey (4.9%), Uruguay (4.7%) and Colombia (4%). However, the economic conditions in Argentina started to improve several years before the American-Spanish war. By 1895 the railroad system were already developed and it connected several inland cities and the imports values were high (see Fajgelbaum and Redding, 2021). That means that Argentinean market were already available to Spanish producers by the end of 19th century but they did not actively look to entered into the new market before the lost of colonial protected markets.

[50]I estimate this new equation $Pat_{jt} = \sum_{k\neq[1879-82]} \gamma_k^1(\text{Period}_k \times \text{Cotton}_j) + \sum_{k\neq[1879-82]} \gamma_k^2(\text{Period}_k \times \text{Weave}_j) + \sum_{k\neq[1879-82]} \gamma_k^3(\text{Period}_k \times \text{Weave}_j \times \text{Cotton}_j) + \alpha_t + \alpha_j + \alpha_j \times \ln(\text{Arg Imp}_t) + \varepsilon_{jt}$, where $\ln(\text{Arg Imp}_t)$ are the natural logarithm of import values in Argentina measured in constant Argentine peso moneda nacional (source Dirección General de la Estadística de la Nación, 1916)

before the entry to global markets during the cuban independence war (1895-1898). On the following periods, the difference remained stable around the same value: on average 9 more patents per technology category. Again it seems that are some anticipation effects. Even before the Spanish cotton fabrics entered to global market competition, there were an increase on high quality patents directed to cotton fabric production. Second, Spanish law allowed the introduction of innovation and ideas already used in other countries but not Spain. Appendix figure D.10 shows the results when I exclude these type of patents, that is using only new ideas or innovations. Cotton weaving new patents also increased after 1898 shows that the innovation implemented were not just a copy of foreign innovation. Overall, I can conclude that my main results are robust to different specification and account for high quality improvements on the production of all cotton (between 1891 and 1898) and cotton fabrics after (1898).

6. Intermediate products prices

6.1. **Finished textile prices after market integration:** My argument is that the full market integration between Spain and its colonial markets affected prices relation between cotton finished fabrics and other fibers fabrics and this is the mechanism that explain the increase on innovation on the cotton sector. Once Spain exported its cotton manufactures production to their colonies the price of this product increased on the internal market and then the incentives on innovators to develop new mechanism for cotton production. To evaluate this hypothesis I compare the behavior of a cotton finished fabric[51] price to the finished manufactures of linen and wool prices[52]. Formally I estimate the following model:

$$\begin{aligned} \ln(P^F_{jt}) = & \left[\sum_{k=1889}^{1898} \gamma^F_k \times \text{Years}_k \times \text{Cotton}_j\right] + \gamma^F_{99-10} \times \text{Colonies Lost}_t \times \text{Cotton}_j \\ & + \alpha_j \times t + \alpha_t + \alpha_j + \varepsilon_{jt} \end{aligned} \tag{6.1}$$

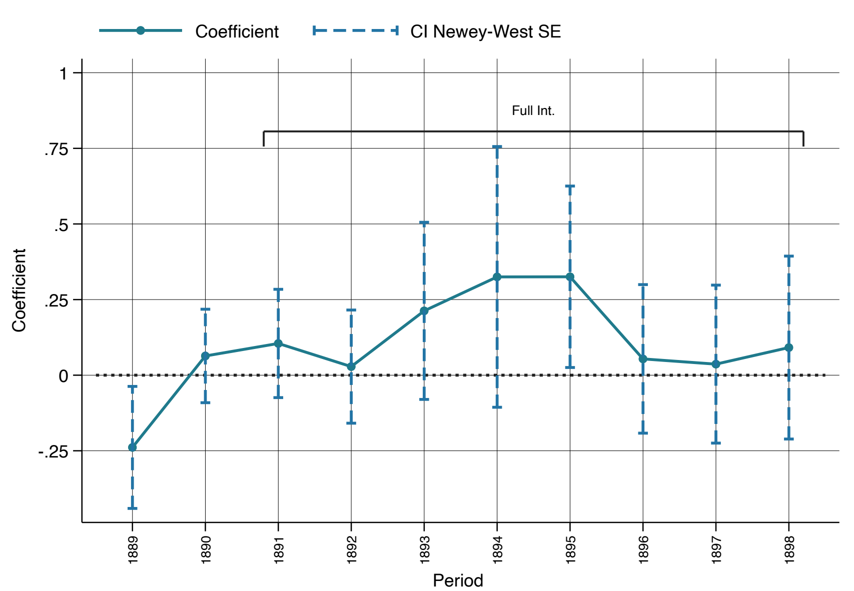
Where P^F_{jt} is the textile price of material j at time t. Years_k are dummy indicators for each year and Colonies Lost_t is an indicator for the years after the Spanish-American war. Cotton_j is a dummy indicator if the material of the textile is made from cotton.

[51] I use *Percalina Lisa Superior* price. The source of this information is the inventory ledgers of *La Espanña Industrial.* This is the only fabric that was constantly produced between 1878 and 1907 and therefore when analyzing this price variety I have less concerns about possible changes on textile quality.

[52] Prices is the average manufactures price for imported goods from England to Spain. The data was gathered by Nadal Ferreras (1978) in pounds and converted to pesetas using historical exchange series provided by Rodney Edvinsson. All the prices are measured as constant pesetas per meter.

I include a differential time trend on the regression since the prices for each material fabric presented different trends before the market integration. I am interested on the coefficients γ_k^F that captured changes on the cotton prices relative to other textiles comparing the market integration years with the years before this shock[53]. I expect an increase on cotton fabric prices after the integration period. However with the adjustment of the innovation I expect this values to return to the levels previous the shock. Appendix figure D.12 shows some evidence of this behavior especially when comparing with wool prices. After 1891 both cotton and wool fabrics prices decreased however the prices is more pronounced for wool finished textile prices. Moreover, the reduction trend reverted for wool fabrics, suggesting that the price of cotton fabrics became relative cheaper after 1895.

FIGURE 7. **Behavior of textile prices**



Notes: This figure shows the coefficients γ_k^F from regression 6.1 for each year starting from 1889 to 1898. 95% confidence intervals using Newey-West standard errors with three lags. Annually data from 1877 to 1907. Total number of observations 99.

Figure 7 shows an increase on the relative cotton finished textile price that started in 1893 and remained high for 3 years. Also, this graph shows that after 1895 this increase trend reverted and the price ratio experienced a fall and it returned to pres-shock levels. This suggest that the initial trigger that motivated the cotton innovation

[53]Including the colonies lost dummy allow me to isolate the effect from the change coming to the insertion of Spain on international markets.

was the increase on cotton relative price. Even more this is consistent with theory that predict that adjustments on innovation will revert this tendency and pushed price ratio to the levels before the initial shock. Finally, estimated coefficients allow me get some sense of the elasticity of substitution between cotton fabrics and other fibers products. If I assume that the prices changes observed on the 1895 have not absorbed yet any adjustment on technologies, 1895's point estimate would imply and elasticity of substitution between cotton textiles and other textiles ($\epsilon^{z,x}$) of 1.07[54].

6.2. **Cotton products prices after colonies lost:** Now following the insertion to international market motivated by the lost of protected markets my argument is that the change on effective weavers to spinners due to an increase on the use cost of weavers affected the price relation of fabrics over threads in the cotton industry. Therefor the change on price is the initial trigger that explains the increase on incentives to innovate on the weaving sector. To evaluate this hypothesis, that is if there is a change on the cotton fabric prices and not on the cotton thread prices, I compare fabric prices[55] with thread prices behavior before and after 1898. Formally I estimate the following model:

$$\begin{aligned} \ln(P_{jgt}) =& \gamma^P_{1891-95} \times \text{Integration}_t \times \text{Fabric}_j + \left[\sum_{k=1896}^{1910} \gamma^P_k \times \text{Years}_k \times \text{Fabric}_j \right] \\ & + q_j + \alpha_g \times t + \alpha_t + \alpha_g + \varepsilon_{jgt} \end{aligned} \tag{6.2}$$

[54]See appendix section A for more details. If prices do not reflect yet innovation adjustments γ^F_{1895} is equal to $1/\epsilon^{z,x} \ln \lambda$. I can estimate λ using the observed ratio increase on patents on each sector. Before 1891 the cotton-other fibers patent ratio was 3.18 and in 1895 this ratio was 4.51. These numbers implies that λ is equal to 1.4. Finally, and given that γ^F_{1895} is 0.33, I estimate and elasticity of substitution of 1.07. Also I estimate the ratio of available raw material in Spain both isolated and with the integrated market. For three fibers (cotton, linen-hemp and wool) I asses the availability in continental Spain as the addition of internal production and imports after subtracting exports. In the case of cotton and linen I estimate internal production using cultivated area in 1929. In the case of wool I estimate internal production using 1890 cattle census and assuming an average yearly production of 2 kg per sheep and a reduction of 0.57% after scour. I calculate an availability in 1895 of 72,940 tons of cotton, 9,126 tons of wool and 21,081 tons of linen (hemp). Jointly, these numbers implied a ratio of cotton to other fibers of 2.4 in continental Spain and with $\lambda = 1.4$ a ratio of 1.7 in the whole integrated market.

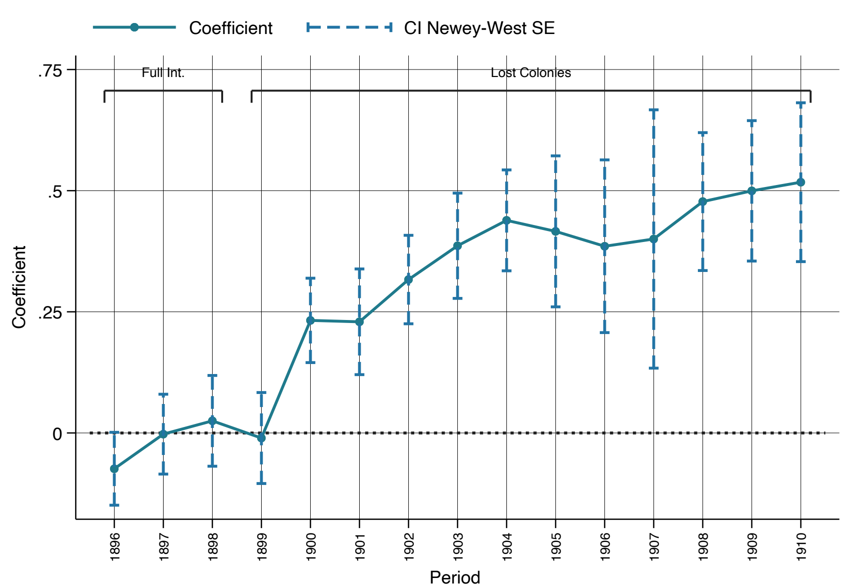
[55]These are prices of fabrics without any finishing process (in Spanish *empesas*)

where P_{jgt} is the price of product j of variety-type g[56] at time time t. Years$_k$ are dummy indicators for each year and Integration$_t$ is an indicator for the first years in the full integration period (1891-1895). Fabric$_j$ is a dummy indicator if the product is a fabric (i.e. not a thread). I am interested on coefficients γ_k^P that capture the differential change of fabric prices between each year of the colonies lost period and the years previous the full market integration in comparison to the change on cotton thread prices. This specification have some challenges. Mainly, the basket of products available for each variety-type is different in each time period and therefore the average quality of the product may change over time. Then, it is possible that changes on product prices might capture changes on the overall quality and not on prices levels. To overcome this issue I control for the quality of the products q_j. This is a quality index for each product j based on the observed prices following the assumption that difference on prices between threads and fabrics within the same year only reveals differences on quality between the basket products[57]. I include a time trend t since the

[56] I use 5 different type of cotton products that were produced by *La España Industrial* between 1878 and 1910 and whose prices were available at the inventory ledgers. Several products of different qualities were produced for each type variety and the quality composition of the basket changes over time. Cotton thread prices are prices for warp thread without size, warp thread with size and weft thread. Cotton fabric prices are *Madras* and *Molesquin* prices. Even though the firm produced several fabrics types these are the only types that were constantly produced on the complete period of my analysis and therefore were on the company stock when inventories were made.

[57] See appendix B for a detailed explanation on the construction of this index.

FIGURE 8. **Behavior of cotton thread and fabric prices**



Notes: This figure shows the coefficients γ_k^P from regression 6.2 for each year starting from 1896. 95% confidence intervals using Newey-West standard errors with three lags. Biannually data from 1878h1 to 1910h2. Total number of observations 913.

series evidences some downward trend before the colonies lost. Appendix figure D.13 shows the behavior of prices and qualities for the five products I am considering. In general there is an increase on the prices before 1898 though this is more pronounced for the fabrics whose prices increased more than 60%. In the case of qualities those values are more stable though there is a positive increase on qualities of one type of fabric. I expect to observe a positive significant effect during the colonies lost period and a non significant in the coefficients before 1898. Finally, I estimated Newey-West standard errors using with a lag of three periods[58].

Figure 8 shows that there are not significant changes in the relative prices during the metropolis-colonies integration. However there is a significant increase on prices after 1898. In particular there is a jump in the difference after 1900. Even more this increase remained stable and significant after that year. Although these results might have some potential issues, as previous mentioned, there is some evidence that there were

[58]Another problem with this estimation is the data periodicity. Even though most of the information is available biannually this is not true after 1903 when only one inventory was conducted per year. I treat the observed price on those years as a the price for the last halfyear and leave a missing observation for the price of the first halfyear. Since the inventory was conducted at the end of the year this price coincide with the periodicity of that part of the year before 1903. Also due to information quality I do not observe 1899 last halfyear and 1891 first halfyear prices.

an increase on relative prices that motivated the change towards weaving innovation. This results are consistent with theory that predict that the change remains even after the adjustment of technology suggesting and increase on 25% of cotton weaving product in relation to the period before the full market integration period.

6.3. **Cotton workers wages after colonies lost:** Finally, the relative cost of worker in the cotton industry should also translate to change on payments of workers within different production stages. The changes on relative use cost between spinners and weavers affects the relative demand for each type of workers and then salaries. My arguments is that these two workers are complements in the production of cotton finished textiles and therefore I hypothesize that this change is translated to a final increase on weavers wages even in the presence of endogenous changes on sector innovation[59].

Appendix section C shows this analysis. I show that there is a significant change on the relative wages after 1898. Moreover, the increase in the wage ratio do not happen immediately after the lost of the colonial markets. Although it started to increase after 1901 it is only significant after 1907. It is also interesting to note that the point estimates are smaller in this case when comparing to the changes on relative prices of worker's final product. This is consistent with the two type of workers being complements and the technology biased theory. Two forces work together when determining the change on relative wages on the presence of innovation. First, the increase on the relative cost of weaver translates to an increase on price of final product and then demand for these type of workers. Second, once innovation adjust this change is mitigated by the relative change on innovation in these sectors that pushed salaries down for the costly labor sector. In fact those two estimations allow me to get a sense of the elasticity of substitution between weavers and spinners. If I assume that the changes observed in 1901 do not reflect yet the adjustments on technologies these coefficients would suggest and elasticity of substitution ($\epsilon^{h,l}$) of 0.24 and an implied increase of weavers cost due to the entrance on new markets of 5.5%[60].

[59]When the two goods are complements an increase in price translates into a bigger relative demand for the costly worker and at the same time it translates into an increase of relative wage of these workers. This would not the case if the two goods were substitutes. In this case an increase in prices translates into a lower relative demand for the costly worker and at the same time a reduction on relative wages.

[60]See appendix sections A for more details. Without a technology adjust γ^W_{1901} is equal to $\left(\frac{1-\epsilon^{l,h}}{\epsilon^{l,h}}\right)\ln\left(\frac{\phi_h^{1901}}{\phi_h^{1882}}\right)$. With the same assumption γ^P_{1901} is equal to $\left(\frac{1}{\epsilon^{l,h}}\right)\ln\left(\frac{\phi_h^{1901}}{\phi_h^{1882}}\right)$. Using these two conditions I can compute the elasticity of substitution $\epsilon^{l,h}$ as $1-\gamma^W_{1901}/\gamma^P_{1901}$ that is $1-0.17/0.23$ and the change of relative cost as $\%\Delta_{\phi_h} = \exp(\epsilon^{h,l} * \gamma^P_{1901}) - 1$

7. Machines Acquisition

Next I turn to installed capital, and how innovation is translated to palpable adoption of new technologies. I look at the behavior of installed machines for different process in the different regions for different industries. The hypothesis is that I should observe an increase on all machines dedicated to cotton during the 1891-1898 period and increase on loom installed after the 1898 war in comparison to other textile sectors. Formally, I compare cotton machine with wool and linen machines using the the following *difference-in-differences* model where subindex p denotes province, m denotes material and subindex t denotes period.

$$
\begin{aligned}
Y_{ptm} = & \beta_1(\text{Integration}_t \times \text{Cotton}_m) + \beta_2(\text{Early lost}_t \times \text{Cotton}_m) \\
& + \beta_3(\text{Late lost}_t \times \text{Cotton}_m) + \left[\sum_{g \in \mathbf{X_p}} \sum_{k \in 1879} \gamma'(g \times \text{Years}_k) \right] \\
& + \alpha_m + \alpha_t + \alpha_p + \varepsilon_{ptm}
\end{aligned} \tag{7.1}
$$

Y_{ptm} is one of the machines types per 10.000 inhabitants and Cotton_m is a dummy that takes the value of one if the machine is used on the cotton industry. Integration_t is a dummy that takes the value of one during the integration period, that is for year 1893-94 and 1895-96, Early lost_t is a dummy that takes the value of one after the colonies lost between 1900 and 1904 and Lost lost_t is a dummy that takes the value of one after the colonies lost between 1905 and 1909. α_m and α_p are province and material fixed effects that captures any time-invariant category characteristics and α_p aggregate time shock. Province with cotton industry are different to provinces with other industries. Therefore I interact the province characteristics measure in 1877 ($\mathbf{X_p}$) with the time fixed effects to control for differential trends by each one of those attributes. ε_{jt} is the error term that I cluster at the province-year level, that is I control for correlation between industries at same year in the same province[61]. The key coefficients are β_1, β_2 and β_3 that capture the differential change in machines between each period and the baseline period 1879[62].

Table 1 presents the empirical estimates of the equation model 7.1 for machines used at the weaving stage. I compare cotton machines with machines in other textile

[61] I only have a small number of provinces (45 provinces), therefore I followed Imbens and Kolesár (2016)'s and calculate and HC2 standard errors tested against a t-distribution.

[62] Again the standard identification applies here. Without the market integration and the entry to global markets the machines used to create cotton textiles would have behaved similar to wool and linen machines.

sectors. Panel A shows the effect on machines per 10.000 inhabitants: either mechanical looms, manual looms or jacquard looms[63].Odd columns compare against the behavior of wool and linen machines while even columns compare only with wool industry. The purpose of this is to have a robustness and compare cotton industry with an industry without a significant presence in the colonies (wool). This table reveals a positive effect in the capital installed at the weaving stages on all the three different periods. All three points estimates are similar. For instance, according to them there were on average around 10 more mechanical looms per 10,000 inhabitants during the colonial-metropolis integration period. After the colonial market lost, the positive effect is also present. There was an increase of jacquard looms of around 0.84 cotton looms on each year after the war. When analyzing the behavior of manual looms I do not observe a differential effect. This shows that technical change helped the industry mechanization. Finally, when comparing only with wool industry these results are robust and I reach to the same conclusions: the results are consistent with innovation findings and they show that the increase on patents at weaving stage translated on more mechanical and jacquard looms working on cotton fabric production.

Panel B on this table evaluates if previous findings are driving by an increase in firms using new technologies. Column 7 and 8 revels that an increase on firms that reported and pay taxes on mechanical looms explains the increase on the number of installed looms. That means that in order to increase competitiveness firms chose change on looms technology. On the other hand, there are not changes on the firms reporting jacquard looms which suggest that in this case existing firm with those technologies introduced more of those type of looms. Finally, while there is not changes on reported manual looms there seems to be a positive effect on firms reporting this type of technologies which suggest that existing manual looms were acquired for some firms and technology was not totally discard. Overall, I can conclude that the positive effect on patent applications tended to correspond to the introduction of new looms.

[63]This type of technology has its own classification: patterns cards or chains and punching of cards. Jacquard looms include both manual and mechanical looms.

TABLE 1. Response of cotton textiles machines on weaving stage to market integration and colony lost

	Panel A Machines per 10.000 inhabitants						Panel B Firms per 10.000 inhabitants					
	Mechanical Looms		Jacquard Looms		Manual Looms		Mechanical Looms		Jacquard Looms		Manual Looms	
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)
Cotton ...												
... x Market integration	10.01*	9.14	0.26	0.26	2.81	−12.29	0.08	0.04	−0.00	−0.01	1.59***	0.28
	(5.96)	(5.79)	(0.17)	(0.26)	(7.74)	(7.70)	(0.05)	(0.03)	(0.02)	(0.05)	(0.55)	(0.60)
	[[0.044]]	[[0.101]]	[[0.227]]	[[0.350]]	[[0.687]]	[[0.082]]	[[0.107]]	[[0.347]]	[[0.927]]	[[0.848]]	[[0.001]]	[[0.548]]
... x Early colonies lost	11.22**	10.38**	0.84**	0.88**	3.21	−11.41	0.14**	0.10**	0.02	0.01	1.87***	0.77
	(4.45)	(4.40)	(0.35)	(0.40)	(7.72)	(7.67)	(0.06)	(0.05)	(0.02)	(0.04)	(0.54)	(0.56)
	[[0.003]]	[[0.019]]	[[0.010]]	[[0.024]]	[[0.645]]	[[0.106]]	[[0.007]]	[[0.074]]	[[0.436]]	[[0.880]]	[[0.000]]	[[0.085]]
... x Late colonies lost	12.13***	11.09**	0.84***	0.94***	3.35	−11.10	0.14**	0.09	0.04*	0.03	1.85***	0.72
	(4.60)	(4.53)	(0.28)	(0.33)	(7.72)	(7.67)	(0.06)	(0.05)	(0.02)	(0.04)	(0.54)	(0.56)
	[[0.002]]	[[0.014]]	[[0.002]]	[[0.005]]	[[0.630]]	[[0.116]]	[[0.014]]	[[0.135]]	[[0.127]]	[[0.413]]	[[0.000]]	[[0.104]]
Observations	1716	1144	1716	1144	1716	1144	1716	1144	1716	1144	1716	1144
Material fixed effects	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	tex ✓	✓
Time fixed effects	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Province fixed effects	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Controls	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓	✓
Comparison Cotton vs.	W and L	W	W and L	W	W and L	W	W and L	W	W and L	W	W and L	W

Notes: Control variables include logarithm of population, men shared , share residents, single shared population, married shared population, catholic shared , share of illiterate, share of born in same province, share of nationals born in different province, share of regular residents in the same municipality. W stands for wool and L for linen and hemp. Columns 1 and 3 compare the cotton industry with wool and linen (hemp) industry and columns 2, 4, 5 and 6 compare the cotton industry only with wool industry. Comparison period 1979. P-values from a test based on HC2 standard errors tested against a t-distribution are in double squared brackets. I follow the correction proposed by IImbens and Kolesár (2016). Standard errors in parentheses are clustered on province-year level. * is significant at the 10% level, ** is significant at the 5% level, *** is significant at the 1% level.

As a robustness, appendix table E.5 shows the same exercise for machines at the spinning stage (Panel A) and finishing stage (Panel B). In the mechanical spindles case, the coefficient that measure the impact during the market integration period between 1891-1898 are positive although non-significant, while in the manual spindles cases the point estimate is negative and non-significant. On the other hand, during the colonies lost period I observe that the coefficients of mechanical spindles is negative. This is consistent with the previous results that show an increase of general cotton patents only on the first period. Unfortunately, the data for that period is not complete for the whole time range and I lack the power to get a precise positive estimation. Finally, for the shearing and raising machines case (finishing stage)[64], I do not observe any significant effect on the installed machinery. Overall I do not observe any differential

[64]Shearing and raising is not a widely process used in the linen industry.

changes after the colony lost on the spinning and finishing machines between cotton and other industries.

8. CONCLUSION

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ONLINE APPENDIX

Appendix A. Two models of Trade and Innovation

A.1. **Cotton and other fibers textiles.** In this section I show a model of innovation between two sectors: cotton textile and other fibers textiles.

A.1.1. *Set up and assumptions.* There is an unique final produced good (apparel), produced competitively using cotton textiles (Y_z) and other textiles (Y_x) as inputs, according to the following aggregate production function

$$Y_f = \left[Y_z^{\frac{\epsilon-1}{\epsilon^{z,x}}} + Y_x^{\frac{\epsilon^{z,x}-1}{\epsilon^{z,x}}} \right]^{\frac{\epsilon^{z,x}}{\epsilon^{z,x}-1}} \tag{A.1}$$

where $\epsilon^{z,x} \in (0, +\infty)$ is the elasticity of substitution between the two inputs. Then the producers of textiles $k \in \{Z, X\}$ maximize their production Y_k under a regular inputs constraint giving the relative demand function:

$$\frac{P_z}{P_x} = \left(\frac{Y_z}{Y_x} \right)^{-\frac{1}{\epsilon^{z,x}}} \tag{A.2}$$

Where P_z and P_x are the prices of the two textiles[65]. Textiles Y_z and Y_x are produced using a continuum of sector specific intermediates ($y_z(i)$ and $y_x(i)$ respectively). Where A_z and A_x is the measure of machines and innovation in each sector[66].

$$Y_z = E_z \left[\int_0^{A_z} y_z(i)^\alpha di \right]^{\frac{1}{\alpha}} \quad \text{and} \quad Y_x = E_x \left[\int_0^{A_x} y_x(i)^\alpha di \right]^{\frac{1}{\alpha}} \tag{A.3}$$

Both textile producers sell in competitive markets and they maximize profits taking intermediate goods prices $p_z(i)$ and $p_x(i)$ as given. This gives the following demands functions for each intermediate good

$$y_z(i) = Y_z \left(\frac{A_z^{2\alpha-1}}{p_z(i)} \right)^{\frac{1}{1-\alpha}} \quad \text{and} \quad y_x(i) = Y_x \left(\frac{A_x^{2\alpha-1}}{p_x(i)} \right)^{\frac{1}{1-\alpha}} \tag{A.4}$$

and the following relative demand equation

$$\frac{y_z(i)}{y_z(j)} = \left(\frac{p_z(j)}{p_z(i)} \right)^{\frac{1}{1-\alpha}} \quad \text{and} \quad \frac{y_x(i)}{y_x(j)} = \left(\frac{p_x(j)}{p_x(i)} \right)^{\frac{1}{1-\alpha}} \tag{A.5}$$

The production function for each intermediate input is linear in the type of material employed ($y_z(i) = \frac{Z(i)}{\phi_z}$ and $y_x(i) = \frac{X(i)}{\phi_x}$. Where ϕ_z and ϕ_x measure the cost in terms of the material needed to produce the intermediate good. This production is subject to resource constraints $\int_0^{A_z} z(i)di \leq Z$ and $\int_0^{A_x} x(i)di \leq X$. The intermediate good sector

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[65] Y_f is the numeràire.

[66] Terms $E_z \equiv (A_z)^{\frac{2\alpha-1}{\alpha}}$ and $E_x \equiv (A_x)^{\frac{2\alpha-1}{\alpha}}$ are two externality terms that assures the existence of a balanced-growth path.

is monopolistic since the producer owns a patent for this product. The monopolist face a demand curve with the constant price elasticity $1/1-\alpha$ and the optimal price in each sector is:

$$p_z(i) = \frac{w_z \phi_z}{\alpha} \quad \text{and} \quad p_x(i) = \frac{w_x \phi_x}{\alpha} \tag{A.6}$$

Where w_z and w_x is the price of each raw material Z and X. This implies that the profits of these firms is equal to a fraction $(1-\alpha)$ of the total sales

$$\pi_z(i) = (1-\alpha)\frac{p_z(i)z(i)}{\phi_z} \quad \text{and} \quad \pi_x(i) = (1-\alpha)\frac{p_x(i)x(i)}{\phi_x} \tag{A.7}$$

Using the market clearing conditions on the raw materials I can write the production function as $Y_z = \dfrac{A_z Z}{\phi_z}$ and $Y_x = \dfrac{A_x X}{\phi_x}$. Using these equations in the relative demand function (A.2) I found the relative price function equation

$$p \equiv \frac{P_z}{P_x} = \left(\frac{A_z Z}{A_x X}\frac{\phi_x}{\phi_z}\right)^{-\frac{1}{\epsilon^{z,x}}} \tag{A.8}$$

Using (A.4) I can rewrite intermediate prices as $P_z A_z = p_z(i)$ and $P_x A_x = p_x(i)$ and the relative profits of monopolistic in each sector as

$$\frac{\pi_z(i)}{\pi_x(i)} = \frac{p_z(i)z(i)}{p_x(i)x(i)}\frac{\phi_x}{\phi_z} = \left(\frac{A_x}{A_z}\right)^{\frac{1}{\epsilon^{z,x}}}\left(\frac{\phi_x Z}{\phi_z X}\right)^{\frac{\epsilon^{z,x}-1}{\epsilon^{z,x}}} \tag{A.9}$$

Using this same condition I can write the raw materials prices ratio as

$$\omega \equiv \frac{w_z}{w_x} = \left(\frac{A_z}{A_x}\frac{\phi_x}{\phi_z}\right)^{1-\frac{1}{\epsilon^{z,x}}}\left(\frac{Z}{X}\right)^{-\frac{1}{\epsilon^{z,x}}} \tag{A.10}$$

A.1.2. *Endogenous technological change.* Introduction of new machines has a fixed cost μ as units of the numeràre. Each innovator decide between designing machines for one of the two sector. Patents are infinitely lived and therefor at the balanced growth path the discounted value in each sector (V_z and V_x) of the profit stream cannot exceed the innovation cost. This implies that innovators are indifferent between the two technologies. That is $V_z = V_x = \mu$ or $\frac{\pi_z}{\pi_x} = 1$. Using this condition jointly with A.9 I find the the technology direction that is compatible with balanced growth.

$$\frac{A_z}{A_x} = \left(\frac{\phi_x Z}{\phi_z X}\right)^{\epsilon^{z,x}-1} \tag{A.11}$$

Also on balanced growth the textiles price ratio and and the endowments payment ratio can be written as

$$p^{**} = \left(\frac{\phi_x Z}{\phi_z X}\right)^{-1} \quad \text{and} \quad \omega^{**} = \left(\frac{\phi_x}{\phi_z}\right)^{\epsilon^{z,x}-1}\left(\frac{Z}{X}\right)^{\epsilon^{z,x}-2} \tag{A.12}$$

A.1.3. *Market Integration.* In this section now I develop the effect of market integration. Now consider Spain with endowments Z^S and X^S get integrated with its colonies that have endowment Z^C and X^C. The endowments of materials in the market are defined as the sum of both the metropolis and the colonies endowments (i.e. $Z^I = Z^S + Z^C$ and $X^I = X^S + X^C$.). Then the relative price equation (A.8) from the integrated market is

$$p^I \equiv \frac{P_z}{P_x} = \left(\frac{A_z(Z^S + Z^C)}{A_x(X^S + X^C)}\frac{\phi_x}{\phi_z}\right)^{-\frac{1}{\epsilon^{z,x}}} = \lambda^{1/\epsilon^{z,x}} p \tag{A.13}$$

Colonies copy technology from the metropolis without any differential cost. Adjusting technology equation (A.9) becomes

$$\frac{A_z^I}{A_x^I} = \left(\frac{\phi_x Z}{\phi_z X}\right)^{\epsilon^{z,x}-1} \lambda \tag{A.14}$$

Where $\lambda \equiv \dfrac{1 + X^C/X^S}{1 + Z^C/Z^S}$. If I assume that cotton is relative more abundant in Spain compare with its colonies (i.e. $\frac{Z^S}{X^S} > \frac{Z^C}{X^C}$) then $\lambda > 1$. Or what is the same a market integration produce an increase on innovation on the relative more abundant product (i.e. cotton). Also when technology is allowed to adjust the price ratio becomes equal to the levels before the market integration

$$p^{I**} = \left(\frac{\phi_x Z}{\phi_z X}\right)^{-1} = p^{**} \tag{A.15}$$

A.1.4. *Change on textile prices.* Coefficients γ_k^F in equation 6.1 identify the relative change between other fibers and cotton (p) before and after the integration, that is $\ln(p^I/p^{**})$ that can be expressed as:

$$\ln\left(\frac{p^I}{p^{**}}\right) = \frac{1}{\epsilon^{z,x}} \ln \lambda \tag{A.16}$$

finally the increase on the technology after the market integration can be expressed as

$$\frac{A_z^I/A_x^I}{A_z/A_x} = \lambda \tag{A.17}$$

A.2. **Spinning and weaving sectors.** In this section I show a model of innovation between two sectors in the cotton textile industry: spinning and weaving sector.

A.2.1. *Set up and assumptions.* There is an unique final good of cotton (textile), produced competitively using two inputs: threads (Y_h) and fabrics (Y_l). Each one is produced using two different type of workers spinners (H) and weavers (L) respectively. The production function is expressed as

$$Y_z^* = \left[Y_l^{\frac{\epsilon^{l,h}-1}{\epsilon^{l,h}}} + Y_h^{\frac{\epsilon^{l,h}-1}{\epsilon^{l,h}}} \right]^{\frac{\epsilon^{l,h}}{\epsilon^{l,h}-1}} \tag{A.18}$$

As in the last section products Y_l and Y_h are produced using a continuum of sector specific intermediates ($y_l(i)$ and $y_h(i)$ respectively). Where A_l and A_h is the measure of machines in each input produced with the two types of labor

$$Y_l = E_l \left[\int_0^{A_l} y_l(i)^\alpha di \right]^{\frac{1}{\alpha}} \quad \text{and} \quad Y_h = E_h \left[\int_0^{A_h} y_h(i)^\alpha di \right]^{\frac{1}{\alpha}} \tag{A.19}$$

The production function for each intermediate input is linear in the type of labor employed in the world $y_l(i) = \frac{l(i)}{\phi_l}$ and $y_h(i) = \frac{h(i)}{\phi_h}$. Where ϕ_l and ϕ_h measure the cost in terms of the workers need to produce either threads or fabrics. Using the sames steps as the previous model I can obtain the price relation between fabric and threads

$$p_{lh} \equiv \frac{P_l}{P_h} = \left(\frac{A_l L}{A_h H} \frac{\phi_h}{\phi_l} \right)^{-\frac{1}{\epsilon^{l,h}}} \tag{A.20}$$

and the wage ratio between weavers and spinner

$$\omega_{lh} \equiv \frac{w_l}{w_h} = \left(\frac{A_l}{A_h} \frac{\phi_h}{\phi_l} \right)^{1-\frac{1}{\epsilon^{l,h}}} \left(\frac{L}{H} \right)^{-\frac{1}{\epsilon^{l,h}}} \tag{A.21}$$

A.2.2. *Endogenous technological change.* Introduction of new machines has the same structure as the in previous section that is fixed cost μ as units of the numeràre. Therefore the technology direction compatible with balanced growth can be expressed as

$$\frac{A_l}{A_h} = \left(\frac{\phi_h L}{\phi_l H} \right)^{\epsilon^{l,h}-1} \tag{A.22}$$

Also on balanced growth the price ratio between fabrics and threads and and the wage ratio between weavers and spinners can be written as

$$p_{lh}^{**} = \left(\frac{\phi_h L}{\phi_l H} \right)^{-1} \quad \text{and} \quad \omega_{lh}^{**} = \left(\frac{\phi_h}{\phi_l} \right)^{\epsilon^{l,h}-1} \left(\frac{L}{H} \right)^{\epsilon^{l,h}-2} \tag{A.23}$$

A.2.3. *Entrance to international market.* In this section I develop the effect of the introduction to global markets. I assume that with the new tastes the cost of weaver increase since they are need to produce more varieties of products, that is an increase of ϕ_l. Given the fact that the two sectors are complements that is $\epsilon^{l,h} < 1$ it is straightforward to observe a positive relation with innovation ratio $\dfrac{A_l}{A_h}$ as well price ratio p_{lh}^{**} and wage ratio ω_{lh}^{**}

A.2.4. *Change on fabric-thread price.* Coefficient γ_k^P in equation 6.2 identify the change between thread price and fabric price before and after the increase on weaver cost $(\phi_h^0 \to \phi_h^1)$, that is $\ln(p_{lh}(\phi_h^1)/p_{lh}(\phi_h^0))$ that can be expressed as

$$\ln\left(\frac{p_{lh}(\phi_h^1)}{p_{lh}(\phi_h^0)}\right) = \frac{1}{\epsilon^{l,h}} \ln\left(\frac{\phi_h^1}{\phi_h^0}\right) \tag{A.24}$$

A.2.5. *Change on weavers spinners wages.* Coefficient γ_k^W in equation C.1 identify the change between weaver wages and spinner wavers before and after the increase on weaver cost $(\phi_h^0 \to \phi_h^1)$, that is $\ln(\omega_{lh}(\phi_h^1)/\omega_{lh}(\phi_h^0))$ that can be expressed as

$$\ln\left(\frac{\omega_{lh}(\phi_h^1)}{\omega_{lh}(\phi_h^0)}\right) = \frac{1-\epsilon^{l,h}}{\epsilon^{l,h}} \ln\left(\frac{\phi_h^1}{\phi_h^0}\right) \tag{A.25}$$

Appendix B. Cotton textile products quality index

In this section I explain in detail the construction of quality index for each cotton product observed on the inventory ledgers. During each period of time I observe data of two different types of products: thread and fabrics. Inside each type I observe different varieties. I observe three thread varieties (warp thread without size, warp thread with size and weft thread) and two fabric varieties (molesquin and madras). Finally I observe the price for different product inside each varieties only it the product was available on the stock of the company. To construct the quality I assume that the prices differences observer on the same product (thread or fabrics) reflect only differences on the qualities. I follow the following procedure:

(1) I calculate the lower price for each product type in 1878. And calculate the prices of all prices on based on that prices. This allow me to estimate the price in terms of a first prices
(2) Then I calculate the lower of those previous estimated price ratio for each period.
(3) I calculate then a new price ratio between each period minimum and original ratio. With this estimation I measure the quality of each observed product in terms of the low quality product of each type.
(4) I estimate the average of this indicator by product across all years in which it was observed and take measure as the indicator quality. This estimation assumes than inside each product of type the lower quality product was always available in all the periods. This seems a reasonable assumption since: i) for the three varieties of cotton thread I always observed the lower quality (thread with numbers lower than 20, and ii) the lower fabric price was always associated to a madras fabric with similar characteristics.

Appendix C. Effect of bias technology on relative wages

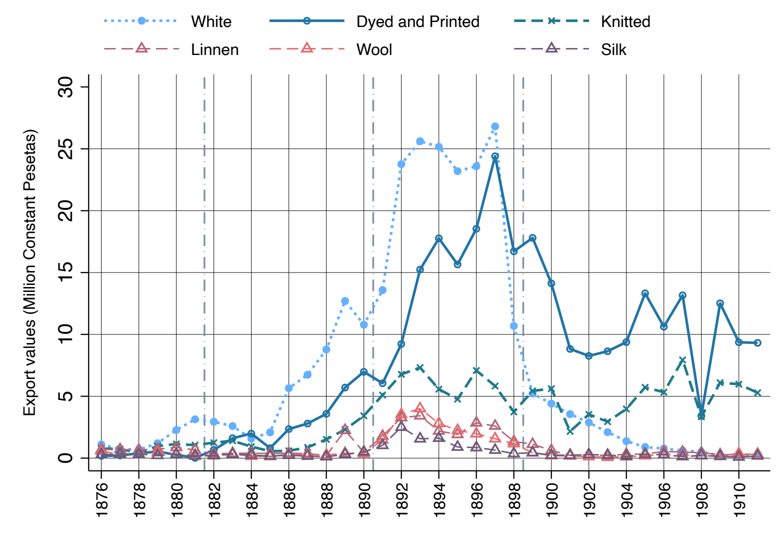
In this section I show the analysis of wages of two cotton textile workers: spinners and weaver. Figures D.14 gives a first evidence that this is the case. After the Spanish-American war weavers wages started to follow an upward trend and they increased constantly while the spinners wage remained constant during this period. I follow a similar strategy than in equation 6.2 and I compare weavers wage to spinner wage after the lost of the colonies in 1898. Formally, I estimate the following model:

$$\begin{aligned} \ln(W_{jt}) =& \gamma^W_{1891-95} \times \text{Integration}_t \times \text{Weaver}_j + \left[\sum_{k=1896}^{1910} \gamma^W_k \times \text{Years}_k \times \text{Weaver}_j \right] \\ &+ \left[\sum_{l \in \mathbf{X_t}} \gamma'(l \times \text{Weaver}_j) \right] + \alpha_j \times t + \alpha_t + \alpha_j + \varepsilon_{jt} \end{aligned} \tag{C.1}$$

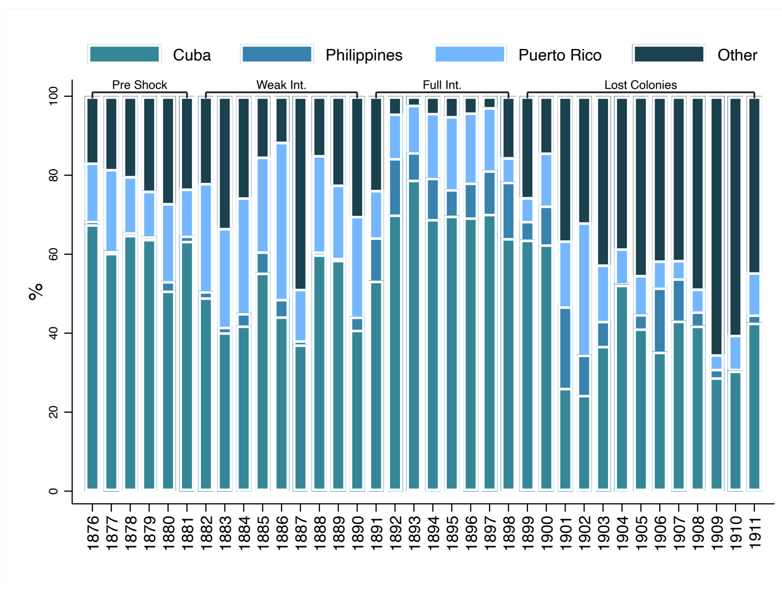
where W_{jt} is the wage received by type of worker j (spinner or weaver) at time t, Years_k are dummy indicators for each year, Integratio_t is an indicators the first years of the full integration period (1891-1895) and Weaver_j is an indicator if the salary is for workers at weaving stage. I include a differential trend in the estimation since the data evidence that the two series had different trends (see Appendix figure D.14). Spinners salaries had a downward trend before the colonies lost while the weavers remained relative constant before 1899. Finally, I also control for the wages of other workers at the weaving stage like personal in charge and warpers at each period $\mathbf{X_t}$. These two variables allow me to control for changes on the amount of work needed from each weaver since both are correlated with the quality and weight of the average produced piece (features that I do not observe in the data). Then the inclusion those variables reduces the concerns that salaries changes are being driven by movements in the amount of work needed to produced different fabric qualities. My interest is on coefficients γ^W_k that captures the change of weavers wages relative to spinner wages at each period of time in comparison to the average relative wage before 1891.

Appendix D. Figures

Figure D.1. **Textiles exports to colonies**



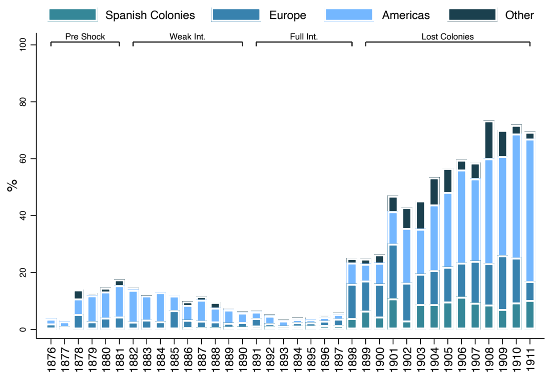
A Textile trade value to colonies



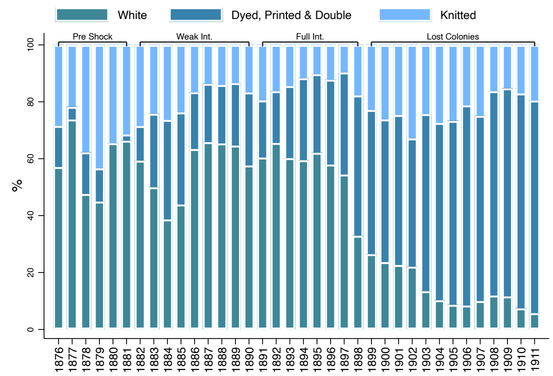
B Linen exports by destination

Source: Same as table 1
Notes: Panel A shows the value of textiles imports to colonies by type of material. I measure values using constant pesetas. I divided cotton fabrics into three different type of fabrics. Despite the known problems of this type of measure (Sudrià, 1983) this capture the relatively quality difference among fabrics. Panel B shows the share of colonial markets in the total linen exports.

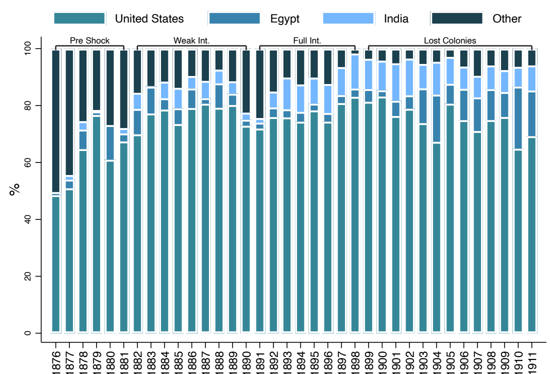
Figure D.2. **Cotton textiles exports and imports**



A Cotton textile by destination (Others)



B Cotton textile exports by type

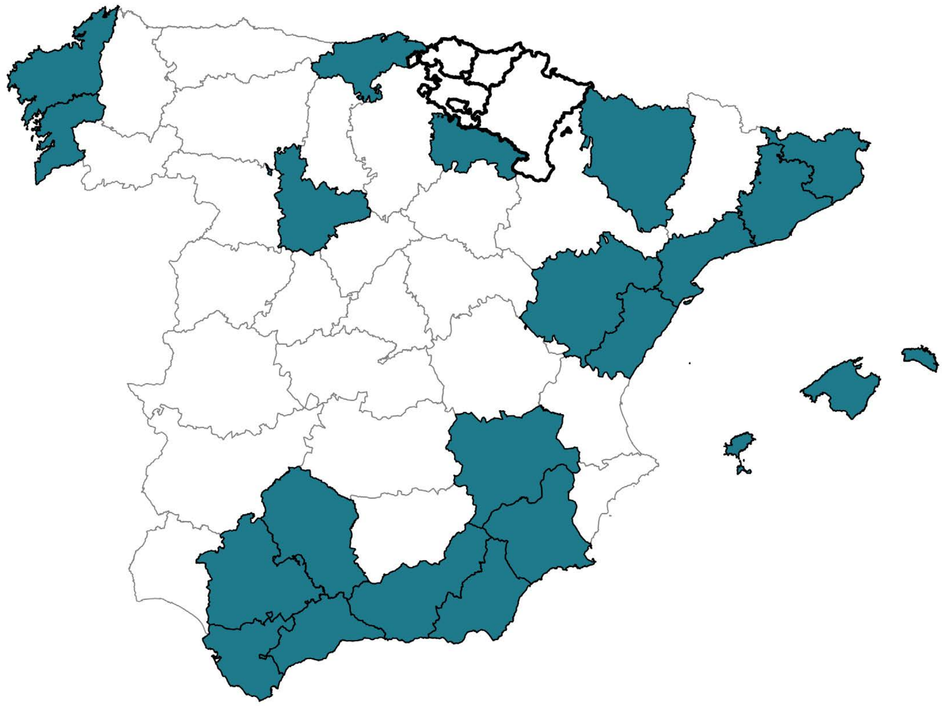


C Raw cotton imports by origin

Sources: Same as table 1

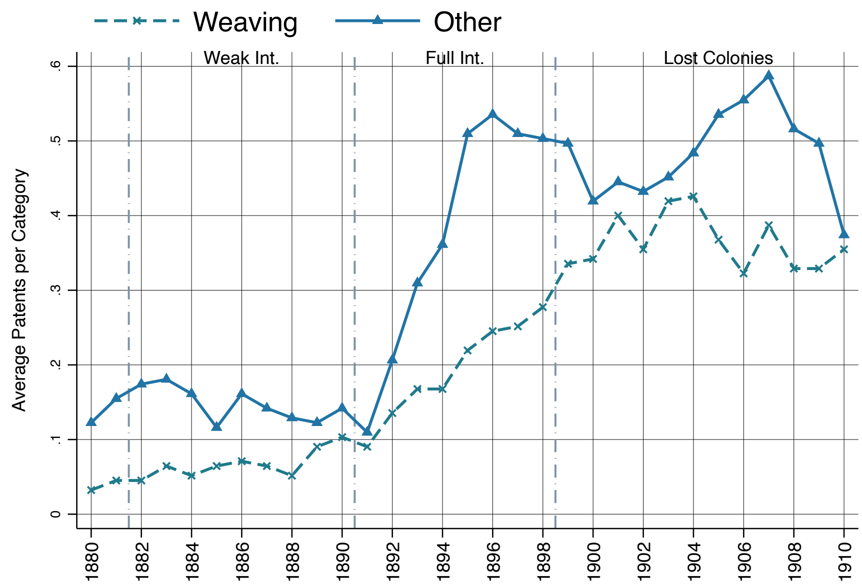
Notes: Panel A shows desegregation of cotton textile destination . It groups countries on American republics, Europe, other Spanish colonies and other regions of the world. Panel B shows the distribution of exports according to the textile type, following Spanish authority categorization. Panel C shows raw cotton country of origin shares.

Figure D.3. **Cotton textile industry location 1879**



Notes: This maps shows the location of cotton industry in 1879. Cotton industry location is define according to the presence of either spindles or looms. Provinces in the Basque County and Navarra did not have information (Shown on thick lines). Canary Islands not shown in the map.

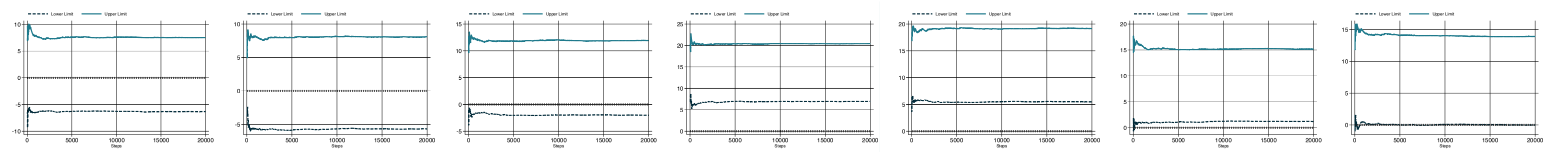
Figure D.4. **Cotton textile patents by stage production**



Notes: This graph shows the evolution of non-cotton related textile patents for weaving and other production stages. I show the 2 years moving average of the raw numbers for each series.

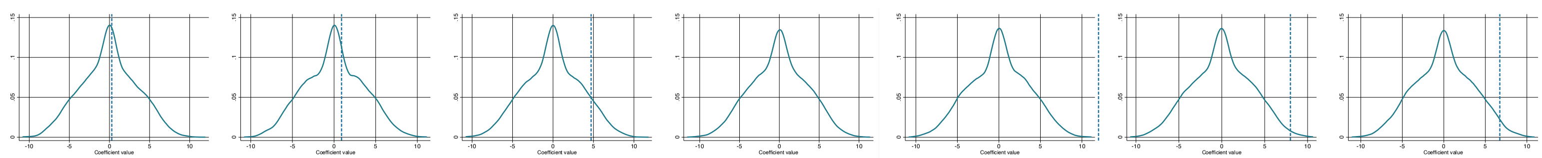
FIGURE D.5. **Randomization Inference Event Study**

Panel A: Lower and Upper Bounds Confidence Interval Convergence



a) Cotton x 1883-1886 **b)** Cotton x 1887-1890 **c)** Cotton x 1891-1894 **d)** Cotton x 1895-1898 **e)** Cotton x 1899-1902 **f)** Cotton x 1903-1906 **g)** Cotton x 1907-1910

Panel B: Placebo Coefficients Distribution

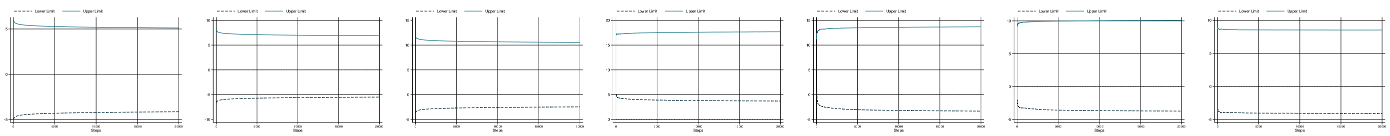


a) Cotton x 1883-1886 **b)** Cotton x 1887-1890 **c)** Cotton x 1891-1894 **d)** Cotton x 1895-1898 **e)** Cotton x 1899-1902 **f)** Cotton x 1903-1906 **g)** Cotton x 1907-1910

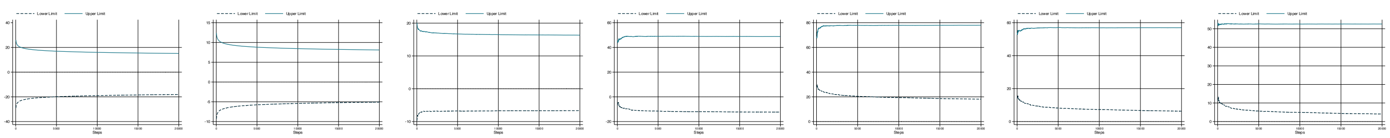
Notes: Panel A shows confidence intervals lower and upper bound convergence path ifor Figure 5 results. I follow the algorithm proposed by Garthwaite (1996) using 20.000 randomization allocations. Panel B shows the distribution placebo coefficients and the position of the coefficient presented in Figure 5. I estimated them using 10.000 randomization allocations.

FIGURE D.6. **Randomization Inference Event Study Triple Difference**

Panel A: Lower and Upper Bounds Confidence Interval Convergence

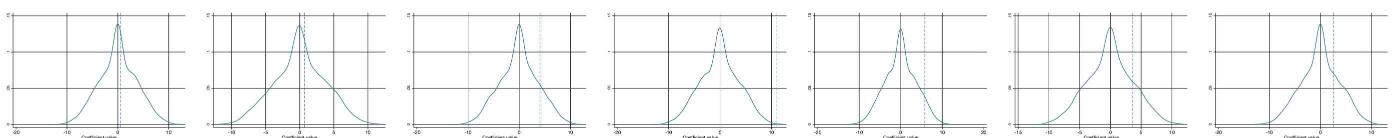


a) Cotton x 1883-1886 **b)** Cotton x 1887-1890 **c)** Cotton x 1891-1894 **d)** Cotton x 1895-1898 **e)** Cotton x 1899-1902 **f)** Cotton x 1903-1906 **g)** Cotton x 1907-1910

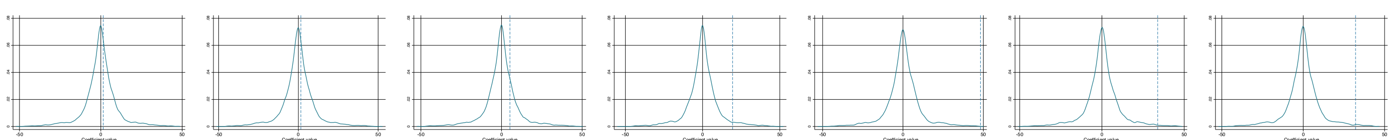


h) Cotton x Weaving x 1883-1886 **i)** Cotton x Weaving 1887-1890 **j)** Cotton x Weaving x 1891-1894 **k)** Cotton x Weaving x 1895-1898 **l)** Cotton x Weaving x 1899-1902 **m)** Cotton x Weaving x 1903-1906 **n)** Cotton x Weaving x 1907-1910

Panel B: Placebo Coefficients Distribution



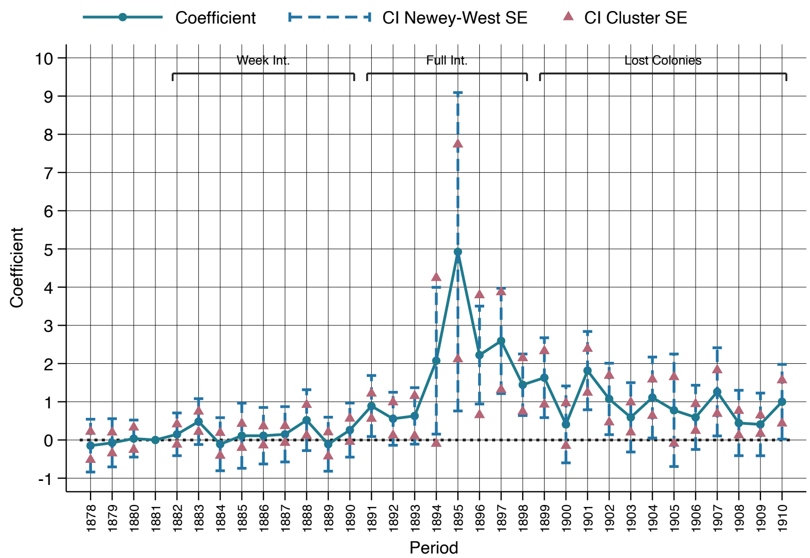
a) Cotton x 1883-1886 **b)** Cotton x1887-1890 **c)** Cotton x 1891-1894 **d)** Cotton x 1895-1898 **e)** Cotton x 1899-1902 **f)** Cotton x 1903-1906 **g)** Cotton x 1907-1910



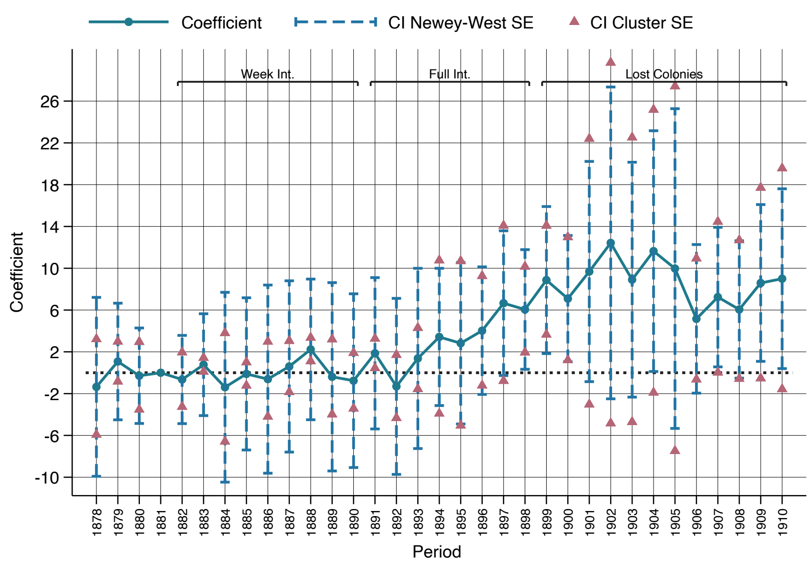
h) Cotton x Weaving x 1883-1886 **i)** Cotton x Weaving x 1887-1890 **j)** Cotton x Weaving x 1891-1894 **k)** Cotton x Weaving x 1895-1898 **l)** Cotton x Weaving x 1899-1902 **m)** Cotton x Weaving x 1903-1906 **n)** Cotton x Weaving x 1907-1910

Notes: Panel A shows confidence intervals lower and upper bound convergence path ifor Figure 6 results. I follow the algorithm proposed by Garthwaite (1996) using 20.000 randomization allocations. Panel B shows the distribution placebo coefficients and the position of the coefficient presented in Figure 5. I estimated them using 10.000 randomization allocations.

FIGURE D.7. **Event study: Effect on cotton and weaving patents using yearly panel**



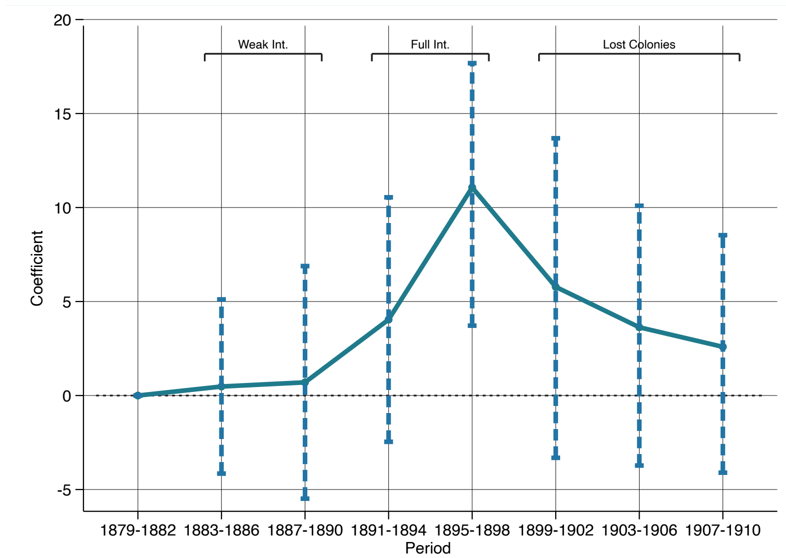
A. Cotton x ....



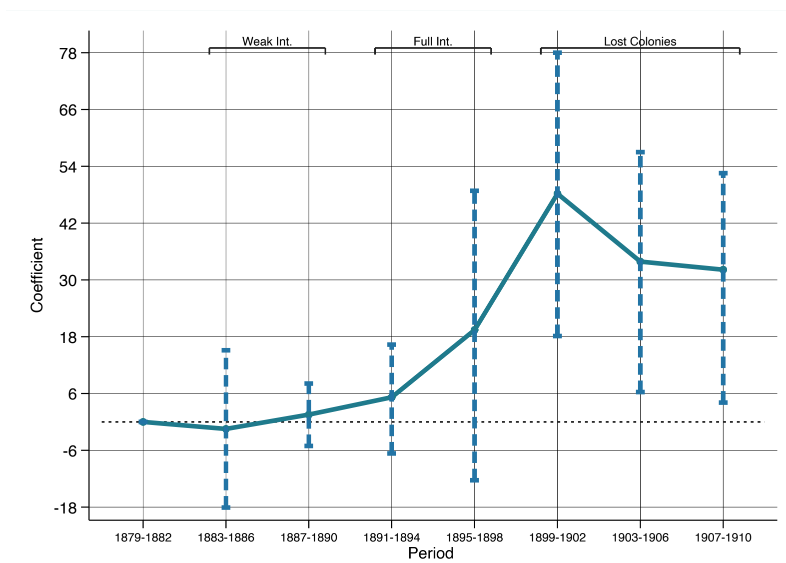
B. Cotton x Weaving....

Notes: Yearly panel form 1878-1911 estimation of the triple difference model including differential technology group trends. Newey–West standard error with a lag length of 3, based onGreene's rule-of-thumb lag length of $T^{1/4}$ rounded upwards. Double cluster standard errors at group and year.

FIGURE D.8. **Event study: Effect market integration and colonies lost on cotton and weaving patents (Only Spanish residents)**



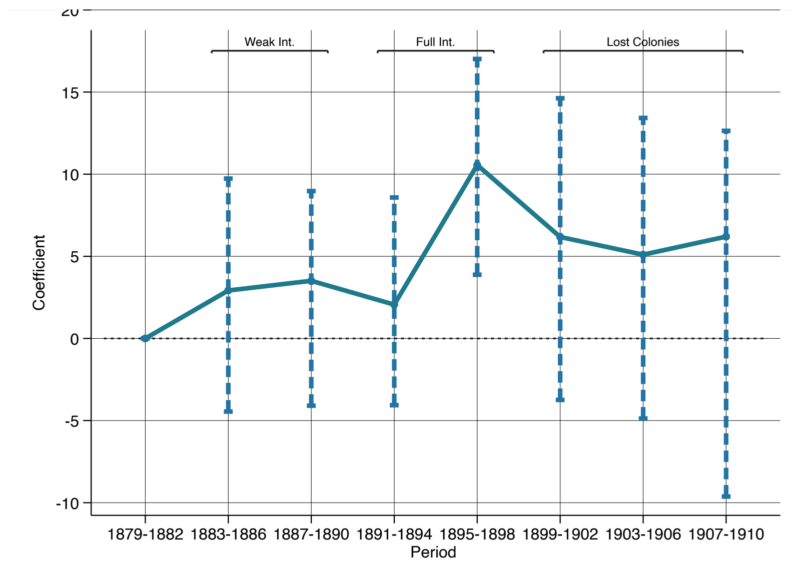
A. Cotton x ....



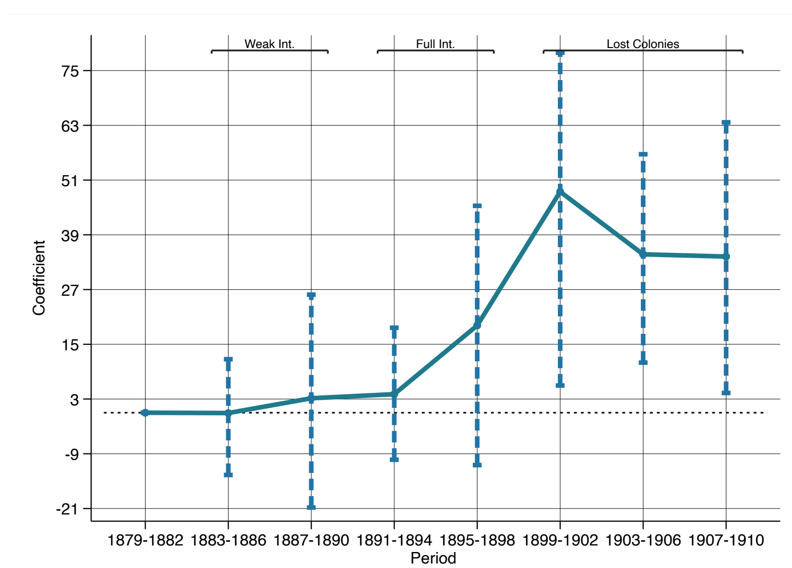
B. Cotton x Weaving x ....

Notes: This figure presents the regression results from equation 5.2 using only Spanish resident's patents. Panel A shows γ_k^1 coefficients and panel B shows γ_k^3 coefficients . 95% Confidence Intervals using randomized inference. I followed the algorithm proposed by Garthwaite (1996) using 20.000 randomization allocations. Total number of observations 496.

Figure D.9. **Event study: Effect market integration and colonies lost on cotton and weaving patents (Controlling by Argentina imports)**



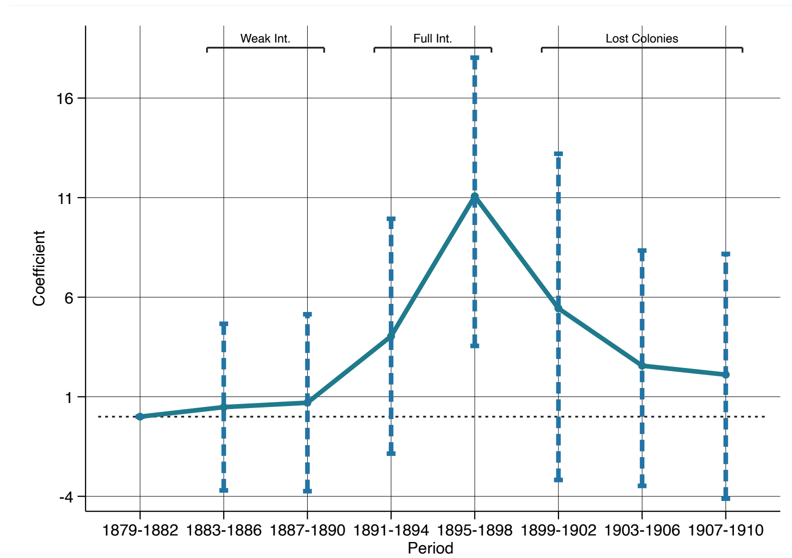
A. Cotton x ....



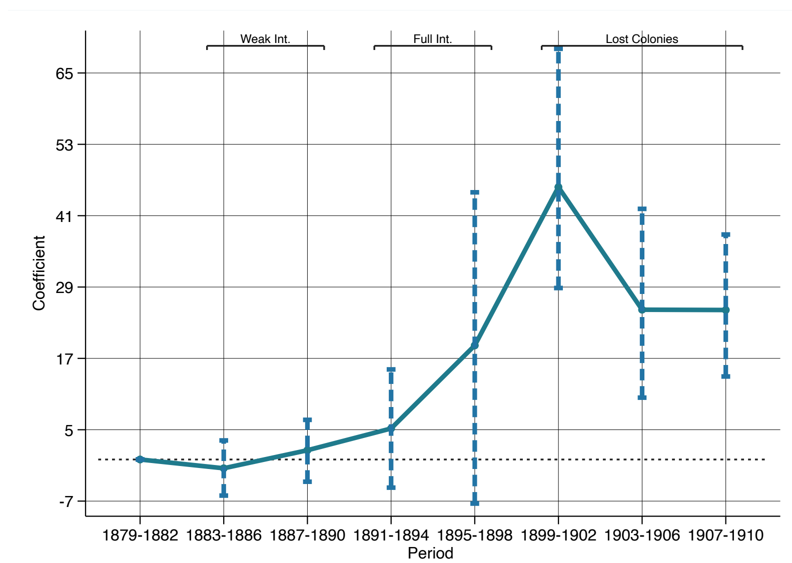
B. Cotton x Weaving x ....

Notes: This figure presents the regression results from equation 5.2 using total patents applications controlling by total Argentinian imports values. I interact the yearly log of total Argentinean imports with technology-category fixed effects. Panel A shows γ_k^1 coefficients and panel B shows γ_k^3 coefficients . 95% Confidence Intervals using randomized inference. I followed the algorithm proposed by Garthwaite (1996) using 20.000 randomization allocations. Total number of observations 496.

FIGURE D.10. **Event study: Effect market integration and colonies lost on cotton and weaving patents (Innovation patents)**



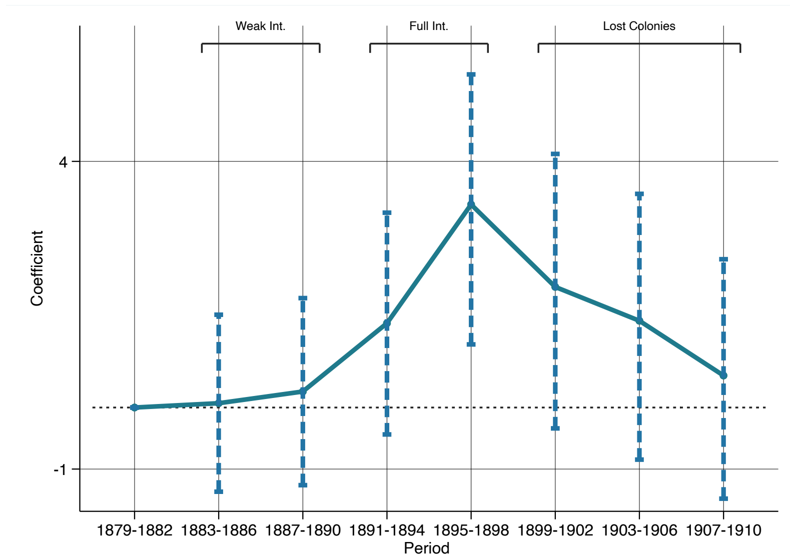
A. Cotton x ....



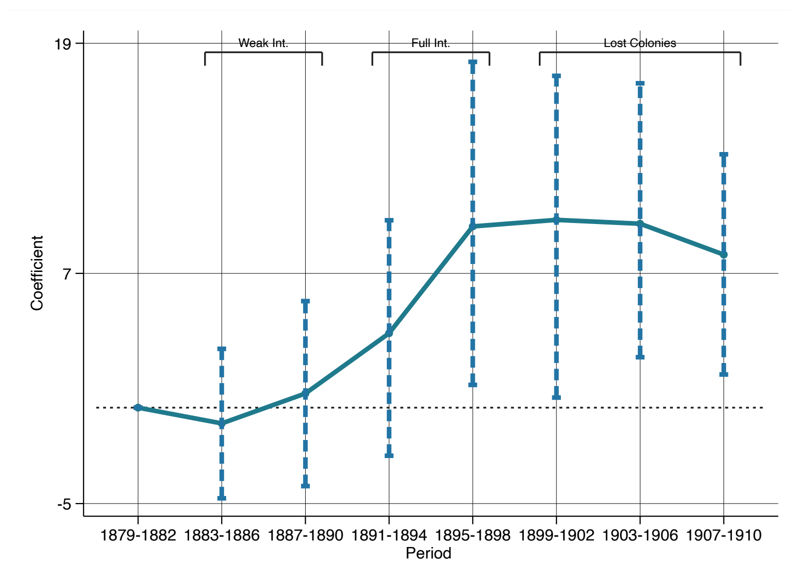
B. Cotton x Weaving x ....

Notes: This figure presents the regression results from equation 5.2 using only innovation patents. Panel A shows γ_k^1 coefficients and panel B shows γ_k^3 coefficients . 95% Confidence Intervals using randomized inference. I followed the algorithm proposed by Garthwaite (1996) using 20.000 randomization allocations. Total number of observations 496.

FIGURE D.11. **Event study: Effect market integration and colonies lost on cotton and weaving patents (High quality patents)**



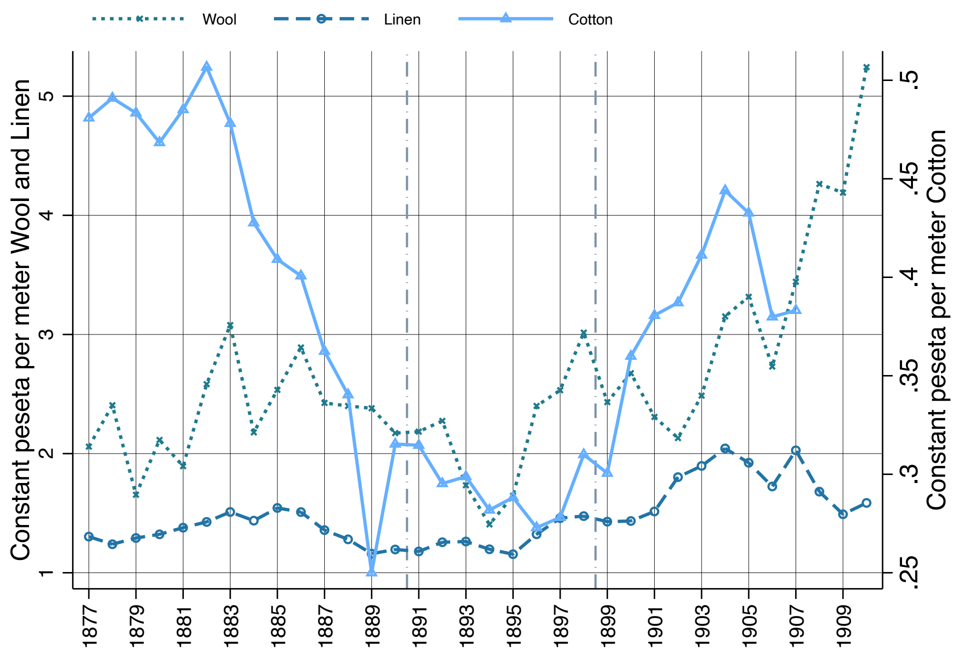
A. Cotton x ....



B. Cotton x Weaving x ....

Notes: This figure presents the regression results from equation 5.2 using only patents have confirmation of being used during the first 2 years after the application. Panel A shows γ_k^1 coefficients and panel B shows γ_k^3 coefficients . 95% Confidence Intervals using randomized inference. I followed the algorithm proposed by Garthwaite (1996) using 20.000 randomization allocations. Total number of observations 496.

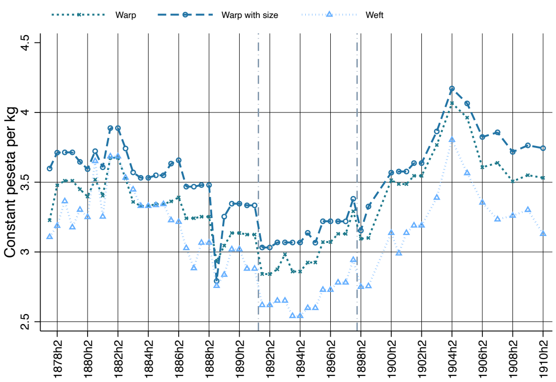
FIGURE D.12. **Cotton, wool and linen prices**



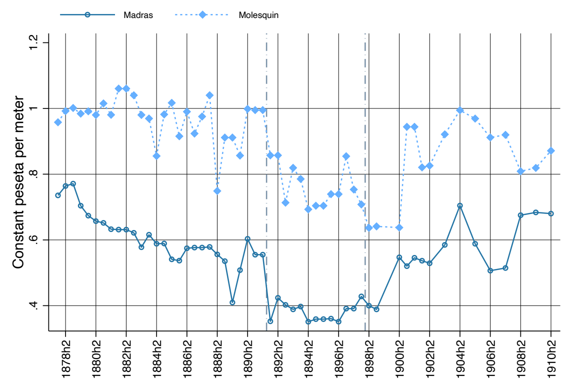
Notes: This graph shows prices series for cotton, linen and wool finished fabric. Cotton price correspond to *Percalina superior lisa* found on inventory ledgers of *La España Industrial*. Wool and linen prices correspond to English export prices to Spain gathered by Nadal Ferreras (1978) in pounds and converted to pesetas using historical series provided online by Rodney Edvinsson. All prices measured in constant pesetas per meter.

FIGURE D.13. **Cotton textile prices and quality**

Panel A: Prices

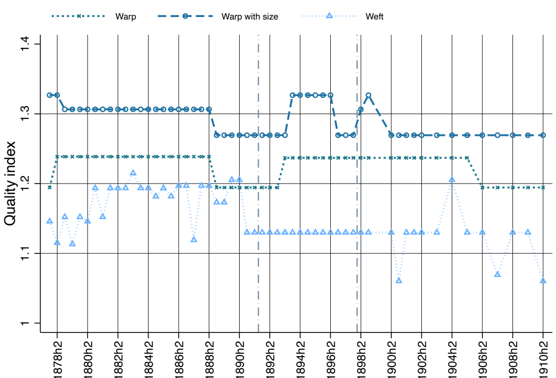


A. Thread

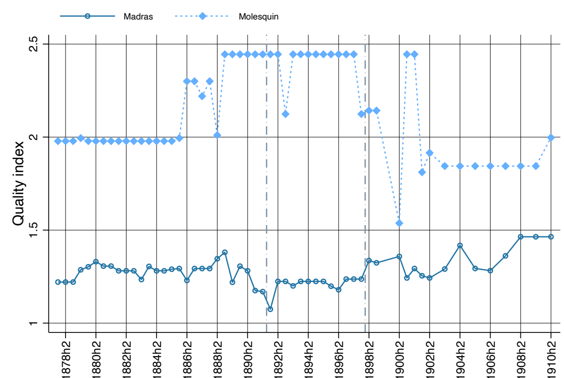


B. Fabric

Panel B: Quality index



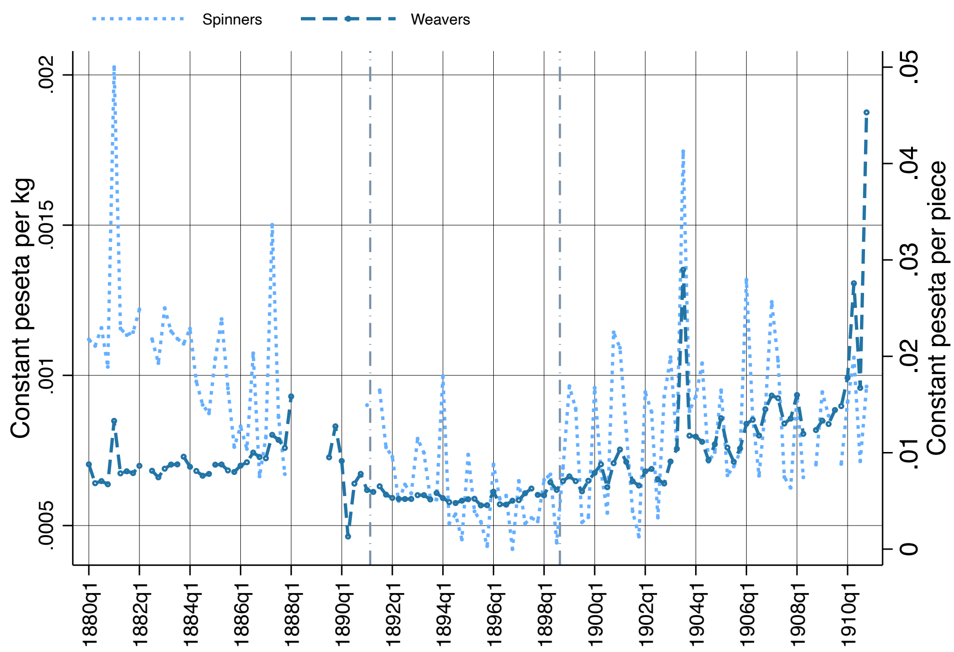
C. Thread



D. Fabric

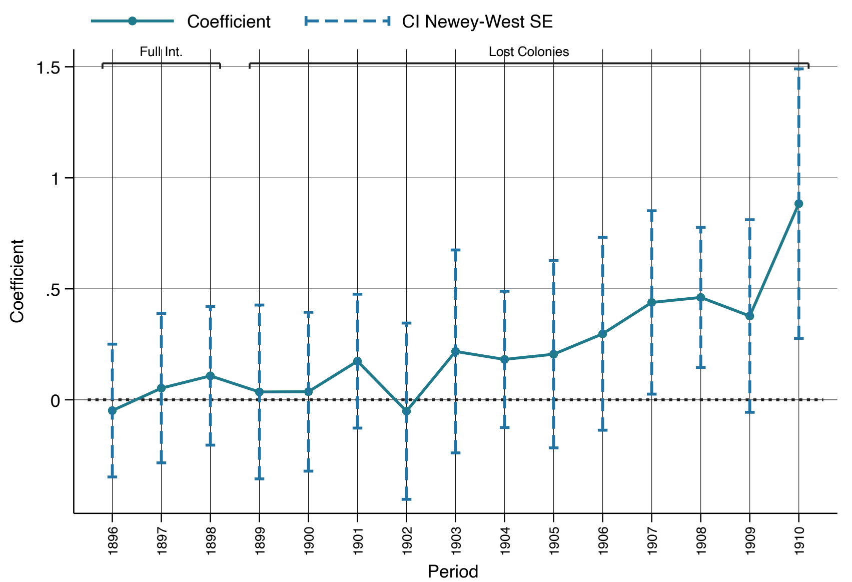
Notes: This graph shows prices (Panel A) and quality index (Panel B) for different product varieties of cotton thread and fabrics. Each series is constructed as an average for price or quality of the available product on the inventory ledgers on each time of period. Data is semi-annually between 1898 and 1902 and yearly between 1903 and 1910. Graphs A and C shows the series for three different thread types: warp thread without size, warp thread with size and weft thread. Thread price is measure as constant pesetas per kilogram. Graphs B and D shows the series for two different fabric types: madras and molesquin. Quality index is measure with respect the lower price product inside the thread or fabric products. Fabric price is measure as constant pesetas per meter.

Figure D.14. **Cotton textiles wages**



Notes: This graph shows wages on cotton industry: spinners and weavers salaries recorded from weekly payroll ledgers of *La España Industrial*. Quarterly data from weeks 1, 14, 27 and 40 from 1880 to 1910. Spinners wage measured as average constant pesetas paid to workers per thread kilogram produced. Weavers wage measured as average constant pesetas paid to workers per fabric piece produced. Information not available between 1888-1890.

FIGURE D.15. **Behavior of spinners and weavers salaries cotton industry**



Notes: This figure shows the coefficients γ_k^W from regression C.1 for each year starting from 1896. 95% confidence intervals using Newey-West standard errors with 4 lags. Quarterly data from 1880q1 to 1910q4. Total number of observations 219.

Appendix E. Tables

Table E.1. textile patent technology classification: 1879-1911

Category	No Cotton	Cotton
Preparation and Spinning		
Mechanical treatment of natural fibrous or filamentous material to obtain fibers or filaments	110	87
Chemical or biological treatment of natural filamentous or fibrous material to obtain filaments or fibers for spinning	46	28
Mechanical methods or apparatus in the manufacture of man-made filaments, threads, fibers, bristles or ribbons	20	21
Chemical features in the manufacture of man-made filaments, threads, fibers, bristles, or ribbons	12	11
Preliminary treatment of fibers	25	96
Spinning or twisting	38	146
Crimping or durling fibers, filaments, yarns or threads, yarns or threads	14	28
Warping, beaming or leasing	6	28
Finishing or dressing of filaments, yarns, threads, cords, ropes ot the like	8	40
Weave		
Shedding mechanism; patterns cards or chains; punching of cards; designing patterns	21	98
Woven fabrics; methods of weaving; looms	184	836
Auxiliary weaving apparatus; wavers tools; shittles	5	106
Knitting	11	82
Textile and Finishing		
Braiding or manufacture of lace, including bobbon-net or carbonised lace; breading machine; braid; lace	35	64
Trimming; ribbons, tapes or bands	13	34
Making nets by knotting of filamentous material; making knotted carpets or tapestries	15	10
Making textile fabrics from filamentous material; non-woven fabrics; wadding	53	172
Sewing	16	147
Embroidering	8	58
Treating textile materials using liquids, gases ar vapours	16	76
Finishing, dressing, tentering or stretching textile fabrics	17	66
Laundering, drying, ironing, pressing or folding textile articles	14	127
Mechanical or pressuring cleaning of carpets, rugs, sacks, hides or other skin or textile articles or fabrics	6	10
Marking, inspecting, seaming or severing textile materials	6	34
Pleating, kilting or goffering textile fabrics or wearing apparel	2	12
Dry-cleaning, washing or bleaching fibers, filaments, threads, yarns, fabrics. Bleaching leather or furs	18	60
Treatment, not provided for elsewhere in class	26	71
Wall, floor or like covering materials	28	3
Dying of printing textiles; dyeing leather, furs or solid macromolecular substances	39	219
Decorating textiles	12	53
Ropes or cables in general	16	26

Notes: List of all patent categories with at least one patent between 1878-1911.

Table E.2. Descriptive statistics province by cotton industry presence

	No cotton presence (1)	Cotton presence (2)	Difference (3)
Log population	12.638	12.768	0.129
	(0.419)	(0.392)	[0.298]
Share of men	0.493	0.488	-0.005
	(0.014)	(0.021)	[0.349]
Share of regular residents	0.963	0.965	0.002
	(0.039)	(0.044)	[0.883]
Share of single	0.535	0.541	0.006
	(0.029)	(0.025)	[0.490]
Share of married	0.400	0.390	-0.010
	(0.031)	(0.029)	[0.253]
Share of literate	0.272	0.195	-0.077
	(0.113)	(0.095)	[0.019]
Share of catholics	0.999	0.998	-0.002
	(0.001)	(0.006)	[0.203]
Share born in the same province	0.933	0.925	-0.008
	(0.088)	(0.056)	[0.716]
Share of regular residents in the same municipality	0.970	0.956	-0.014
	(0.017)	(0.085)	[0.475]

Notes: Column 1 reports mean and standard errors for province without cotton machines in 1879. Column 2 reports mean and standard errors for province with cotton machines in 1879. Column 3 reports differences between province with and without presence of cotton machines. p-value in square brakets.

TABLE E.3. Cross sectional dependence and serial correlation tests Difference-and-difference Model

	Yearly Model (1)		*4 Years Model* (2)	
	Panel A: Cross sectional dependance			
Pesaran CD-test	7.881		14.419	
	[0.000]		[0.000]	
	Panel B: Serial Correlation			
	AR(1)	AR(2)	AR(1)	AR(2)
Q-stat	5.469	5.488	1.610	4.238
	[0.019]	[0.064]	[0.204]	[0.120]
LM-stat			15.915	26.387
			[0.026]	[0.015]

Notes: This table presents the test for cross sectional dependence (Panel A) and serial correlation (Panel B) for difference-and-difference models errors. Panel A null hypothesis is cross section independence against alternative hypothesis of correlation among panel groups. Panel B null hypothesis is not serial correlation against the alternative hypothesis of serial correlation up to order 1 or 2. Q-stat is Born and Breitung (2016) biased corrected test. LM is portmanteau test for serial correlation developed by Inoue and Solon (2006). This test is designed for panels with small number of period observations (T), as in the case of 4 year panel. With moderate number of periods the test is not adequate since its dimension increases with the number of periods. Therefore the test is not suitable in the yearly panel. P-values in double brackets.

TABLE E.4. Cross sectional dependence and serial correlation tests Triple difference model

	Yearly Model (1)		*4 Years Model* (2)	
	Panel A: Cross sectional dependance			
Pesaran CD-test	5.300		5.879	
	[0.000]		[0.000]	
	Panel B: Serial Correlation			
	AR(1)	AR(2)	AR(1)	AR(2)
Q-stat	6.474	7.083	2.835	5.045
	[0.011]	[0.029]	[0.092]	[0.080]
LM-stat			10.516	18.871
			[0.161]	[0.127]

Notes: This table presents the test for cross sectional dependence (Panel A) and serial correlation (Panel B) for triple difference models errors. Panel A null hypothesis is cross section independence against alternative hypothesis of correlation among panel groups. Panel B null hypothesis is not serial correlation against the alternative hypothesis of serial correlation up to order 1 or 2. Q-stat is Born and Breitung (2016) biased corrected test. LM is portmanteau test for serial correlation developed by Inoue and Solon (2006). This test is designed for panels with small number of period observations (T), as in the case of 4 year panel. With moderate number of periods the test is not adequate since its dimension increases with the number of periods. Therefore the test is not suitable in the yearly panel. P-values in double brackets.

TABLE E.5. Response of cotton textiles machines on spinning and finishing sector to market integration and colony lost

	Dependent Variable: Machines per 10.000 Inhabitants					
	Panel A: Spinning				Panel B Finishing	
	Mechanical Spindles		Manual Spindles		Mechanical Raising	Mechanical Shearing
	(1)	(2)	(3)	(4)	(5)	(6)
Cotton ...						
... x Market integration	73.80	117.70	−0.21	2.03	0.02	0.03
	(184.17)	(153.64)	(1.96)	(3.21)	(0.11)	(0.09)
	[[0.662]]	[[0.412]]	[[0.912]]	[[0.496]]	[[0.715]]	[[0.802]]
... x Early colonies lost	−49.04	−4.12	−0.30	1.92	0.04	0.08
	(101.56)	(92.68)	(2.07)	(3.51)	(0.11)	(0.09)
	[[0.672]]	[[0.963]]	[[0.884]]	[[0.555]]	[[0.292]]	[[0.600]]
... x Late colonies lost	−107.70	−5.35	0.93	4.39	0.07	0.07
	(95.94)	(72.15)	(1.90)	(3.05)	(0.10)	(0.09)
	[[0.296]]	[[0.937]]	[[0.612]]	[[0.126]]	[[0.341]]	[[0.389]]
Observations	1716	1144	1716	1144	1144	1144
Material fixed effects	✓	✓	✓	✓	✓	✓
Time fixed effects	✓	✓	✓	✓	✓	✓
Province fixed effects	✓	✓	✓	✓	✓	✓
Controls	✓	✓	✓	✓	✓	✓
Comparison Cotton vs.	W and L	W	W and L	W	W	W

Notes: Control variables include logarithm of population, men share, share residents, single shared population, married shared population, catholic shared, share of illiterate, share of born in same province, share of nationals born in different province, share of regular residents in the same municipality. W stands for wool and L for linen and hemp. Odd columns compare the cotton industry with wool and linen (hemp) industry and even columns compare the cotton industry only with wool industry. Comparison period 1979. P-values from a test based on HC2 standard errors tested against a t-distribution are in double squared brackets. I follow the correction proposed by Imbens and Kolesár (2016). Standard errors in parentheses are clustered on province-year level. * is significant at the 10% level, ** is significant at the 5% level, *** is significant at the 1% level.