TWO

The Theoretical and Historical Origins of Trade Issues

Two competing visions have dominated discussion of international trade for more than two centuries. These ideas, which linger beneath the surface of most contemporary issues, can be seen with greatest clarity in the context of the historical periods that spawned them. Examining the origins of these visions can help us to understand both how each resolves the three dilemmas of trade and why nations have adopted the trade strategies implied by them.

Liberalism and Mercantilism

One vision is that of economic liberalism, which has been dominant in theoretical circles since the very advent of systematic thinking about economics. Economic liberalism was first articulated in precise form by Scottish political economist Adam Smith (1723–1790) in his brilliant masterpiece of 1776, *An Inquiry into the Nature and Causes of the Wealth of Nations*. This school of thought, which was advanced by a long line of British theorists including David Ricardo (1772–1823) and John Stuart Mill (1806–1873), now numbers most contemporary economists among its membership. Economic liberalism is often summarized by the answer it offers to government seeking advice on how to deal with the market: *laissez-faire* (from the French "allow it to act" or "leave it alone").[1] Thus, liberalism holds that international trade should be conducted by private actors largely free of government control. That advice is predicated on the premise that the most important value to be maximized by the state is the consumption of its citizens, usually summarized by a nation's gross national product.

The second perspective derives from mercantilism, a body of thought that originated with the mercantile policy (i.e., commercial or trade policy) of European nations, especially England, from the sixteenth century to the middle of the nineteenth. Though the practice of mercantilism long predated liberalism, the best-known text in the mercantilist tradition is Friedrich List's *The National System of Political Economy*, written in 1841, half a century after Smith's death. List's counterattack against Smith's liberalism is better known than the original doctrine he defends, because the sophistication of Smith and

Ricardo's analysis elevated the rigor of subsequent economic debate beyond that of the narrow and piecemeal writings left by the early pamphleteers who supported mercantilist policies.

Even today, mercantilism is not so much a theory as a bundle of ideas centered around the conviction that governments must regulate trade in order for it to further the **national interest**. Perceptions of that national interest have varied from time to time, from place to place, and from author to author, but most variants of mercantilism have emphasized the goals of national self-sufficiency, a favorable balance of trade, the vitality of key industries, and the promotion of the power of the state, especially in foreign policy. That is, mercantilists resolve the values dilemma by de-emphasizing liberalism's focus on consumption and instead embracing various alternative values. They also resolve the state goals dilemma by elevating elements of the national interest involving security and self-sufficiency above liberalism's emphasis on the desirability of interdependence and cooperation. Because the national interest encompasses a multitude of different goals that must be judged by each nation in its particular circumstances, however, no universal policy advice is offered by mercantilism. Still, protection against imports and the promotion of exports is common to most versions.

Much of the early writing of both mercantilism and liberalism concerned the controversies surrounding the English **Corn Laws**, a series of protectionist measures that regulated the trade of agricultural goods, especially grain, between the fifteenth and nineteenth centuries.[2] Their repeal in 1846 ushered in a period of free trade that represented the triumph of economic liberalism over mercantilism, which had dominated both economic theory and political practice in England for most of the previous three centuries.

However, the history of international trade reveals that the mercantilist inclination to regulate trade, particularly in order to protect domestic producers, has been somewhat more commonly adopted by nations than has the liberal policy of free trade. Perhaps it is more accurate to say that no nation has ever completely accepted or completely rejected either view. Instead, governments have sought to encompass elements of both in fashioning their trade policies. This is understandable because both theories are "true", but neither is universally so. Each is rooted in a set of assumptions that are more valid in some instances than others and each addresses concerns that are more salient to some states' priorities in interests, values and goals than others. As a result, national policies vary, but each is a compromise that reflects a different resolution of the fundamental dilemmas posed by trade.

In this chapter, I examine the debate over the Corn Laws because it so closely parallels contemporary contests between free trade and protection. The lessons of this period help us to understand some of the puzzles of our own era, especially why nations have selected such a great variety of different trade policies, despite liberal theory's ardent and universal advocacy of free trade.

MERCANTILIST TRADE POLICY

Early English mercantile policy involved three major elements: the promotion and protection of industry, the **Navigation Acts**, and the Corn Laws. All involved restricting the scope of markets in international trade, and each is remarkably similar to mercantilist policies widely practiced today.

The motivations for the promotion and protection of industry—we would call their modern counterparts "industrial policy"—continue to inspire contemporary advocates of trade limitations. One goal was the creation of industries that would foster the state goals of self-sufficiency and economic development. This drive was manifested in a variety of actions dating to the time of Queen Elizabeth's reign (1558–1603), including exclusive patents (legal monopolies) to develop domestic industries that could substitute for imports: sugar refining, salt production, glass manufacturing, soap production, and others. Many industries were also introduced into England by government policy that encouraged the immigration of foreign workers with special skills. Once initiated, these industries were then sustained by import restrictions in the hope that eventually they would develop sufficiently to be capable of exporting. Support for **infant-industries** is an integral part of all modern mercantilist policies, including the **import-substituting industrialization** (ISI) common to most of Latin America in the 1950s and 1960s and the postwar industrial policy of Japan.[3] Self-sufficiency and economic development were state goals given greater urgency by the concern that Elizabethan England lagged behind such continental rivals as the Dutch and the French in industrial development.

Exports were encouraged in part because they produced an inflow of **treasure**—gold or silver—to pay for them. Today, we would refer to this net inflow as a balance-of-trade surplus. The revenue earned from exports could be used to purchase goods from abroad that could not be produced at home, such as wine, tea, and spices. Treasure could also be accumulated for use at a later time. Given the crude monetary system of the age, the inflow of precious metals was also necessary to maintain the domestic money supply, especially as the nation shifted from an elementary agricultural economy dominated by barter exchanges and self-sufficiency to a more complex modern economy in which money and credit were needed to facilitate transactions. Exports were also desirable because once established they could be taxed to generate revenue that would support state interests, such as maintaining the navy or sustaining the power of the Crown against domestic challengers. Requiring exporters to secure government licenses also gave government officials the ability to earn revenues while playing favorites among license applicants.

Moreover, exports provided employment for workers and profits for industrialists, both of which fostered the growth of the economy as a whole. Rising employment increased the demand for food and thus benefitted the agricultural sector. The export trade helped to strengthen the merchant marine, which trained seamen for service in the navy, a vital factor in maintaining the power and security of an island nation like Britain. For all these reasons, exports were promoted, sometimes by bounties (subsidies) and sometimes by encouraging the cheap importation of raw materials necessary to manufacture goods for export.

At the same time, however, import restrictions were imposed on most goods. Trade regulations were designed to protect domestic manufacturing industries and their workers from a very early time. The first beneficiary in England, textile production, was protected as early as the thirteenth century, but a parliamentary law of 1337 is the first classic package of infant-industry protection. It included an **embargo** (i.e., prohibition) on the exportation of raw wool to prevent the textile industries of other nations from acquiring this important raw material to compete against English weavers. It also encouraged the emigration of clothworkers from abroad in order to build an English industry that would be capable of exporting finished cloth.[4] Most important, it added a prohibition against the importation of foreign cloth.

Import restrictions of this sort were designed for several purposes. First, they protected the employment of laborers and the profits of owners, considerations that motivate the bulk of import restrictions in the current era. Typical was the act of 1700 in which Parliament restricted the importation of silk textiles from India on the grounds that it would directly endanger the jobs of 250,000 employees in the English woolen-textile industry and indirectly lower the price of wool, threatening the prosperity of the landed interests supported by sheep grazing. Modern-day analogues include the Multi-Fiber Agreement (MFA) and its predecessors, which have protected the U.S. cotton textile industry since 1961.

Second, import restrictions typically took the form of tariffs, which provided a substantial amount of government revenue. This consideration is less relevant in the modern age among developed countries, but it remains central to many less developed countries for the same reason as in early England: Revenues were difficult to raise through general taxation because of the relatively low level of taxable domestic activity and the logistical problems of collection. The importance of this consideration is shown by the necessity of reintroducing the income tax in England as part of the package of import duty reductions between 1841 and 1846 that culminated in the repeal of the Corn Laws. Even in 1994, final U.S. Senate passage of the long-awaited Uruguay Round trade agreement was held up by the need to find $14 billion to replace the import tax revenue that would be lost when tariffs were reduced.[5]

Third, import restrictions were used as a tool of foreign policy both in order to induce other nations to open their markets to British industries and to harm enemies while helping friends. For example, when Jean-Baptiste Colbert raised French tariffs to levels that effectively prohibited the export of English cloth to France in 1667, Parliament retaliated with tariffs and prohibitions on French goods in England. A 1703 commercial treaty imposed a lower tariff on Portuguese wine than on French wine, thus diverting the lucrative wine trade away from France, which was England's greatest political, military, and commercial rival. Retaliatory tariffs designed to bring other nations to the bargaining table are now commonplace; in 1992's "beer war" the United States imposed a 50 percent duty on Canadian beer to protest Ontario's environmental tax on aluminum cans and warehouse charges for U.S. beer. Tariffs are still frequently used as a carrot and stick in other foreign policy areas, such as the U.S. policy of threatening to withdraw the preferential tariff rate known as **most favored nation** status from China in order to induce progress on human rights.

Domestic producers were also favored by another mechanism of protection, the domestic preference sentiment, whose modern expression is found in the Buy America program and the propensity of Japanese consumers to purchase domestic rather than imported products. Then as now, domestic preference was partly a matter of public sentiment and partly a matter of government policy. For example, there was a period in which woolen clothing was mandated for some occasions, including burial, in order to sustain the production of the domestic textile industry. The consumption of herring to sustain the fishing industry was encouraged by mandated "fish days." For a time the importation of Indian fabrics was prohibited by law; at another point, English textile workers took matters into their own hands by throwing acid on women who wore clothing made of Indian calicos.[6] The latter scene anticipates the symbolic destruction of Japanese cars by Detroit autoworkers two centuries later. It also presents a vivid picture of the kinds of distributional trade-offs that liberal theorists remind us always attend import restrictions: The protection of English workers was paid for by English consumers because the price of English woolens was about eight times higher than that of foreign textiles.

The national interest was also protected by the Navigation Acts, which date from 1381. Because defense of an island nation and, later, the maintenance of a far-flung empire required a strong navy, the Navigation Acts required that English grain be carried only by

English ships. This prohibition was designed to stimulate shipbuilding and sustain the merchant marine, which, like the fishing industry, trained sailors in seafaring skills useful to the navy. The Navigation Acts were only one part of an extensive system of government control designed to strengthen naval power. For example, to guarantee that wood supplies for shipbuilding would be available, a 1558 act prohibited timber cutting for use in iron smelting within fourteen miles of the coast. Monopolies were granted by royal letters patent to encourage investment and innovation in the production of munitions and in the mining and smelting of metals required for their production. Thus we see that mercantilist trade policy complimented domestic policy; both were formulated in the pursuit of such nationalistic values as defense and national power. In the modern era, states subsidize national airlines and defense contractors for similar reasons.

The Corn Laws

However, neither the protection and promotion of manufactures nor the Navigation Acts were as controversial as the Corn Laws, which perfectly express the distributional, values, and state goals dilemmas inherent in all trade policy debates. The Corn Laws and proposals for free trade represent polar opposites that illustrate both the arguments that sustained mercantilism and those of economic liberalism that eventually defeated them. The Corn Laws were a complex series of mercantilist trade regulations enacted by Parliament over a period of several centuries in order to control the price of grain. Depending on domestic supplies and prices, both exports and imports of grain were restricted at various times. Sometimes they were discouraged with quotas or taxes, sometimes promoted with bounties or subsidies, and sometimes outright prohibited—but seldom was the market permitted to freely determine prices or trade volumes.

The Corn Laws were initially designed largely to protect consumers. For example, when poor harvests caused a supply shortage and high prices, grain exports were prohibited. Just as consumers required shielding from market forces, government policy recognized the need to protect producers as well. As early as 1463, for example, the importation of low-priced grain from abroad was restricted and producers were allowed to dispose of a surplus through foreign trade. Generally, exports were permitted only when prices were relatively low (thus signaling that supplies were adequate to demand and that domestic consumers were protected from shortages and “unjust” prices) and often only when licensed by the state. This power was contested by the Crown and Parliament, with the Crown preferring regulations that earned it revenue and protected consumers and Parliament tending to the protection of landowners and producers.[7] Prior to 1660, the predominant beneficiaries of government policy were the Crown and consumers, but the Restoration of 1660 increased the power of the landowners in Parliament and the Revolution of 1689 established the dominance of Parliament over the Crown. With these changes in the political balance of power, government policy shifted in favor of producers and against consumers.[8]

Over the next 150 years, the Corn Laws were contested terrain both in academic debates and in practical politics, especially because their differential effects on various groups posed a stark distributional dilemma. Parliament dealt with them nearly annually as weather-related fluctuations in supply drove prices to levels that threatened either producers or consumers. When prices for grain rose, consumer riots were often directed against the Corn Laws, which were thought to be exacerbating supply shortages by keeping out imports and encouraging exports. When prices fell, farmers who rented land would frequently find themselves producing at a loss and landowners would be obliged to lower rents at considerable loss to their principal source of income. Parliament generally tried to strike a balance. On behalf of consumers, exports were prohibited or heavily taxed when domestic supplies were limited. On behalf of producers, plentiful domestic supplies would trigger not only a prohibition or heavy tax on imports but also a bounty (today we would call it an export subsidy) on exports. In this way, producers were encouraged to employ peasants and keep acreage in production in anticipation of years when such capacity might be needed to meet domestic demand.

Thus, an elaborate system of price regulation was maintained with tariffs and export subsidies triggered at a price meant to define the lower boundary acceptable to producers; import subsidies kicked in at a price meant to be the ceiling acceptable to consumers. This cumbersome system was frequently changed by Parliament in response to both annual market conditions and the intense political activity of landowners and peasants—with the petitions of the former being generally more effective than the riots of the latter. However, until the nineteenth century no one seriously advocated the abandonment of the mercantilist market-regulating approach altogether by allowing free imports and exports. The effects of food prices on a range of economic, social, political, and cultural outcomes were far too great to allow them to be determined by uncontrolled forces like market supply and demand.

The desirability of maintaining self-sufficiency in such a critical area as food production was the most consistent argument used by protectionists. Of course, this concern with national security was imbedded deep in the characteristic perspective of mercantilism. Thus, it is ironic that this argument was best stated in succinct form by Adam Smith, whose writing on behalf of free trade made him not only the foremost exponent of economic liberalism but also a much-quoted opponent of the Corn Laws. He noted, simply and eloquently, that “defense is of more importance than opulence.”[9] Protectionists frequently applied Smith’s reasoning to support the Corn Laws even though these words were written in support of the Navigation Acts, which he regarded as necessary for the defense of the realm. (He opposed the Corn Laws, since he did not regard self-sufficiency in food as essential for national security.)

The widespread fear that abandoning agricultural protection would exchange self-sufficiency for a dangerous reliance on imports was founded in the economic and political conditions of the day. Because grain prices were often lower on the continent than in England, tariffs were thought necessary to protect English producers from European imports. Though cheap imports would benefit consumers in the short term, they would mean misery for English agricultural interests and could have detrimental effects for the nation as a whole in the long term. If English grain producers were not guaranteed a steady market, they would begin to shift their production away from these import-competing products or abandon investment in their land altogether. Indeed, a steady increase in sheep pasturing did impinge on the acreage held in grain production. Moreover, many landowners began to devote more time and wealth to investment opportunities in industry and commerce than to improvements in agricultural output. If this trend were to continue over time, protectionists feared, England would come to rely on foreign imports of grain not just in years of a bad English harvest but on a regular basis.

In this period, it is not surprising that such foreign reliance should make mercantilists nervous. It would leave the nation dangerously sensitive not only to weather and other harvest conditions in Europe but also to any disruption of trade. Further, the threat of disruption would reduce the freedom of action that the government of a self-sufficient nation could enjoy in conducting foreign relations.

It was feared that politically motivated disruption of trade could become an instrument of statecraft (or war) that would put England at a severe disadvantage in conducting its foreign policy. Certainly, Elizabeth had been well aware of the advantage possessed by England in its war with Spain: England was self-sufficient in food at that time, but Spain was not. More recently, England's great rival, France, had sharply controlled the export of its grain when it was in short supply at home. Although this was done principally in order to protect French consumers (as was common in England and most other nations), it was feared that such control might also be exercised in order to force foreign policy concessions from England under the threat of mass starvation. Thus, mercantilists sought self-sufficiency where possible. Further, for those products in which England could not achieve self-sufficiency, reliance upon trade with their own colonies, a trade not so sensitive to potential political disruption, was preferred to trade with rival continental powers.

The interruption of trade by large-scale war was also justifiably feared not only because England was at war with France during most of the period from 1793 to 1815 but also because war had been a frequent occurrence in Europe for centuries. Indeed, between 1562 and 1721 there were only four years in which all of Europe was at peace.[10] Moreover, England would not want to be put in a position of actually aiding an enemy. Sir Henry Parnell's support of the highly protectionist Corn Law of 1815 called attention to England's heavy importation of wheat and flour from France in 1810, which had enabled Napoléon to both quell an insurrection in southern France and collect heavy export duties that were used to strengthen the French war effort. This resolution of the state goals dilemma--emphasizing market controls to protect national security, self-sufficiency, and state power--is characteristic of mercantilist inclinations even today.

The protection of agriculture to keep prices and land rents high also had a justification rooted in the values dilemma. The maintenance of a strong agricultural sector was a value synonymous with the preservation of a prosperous and peaceful rural community, which from time immemorial had been the heart of English society as well as the core of the economy. When debates required that a policy's effect on national prosperity be defined and measured, the usual method was to invoke the strength of the rural sector. In turn, this usually meant that the well-being of landowners—especially the level of land rents—was used as a criterion. John Locke gave expression to this widely accepted interpretation: "An infallible sign of your decay of wealth is the falling of rents, and the raising of them would be worth the nation's care, for in that ... lies the true advantage of the landed man and with him of the public."[11]

Since the social ideals of the landed gentry dominated both Parliament and the national culture, it is hardly surprising that the vision of England that motivated national policy remained rooted in this traditional, romantic, and self-serving view. Similarly, the protection of rice production in contemporary Japan can be explained partly by its enormous symbolic significance for Japanese tradition and partly by the predominantly rural political power base of the long-ruling Liberal Democratic Party. Mercantilism represents both a choice among alternative values and a preference among distributional outcomes.

Given the material conditions at the time, equating national prosperity with the wealth of landowners did have considerable merit. It was the income derived by landowners from ground rents that fueled the entire economy. Most investment originated in the savings of landowners, even that which built the manufacturing sector that eventually transformed the nation. Government revenues depended directly on the wealth produced by ground rents, since taxes were largely raised from these same landowners. Of course, definitions of national prosperity were inevitably to change as the economy became more reliant on manufacturing for profits, for savings and investment, for employment, and for taxable income. In the process, industrial development allowed capitalists to offer an alternative vision of England just as the advent of political democracy allowed the masses to suggest an alternative definition of what constituted national prosperity. Values can seldom be wholly separated from economic and political conditions.

The Roots of Mercantilism

The mercantilist view that international trade should be sharply regulated cannot be understood in a historical vacuum. Indeed, far from an aberration, it is a natural outgrowth of then prevalent theoretical and ethical perspectives on *all* markets. Prior to the evolution of modern economic society, free markets were no more common in the domestic economy than they were in international trade. In fact, mercantilism thrived in an environment in which none of the three elements of economic liberalism identified earlier— individualism, private property, or the free market—were widely accepted in either theory or practice.

The absence of these three elements is best illustrated by the communal character of agriculture, the dominant sector of the economy, as it had been widely practiced in England for centuries.[12] The open-field system of production was marked by a collective "commons," joint labor, and production decisions made at the village level. In a typical village, an individual would own or rent several small strips of land, but they were seldom contiguous. Because they were so intermixed with the plots of others, because the boundaries between them were not fenced, and because the entire open field would be given over to communal pastureland after the harvest, independent decisionmaking—entrepreneurship—was impossible and collective cultivation was imperative. If individualism was thus limited, so too was the freedom to use private property as one saw fit. The overlapping network of obligations typical of feudal systems meant that land ownership was not absolute. Though economically inefficient, this system promoted equality and full employment among agricultural laborers while it served as the basis for social interaction. The well-ordered village was the ultimate expression of the values of the period: It was a stable collective maintained by an ethical system rooted in a strongly hierarchical conception of society. It was also more or less self-sufficient, with most local production consumed locally rather than being sold on a larger market.

Prior to the nineteenth century, reliance upon the unregulated market was also uncommon outside of agriculture. The reasons parallel the three factors introduced in Chapter 1 to explain the choice of foreign economic policy by any nation. First, ethical considerations that originated in medieval social and economic theory cast doubt on the justice of markets. Second, material conditions did not allow efficient markets to develop. Third, the most powerful actors of the period—the church, the Crown, and landowners—were satisfied with the regulated economic system.

In the medieval period, it was believed that commodities should be sold at just prices that would enable each man to "have the necessaries of life suitable for his station."[13] To engage in a transaction that did not meet that standard was to commit the sin of avarice, punishable by both the church and the state. For example, in order to guarantee just prices, the parliamentary act of 1552 severely regulated the activities of brokers or merchants, prohibiting supply manipulation designed to increase prices and the resale of grain at a higher price in the same local market.

This last regulation is a striking reminder that the ethical status of markets and the morality of activities that benefit from their operation was a highly controversial issue centuries before Marx's critique of capitalism. Among the most visible manifestations of the moral outrage generated by market operations is the famous Rusby trial of 1800. During a period of grain shortage that had driven up food prices, riots were commonly directed against the brokers who were blamed for much of the price increase. John Rusby, a London jobber, was alleged to have purchased a lot of oats at a price of 41 shillings and to have resold a part of it later that same day for 43 shillings. This action, which today would be considered profitable and altogether legal brokerage, was regarded in the medieval tradition as unethical "regrating" and prohibited by local regulations throughout much of England long before it was codified in national law in 1552. These specific statutes were repealed in 1772 and 1791, but the offenses were still punishable under the common law. More important, they were still considered unethical—a violation of common morality—by the bulk of the population, especially when seen to contribute to prohibitive prices in a time of food shortage and economic desperation. Rusby was found guilty and heavily fined—and a London mob intent on lynching him destroyed his house. Similar riots in sympathy occurred throughout the nation.

According to medieval social theory, a divergence was generally acknowledged to exist between private interests and the public interest. Because this divergence made it a duty of government to protect the community from the harmful effects of the market, commerce and industry were also sharply regulated during the entire mercantilist period. For example, in addition to restraints on brokers, market regulation to protect consumers also included a standard system of weights and measures for various consumer goods, especially food and cloth. Laws governing the size and composition of bread loaves had existed for centuries before being meticulously codified by the Tudors and Stuarts beginning in the sixteenth century.[14] In conformity with accepted moral law, it was said that "the most desirable course is that prices should be fixed by public officials, after making an enquiry into the supplies available and framing an estimate of the requirements of different classes."[15] To that end, prices were fixed for various commodities at various times, especially bread and coal but also sometimes cloth, ale, and tea, among others. The market might serve the private interest of the seller, but it was not trusted to yield the just prices that were deemed to be in the public interest.

Restrictions on financial and labor markets were even more severe. Moneylending at excessive interest rates was prohibited by **usury laws** that were not finally repealed until 1854. Indeed, not until 1545 was money lending at *any* interest rate sanctioned by Parliament. These laws merely codified accepted moral standards that go back to biblical times. Parliament also mandated that wages be fixed by local justices of the peace rather than established by the supply and demand for labor, though the practice does not seem to have been universally followed. Finally, a minimum-wage law to protect workers (in the woolen industry) first appeared in 1604.[16] Thus, the regulation of markets to guarantee justice and to protect both consumers and workers has been an established governmental obligation in the Anglo-American tradition for centuries.[17]

It is undeniable that government regulation of the market was rooted in the ethical values that the church successfully transmitted from the early ages of Christianity. But the condition of markets during this period was also a significant spur to government action in support of those values. Limitations of transportation, the relatively low level of commercial activity, guild controls, and modest standards of living combined to generate markets that were, in the vernacular of our age, "thin." That is, limited supply and demand left prices unstable and easily manipulated by unscrupulous profiteers. Thus, government control was directed not so much at the competitive markets extolled by modern economic theory but at the monopolistic or oligopolistic markets then most common.

The absence of individualism and free markets was especially striking in the area of trade, where the interests of powerful actors were as much an explanation as prevailing theory or the condition of markets. Initially, towns attempted to maintain self-sufficiency in key products, an effort that was mirrored in the drive for national self-sufficiency in later centuries. Moreover, trade between towns was sharply controlled by local merchant guilds as early as the twelfth century. Members of the guild were able to prohibit non-members from engaging in trade or to tax them for the privilege of doing so. In exchange, guild members were required to permit other members to participate in any transaction that they arranged and to share its benefits. Clearly, individual entrepreneurial activity was neither valued nor rewarded. Like in the agricultural system earlier described, there were few opportunities for individual enterprise. Unquestionably, economic liberalism could not thrive in such an environment; indeed, its principles could not even be clearly articulated.

Mercantilist and Liberal Responses to Trade Dilemmas

Mercantilism	Liberalism
1. Value trade-offs	
Trade should be regulated to achieve social justice, national economic development, stability, and self-sufficiency.	Trade should be free to maximize efficiency, productivity, consumption, and freedom.
2. Distributional outcomes	
Trade should be regulated to shield consumers from high prices and to protect producers, landowners, and workers from foreign competition.	Trade should be free so as to benefit the most efficient (i.e., industrialists).
3. Effects on the state	
Trade should be regulated to achieve state power and wealth, national security, and autonomy.	Trade should be free to achieve interdependence and peace.

Against this backdrop of suspicion of markets and their sharp regulation in the domestic sphere, it was natural that similar attitudes would prevail as trade expanded from the intertown to the internation arena. The East Indies and Hudson Bay trading companies exerted an oligopolistic control of trade with British colonies analogous to that of the merchant guilds. It can hardly be surprising that international trade was also heavily regulated by the government in the mercantilist age.

In fact, mercantile trade policy represented a distinctive response to each of the three dilemmas with which this book began: those concerning competing values, distributional outcomes, and effects on the state. The government controlled markets, especially those in international trade, in order to affect specific distributional outcomes such as the protection of consumers and grain producers. Mercantile trade policy also pursued the values of social justice, national development, and self-sufficiency more consistently than the values of efficiency and profitability associated with liberal trade ideas. Finally, advocates of mercantilism saw unregulated trade more as a threat to state power, autonomy, and national defense than as a guarantor of international peace.

THE DEMISE OF MERCANTILISM AND THE BIRTH OF LIBERALISM

This variant of mercantilism evolved in response to existing conditions in the economy and foreign affairs, in tune with prevailing currents of social, ethical and economic theory, and in recognition of the realities of the distribution of power within and among nations. These three factors, sketched in the conclusion of chapter 1, account for why mercantilism initially prevailed, but changes in them also explain its eventual demise: even while mercantilist trade policy was dominant, the foundations on which it had been erected were crumbling. Initially, the rise of the market was driven by rapidly changing material conditions at the same time that the values impeding it fell into decline. As a result, English industry advanced more rapidly than its foreign competitors. Then, the advent of liberal theory justified government policies that further strengthened the role of markets, especially those in international trade. Finally, the rise of social groups that championed free trade dramatically shifted the balance of political power domestically. By examining each of these in turn, we will see why mercantilism was seen as a curious anachronism by the middle of the nineteenth century and as ill suited to meet the modern challenge.

But be forewarned: In the next chapter, I also trace the demise of the very free trade system whose ascent is about to be chronicled. Although classical mercantilism is necessarily rooted in time and place, analogous factors have produced neomercantilist forces that influence economic policy everywhere. Thus, the changes that swept away mercantilism—especially the abandonment of the Corn Laws in 1846—should be seen as paving the way for the amalgam of mercantilism and liberalism that has emerged in our own time. Today, variations among nations in prevailing theories, market conditions, and power balances explain why they have chosen trade policies that reflect different resolutions of the dilemmas concerning alternative sets of values, state goals, and distributional patterns.

THE RISE OF THE MARKET

Rapidly evolving material conditions lie at the hub of economic, political, and social changes. The center of economic life was shifting from the countryside to the towns in response to the major improvements in machinery and factory technique that we refer to as the Industrial Revolution. The rapidly growing population, much of it increasingly located in industrial towns, fueled a large increase in demand for grain. Dramatic improvements in domestic transportation systems were also permitting a much longer range exchange of goods, so that grain surpluses in one area could be more easily marketed elsewhere.[18] Improvements in transportation were making international trade easier as well, so that demand from abroad encouraged increases in production and the threat of supply from abroad motivated English producers to improve production techniques and lower costs.

The communal style of agriculture, which was so admirably suited to the milieu in which it arose, could not adapt to these changing needs because it was hopelessly inefficient. Thus, the **enclosure** movement, in which the open fields and commons were enclosed (i.e., privatized and permanently fenced), that had been under way as early as the late Middle Ages, accelerated dramatically and contentiously after 1765. By the early nineteenth century, the predominant form of agricultural production had become capitalist rather than communal; land was owned by individuals in much larger, more contiguous, and permanently demarcated plots and worked by either wage labor or tenants who paid rent.[19] The agricultural system became more attuned to the market and less reliant on communalism, accepted practice, and government control. Land was bought and sold on the open market much more freely than in the past, labor was hired at market-driven wages when needed and dismissed when no longer required, and production decisions concerning cropping and grazing were made by individuals with an eye toward maximizing profit. The result was a sharp boost in efficiency: Agricultural output increased and the labor required to produce it decreased.

But the enclosure movement produced enormous controversy and extensive violence. It did so precisely because it so vividly illustrates two of the dilemmas of relying upon markets, whether in international trade or in domestic agriculture. Free markets, though more efficient and productive, produce distributional consequences and compromise other values. Enclosure resulted in large-scale unemployment of agricultural laborers and their eviction from the land. The heart of the old society—the slowly changing, self-contained, communitarian village—was ripped apart. Social harmony was strained and public order was undermined by the riots that frequently accompanied enclosure. The attitude of the villagers toward forced enclosure expresses these dilemmas:

> True, our system is wasteful, and fruitful of many small disputes. True, a large estate can be managed more economically than a small one. True, pasture-farming yields higher profits than tillage. Nevertheless,... our wasteful husbandry feeds many households where your economical methods would feed few. ...In our unenclosed village there are few rich, but there are few destitute, save when God sends a bad harvest, and we all starve together. We do not like your improvements which ruin half the honest men affected by them. We do not choose that the ancient customs of our village should be changed.[20]

At issue was a clash in ethical viewpoints. The traditional view regarded land ownership as principally a stewardship, an obligation to maintain a system that produced products for the public good and sustained gainful employment for the peasants who worked the land and constituted the village. The profit derived by the landowner was an important component of the whole organism—because he too had a right to the standard of living properly associated with his station—but the profit motive did not assume the primacy that it was to achieve in later liberal economics. The more modern view stripped from the ownership of property any obligation to use it for the public good and asserted that a fundamental right associated with the ownership of property—indeed, the very meaning of "property"—was the freedom to use it in whatever way its owner saw fit. It was not within the purview of society as a whole or the state in particular to judge whether that use was in the public interest.

These changes were symbolic of a larger transition in the realm of values and social theory, from a largely religious conception of society built upon an ethics of duties and obligations to a more secular vision that emphasized an ethics of rights—especially property rights—originating in natural law. It substituted for the communitarian vision of social organization an individualist conception, which reached its height with the British liberal theorists John Locke (1632–1704), who exerted such a powerful influence on the American constitution, and John Stuart Mill (1806–1873), whose passionate defense of the freedom of a citizen from the government still stands as the foremost statement of liberal thought with respect to civil liberties.

These transformations in values were brought about in part by the diminishing influence of the church as it became subordinated to the government after the Reformation and in part by changes in religious doctrine and social ethics associated with the Reformation itself. In particular, many theorists, most famously Max Weber in his 1930 classic *The*

Protestant Ethic and the Spirit of Capitalism, have ascribed the "triumph of the economic virtues" to the influence of Puritanism, which not only tolerated profit-maximizing behavior that had been condemned by more traditional religious teachings but elevated such practices to the status of moral virtue. Weber's Protestant ethic was not merely a commitment to hard work in pursuit of a calling in order to glorify God but a drive for achievement that included sharp business dealings and canny calculation of the means to achieve wealth. With these changes came greater tolerance for market outcomes in which those with greater bargaining power benefitted at the expense of those with less. Over time, the justification for profit seeking came to be rooted much more deeply in the secular utilitarian ideas familiar to us today than in any religious precepts. With this evolution a separation developed between the realm of ethics and the realm of business, with organized religion ceasing to have much to say about the latter.[21] It is no coincidence that the full elaboration of an economic theory relevant to the age arrived only after this division between ethical thought and economic management had become accepted. Liberalism emphasized the expansion of productive output as its goal and reliance upon individual entrepreneurship and market forces as the means to achieve it. Both were too discordant with the older Christian tradition to have been tolerated in the earlier society, which was organized around its ethical precepts.

Contemporary Parallels

Increasing reliance on markets induces distributional changes and value clashes.

As the communitarian state-controlled economy in Russia has given way to an individualistic market-based system, unemployment and inequality has grown. A recent poll in Russia revealed that 48% would prefer an economic system based on "state planning and distribution" and 35% "private property and the market" (Economist, December 18, 1999, p.21)

In Africa, leaders like Tanzania's Julius Nyerere and Ghana's Kwame Nkrumah rejected capitalism and sought to build a traditional African collectivist economy that extolled human dignity, often centered around the traditional village.

This attitude change, like the increased prominence of the market in determining social outcomes, was neither universal nor complete. Not surprisingly, it was centered among the commercial and merchant classes that benefitted most from it, while those who suffered from the insecurity and inequality inherent in impersonal market forces longed for the protection afforded by social institutions that embraced values other than the maximization of material profit. Thus, the enclosure movement proceeded not only because of the efficiency gains it promoted but because its distributional consequences were favorable to political forces that were on the rise. In particular, enclosure was beneficial to the landed gentry both because it produced greater profits and because it divorced the rights of landowning from its customary obligations to maintain stable employment for the peasantry. Because the Crown was more deeply committed to the values of the traditional village than to increasing agricultural production, the government at first opposed the commercialization of agriculture, the enclosure movement, and the transition from crops to pasture. However, with the coming to political power of the landed gentry after 1660, government policy began to change. As the Industrial Revolution shifted the demand for labor and food after 1765, public law strongly favored enclosure and the production changes it permitted. These changes were both inevitable and, on balance, desirable: The huge improvements in living standards of the masses and the emergence of Britain as a world power would have been impossible without them.

Many of the same forces that led to greater reliance upon free markets in agriculture also brought about laissez-faire policies in other areas of the domestic economy. For example, domestic price regulation, which was opposed by increasingly powerful industrialists, had begun to fade by the middle of the seventeenth century. As early as 1437 Parliament moved to limit the interference with free markets by craft guilds.[22] The merchant guilds that controlled domestic trade disappeared long before their counterparts in international trade.

A critical factor was that the Crown, which had been the principal agent of market regulation, was too weak after the Restoration to maintain control of a complex, expanding economy. Merchants and industrialists were restive and intolerant of a government regulatory system that constrained their activities, created artificial monopolies in the interests of political favorites, and induced inefficiency and corruption. The limits of government control had been surpassed, perhaps most vividly in the Corn Laws themselves. The balancing act between keeping prices low enough for consumers but high enough for producers had always been difficult; the unwieldy system of prohibitions, sliding-scale duties and bounties, and trigger prices required frequent amendment and even more frequent temporary suspension in the face of changing market conditions. As increased demand and larger-scale trade induced even greater price fluctuations, it became evident that government could not control even this relatively simple market. Effective management of more complicated arrangements seemed unlikely, especially in labor markets, financial markets, and long-distance trade.

Thus, laissez-faire principles slowly came to eclipse government regulatory arrangements. Wage control was abandoned in the woolen industry, the core of the emerging industrial sector, in 1756. Employers were no longer required to maintain employment for workers during a depression. The apprenticeship system of the craft guilds was also rapidly in decline when finally abolished in 1835. Consumer-protection laws that regulated production standards for cloth disappeared.[23] It was in this environment that free trade theory emerged.

THE ADVENT OF FREE TRADE THEORY

In 1751, Charles Townshend wrote a pamphlet on the Corn Laws that foreshadowed later liberal arguments. He attacked import restrictions and export bounties that raised the price of grain not because of their impact on agriculture but on the then-novel grounds that they injured English manufacturing industries. He noted that when food prices increased, the wages paid to manufacturing workers had to increase in order to cover their “necessaries.” The resulting price increases in finished goods made English industry uncompetitive with that of other nations. This was especially damaging because English import restrictions had exactly the opposite effect on nations with whom England competed: Preventing foreign farmers from exporting their grain to England tended to keep grain prices low abroad just as it kept grain prices high in England. This enabled foreign wages to remain relatively low and finished products, correspondingly cheap.

This basic argument, strengthened, as we shall see further on, by the later elaboration of Adam Smith, was central to parliamentary debate in 1791, which for the first time featured explicit arguments for free trade derived from theoretical ideas. It was also during this debate that the first major clash occured between the landed interests that dominated Parliament and the growing commercial and manufacturing cities of the Midlands and North. Prior to this, arguments for free trade lacked the gravity they would later attain due to the changing economic structure (especially the dominance of the manufacturing sector), social structure (especially the growth in size of the cities), and political structure (especially the importance of the capitalist class). Nor had the theoretical ideas themselves developed sufficient cogency until presented systematically by Adam Smith in 1776.

With agricultural interests still dominant in Parliament, the last highly restrictive Corn Law was adopted in 1815. This marked the high point of both agricultural protectionism and the class antagonism that was increasingly attendant to these issues. During the parliamentary debate of 1813 to 1815 fierce rioting against the proposed legislation occurred since most Londoners were convinced it would mean higher food prices. Further, the class bias in favor of landowners manifested so clearly in this bill was also evident in the debate surrounding it. As a result, all of the ire of the lower classes over food prices, which had long fallen on brokers such as Rusby, was now directed against the Corn Laws and the landed members of Parliament who supported them. It was against this law that the agitation for free trade was directed in the following thirty years, bequeathing to us such a rich literature of theoretical and practical considerations.

The arguments for free trade, which had surfaced in a less systematic way at least a century previously, became imbedded in the evolving theoretical edifice of economic liberalism, championed most visibly by Adam Smith and the English economic theorist (and member of Parliament) David Ricardo. Smith's argument for free trade rested on the concept of **division of labor** and drew a parallel with the argument concerning specialization in the domestic economy that was at the time better known and more widely accepted.

By the end of the eighteenth century, a reasonably extensive domestic division of labor had already developed: Individual peasants did not make their own shoes, grind their own grain, bake their own bread, weave their own cloth, or tailor their own clothing. With the growth of the town and specialized artisans, it became apparent that considerable savings could be achieved by concentrating one's efforts on producing that good which took advantage of the skills and productive resources at hand and by contracting through domestic trade for the other necessaries of life. For example, the skilled artisan was a better weaver than a peasant, owing to his more extensive tools, better access to quality materials, acquired skill, and advantages of specialization. It was more practical and profitable for all parties to enter freely into the division of labor—that is, to specialize and trade—than to maintain self-sufficiency.

This argument was key to gaining ethical acceptance for the role of the market. Liberal theory contended that free markets would serve the highest moral purpose by maximizing aggregate consumption and thereby maximizing the welfare of the entire society. This position was wholly compatible with the emerging materialist conception of welfare and utilitarian ethical standards, though it remained at odds with the prior ethical tradition.

Smith applied the division of labor logic more broadly. The birth of modern international trade theory can be traced to his memorable phrase, "What is prudence in the conduct of every private family, can scarce be folly in that of a great kingdom."[24] If local trade between the artisans of a town and the peasants of the surrounding countryside can benefit both, if interregional trade between the grain-producing regions of England and areas where the land is more conducive to sheep grazing can be mutually beneficial, why cannot international trade that capitalizes on the respective blessings of different nations be equally advantageous? Thus, nations, like families, should specialize in some products for sale (exports) while acquiring others through purchases (imports).

The important intellectual breakthrough supplied by liberal thought is its blurring of the distinction accepted in medieval economic theory between the public good and the private good. Indeed, liberalism in its rawest form virtually dissolves that distinction. In this famous passage, Smith maintains that the pursuit of maximum profit by individuals inevitably steers them—as if guided by the so-called invisible hand of self-interest—toward behavior that maximizes the benefit of the community as a whole:

> As every individual ... endeavors as much as he can both to employ his capital in the support of domestic industry, and so to di
> its produce may be of greatest value; every individual necessarily labours to render the annual revenue of the society as great as
> indeed, neither intends to promote the public interest, nor knows how much he is promoting it.... He intends only his own gai
> in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse
> not part of it. By pursuing his own interest he frequently promotes that of society more effectually than when he intends to pr

Inherent in this logic is the assumption that because all individuals are best equipped to make production decisions concerning their own skills and circumstances, they will naturally specialize in the production of the good in which they have a competitive advantage. Applying the same principle to international trade, Smith thus contended that trade barriers limit not just the private benefits but the public benefits of the gains from trade that accrue to the nation as a whole.

The most elaborate expression of this gains-from-trade argument appeared in Ricardo's 1817 classic, *The Principles of Political Economy and Taxation*, written forty years after Smith's masterpiece and building considerably upon it. Ricardo's famous example of the gains to be achieved by trading British cloth for Portuguese wine remains a powerful statement of the liberal position for free trade.[26] He began with the supposition that the climates, lands, and skills of the people were different in England than in Portugal and that the requirements for successful production of goods such as wool and wine were thus better met in one than the other. Because of this combination of what Smith earlier had called "natural advantages" and "acquired advantages," England was an efficient producer of wool cloth and Portugal an efficient producer of wine. Ricardo observed that each has an advantage in the production of one of the two goods, which he expressed in the form of the amount of labor required to produce each good in each country.

The example displayed in Table 2.1 is in the spirit of Ricardo's original, though the numerical exposition has been simplified to ease the application. Suppose that given the climate, soil, and manufacturing capital available in England, a worker would be capable of producing either two yards of cloth or one gallon of wine per hour. Suppose further that a worker in Portugal could produce only a single yard of cloth but two gallons of wine in the same time. England would be said to have an **absolute advantage** in the production of cloth, and Portugal possessed an absolute advantage in the production of wine.

To see that trade between them would be profitable to both, consider the levels of production in the absence of trade, assuming that both countries chose to produce the same amount of cloth as wine. In England, 100 hours devoted to the production of cloth and 200 hours to the production of wine would produce 200 yards of cloth and 200 gallons of wine. In Portugal, that same production—200 units of each good—would require that 200 hours be devoted to cloth and only 100 to wine.

But suppose that each producer observed these relative advantages and chose to specialize in the production of only one good and to trade part of that production for the other. The English worker, specializing completely in cloth, could produce 600 units of cloth and the specialized Portuguese worker could produce 600 units of wine. If they then agreed to trade 300 units of one for 300 units of the other, each nation could consume 300 units of both goods, whereas in the absence of specialization and trade, each could consume only 200 units of each good. The gains from trade consist of the increased consumption made possible by each producer allocating his resources in the most efficient way.

But Ricardo saw beyond Smith's idea of absolute advantage, illustrated in Table 2.1. He observed that profitable trade could occur between the two countries even if the worker in one country was more efficient in the production of both goods than the worker in the other country. This idea, illustrated in Table 2.2, is Ricardo's enduring legacy to contemporary international trade theory: the theory of comparative advantage. Here, England is more efficient than Portugal in the production of both goods: An English worker can produce 3 units of wine and 6 units of cloth per hour, and the Portuguese worker's efficiency is the same as before—2 units of wine and 1 of cloth. Although England has an absolute advantage in the production of both goods, Portugal is said to have a **comparative advantage** in wine because its workers can produce more wine than cloth and the reverse is true in England. As a result, trade can still be profitable.

In this example, without trade England would divide its 300 labor hours so as to produce (and consume) 600 units of both wine and cloth, while Portugal, with 600 labor

Production Possibilities	Labor Hours	Productivity per Hour Wine	Cloth
England	300	3	6
Portuga l	600	2	1

Without Trade	Hours X Productivity Wine	Cloth	Production Wine	Cloth	Consumption Wine	Cloth
England	200 X 3	100 X 6 600	600	600	600	
Portugal	200 X 2	400 X 1 400	400	400	400	

After Trade	Hours X Productivity Wine	Cloth	Production Wine	Cloth	Consumption Wine	Cloth
England		300 X 6	1800	700	1100	
Portugal	600 X 2		1200		500	700

TABLE 2.2 Gains from Trade with Comparative Advantage

Production Possibilities	Labor Hours	Productivity per Hour Wine	Cloth
England	300	1	2
Portugal	300	2	1

Without Trade	Hours X Productivity Wine	Cloth	Production Wine	Cloth	Consumption Wine	Cloth
England	200 X 1	100 X 2 200	200	200	200	
Portugal	100 X 2	200 X 1 200	200	200	200	

After Trade	Hours X Productivity Wine	Cloth	Production Wine	Cloth	Consumption Wine	Cloth
England		300 X 2	600	300	300	

TABLE 2.1 Gains from Trade with Absolute Advantage

hours in this case, would produce 400 units of each. With the prospect of trade in mind, however, England completely specializes in cloth—the product in which it holds a comparative (as well as an absolute) advantage—producing 1800 units. Portugal shifts all 600 of its labor hours to the production of wine—the product in which it holds a comparative (but not an absolute) advantage. Not only does this represent a considerable increase above the total production without trade, it also permits the two nations to exchange 700 units of wine for 700 units of cloth. When they do so, each nation consumes more of both products after specialization and trade than when self-sufficient in both. Thus, we can see that trade can be profitable even if one country possesses an absolute advantage in both goods. (That does not mean that both nations profit equally, but assessing the relative gains requires far more sophisticated analytic tools than this example provides.)

This simple statement of the gains-from-trade argument remains the most vivid demonstration of Ricardo's theory of comparative advantage. And it is the theory of comparative advantage, itself merely a subset of the more general theory of economic liberalism, that gives such intellectual force to the drive for free trade. It is cited as frequently in the trade controversies of the late twentieth century as it was in the Corn Law debates more than a century and a half ago.

But the liberal argument for free trade is far from timeless: It depended for its force on particular historical developments of the modern age. For example, efficient allocation of resources among different economic sectors is not an idea that could arise in a relatively stagnant medieval economy with only one dominant sector. Similarly, it would have been imprudent to rely upon trade when transportation systems were technologically backward and politically fragile. But Ricardian theory is especially modern in its acceptance of a vision quite at odds with mercantilist ideas: that maximum aggregate consumption is the proper central goal of national policy. Liberals assume that national prosperity is the dominant element of the national interest and that it consists of the aggregated welfare of all the individuals that make up the nation. Welfare, in turn, is identical with consumption. Liberalism thus embraces a secular, materialist, individualistic conception of national welfare quite distinct from earlier emphases on a stable, organic, and collective social whole. It is implicitly far more attentive to the welfare of the masses than notions of national prosperity which emphasize the status of landowners or the power of the state. If it is not yet explicitly egalitarian or democratic, it uses a language that can more easily accommodate these more progressive ideas.

In another sense, too, liberalism was born to a moment: Although liberal theory had undeniable analytical merit, it was the changing balance of political power that was decisive in bringing about the demise of the Corn Laws.

THE POLITICAL CONFLICT OVER THE CORN LAWS

Indeed, Ricardo's brilliant theoretical ideas were translated into the free trade policies of the 1840s by somewhat surprising political forces. The trade policy preferences of various groups reflected their perceptions of the dilemmas of trade, but the resulting political alignments did not follow precisely the expectations one might derive from Ricardian theory. In particular, although liberal theory identifies the major beneficiaries of free trade as consumers, whose welfare improves when declining trade barriers allow the competition from imports to push prices down, the fight for free trade in grain was actually led by industrialists.

One reason, of course, is that industrialists were permitted to vote and the working class was not. Another was the special skill of the Anti–Corn Law League, which was headed by Richard Cobden and John Bright and centered among the manufacturing interests of Manchester. Through its influence on parliamentary leaders such as William Huskisson, William Pitt the Younger, and Sir John Peel, the Anti–Corn Law League was the principal architect of the drive for repeal from the end of the 1830s to eventual success in 1846. These industrial interests were motivated by both philosophical and practical considerations.

Philosophically, laissez-faire arrangements would give a great deal of freedom to capitalists who were becoming increasingly restive with the government regulations that constrained their entrepreneurial behavior. Unlike mercantilism, which placed the state at the center of economic development, Smith's "invisible hand of self-interest" analogy made it clear that a sound economy must be propelled by the creative activities of the capitalist entrepreneur. In liberal theory, it is the private individual—not the government—who discovers comparative advantage, invests in the export sector, and engages in trade. Government's only role is to stay out of the way. Such a doctrine would obviously have enormous appeal to an entrepreneur who not only welcomed the freedom from government control but no doubt appreciated that his profit-maximizing behavior—once castigated as the sin of avarice—could be portrayed as the act of a patriot.

Though liberal theory certainly held its intellectual attractions for industrialists, the repeal movement was largely motivated by practical opposition to the Corn Laws themselves. Hostility stemmed from the conviction that whatever their original rationale, these laws had long since degenerated into simple import barriers designed to protect landowners. This was correct: The provocative Corn Law of 1815 was openly designed to benefit the landed interests in utter disregard for its impact upon consumers. Unlike earlier versions dating back centuries, the 1815 law suspended all the restrictions on exports, which were designed to keep prices down, but imposed high tariffs on imports, which served to restrict grain supplies and drive prices up by keeping foreign grain out.

Capitalists feared that if grain-producing nations in Europe and America could not sell their products in England because of the Corn Laws, they would have no money to purchase English industrial products. They speculated that the repeal of the Corn Laws would stimulate demand abroad and that English manufacturers would benefit by capturing at least a portion of that expanding market. Following that logic, they also argued that nations unable to acquire British manufactures would launch industry of their own. Moreover, since British trade barriers would encourage them to erect retaliatory tariffs to protect these fledgling industries, such industries could eventually become global competitors. Repeal of the Corn Laws could avoid this scenario by encouraging other European nations to remain specialists in grain production in order to serve the English market.[27]

But it was the effect of food prices on the production costs of British industry that lay at the heart of both the theoretical debate and the political controversy. Capitalists argued that repeal of the Corn Laws would lower food prices because grain could be imported from Europe more cheaply than it could be grown at home. In turn, that meant that wages in British industry could be lowered—without diminishing the standard of living of workers. Finally, this would permit British manufacturers to be competitive with foreign firms because the wage savings could be passed on to consumers. At the same time, of course, lower food prices meant that consumers would have more money to spend on the manufactured goods being produced by British industry. Capitalists thus expected to sell more products at home as well as abroad after the repeal of the Corn Laws.

The most obvious opposition to the Anti–Corn Law League, the landed gentry who benefitted directly from agricultural protection, were unmoved by the liberal arguments. Whatever the gains from trade might be, they certainly would not accrue to landowners, who would unequivocally lose in a free competition with cheaper grain producers in North America and Europe. Thus, the chief political battleground concerned two groups of workers with seemingly different interests: urban workers apparently tied to the health of the manufacturing sector and the peasantry, presumably tied to the sectoral interests of agriculture.

It is the latter group whose concerns were addressed most directly by Ricardian arguments, because the unique contribution of liberal theory lay in its response to the protectionists' contention that free trade would injure workers in this previously protected sector of the economy. The liberal position, illustrated by the Ricardian example of wine and cloth, offered a rebuttal to concern for the fate of agricultural laborers if repeal of the Corn Laws brought about the expected demise of grain production in England. Although Ricardo granted that employment in the production of wine might indeed decline or even disappear altogether in Britain, he maintained that there was really nothing to fear, even for workers in the wine industry because the decline in wine production would be accompanied by a compensating expansion of cloth production so that total employment would remain the same.

Following Ricardo, liberals argued that the repeal of the Corn Laws would not decrease employment but only shift it from the inefficient agricultural sector to the manufacturing sector, in which England had a comparative advantage. Liberal theory insists that it is far better to tolerate these short-term dislocations—these transition costs—than to protect an inefficient industry, because total national consumption will increase with a more efficient allocation of resources.[28] The liberal argument for the North American Free Trade Agreement was identical: American workers losing their jobs to Mexican imports were expected to find employment in industries that export to Mexico.

How is this key argument received? Those likely to immediately gain from free trade—the British cloth industry in the Ricardian example and the manufacturing sector in the case of the Corn Laws—can be expected to grant the logic of the free trade argument. After all, those in the most competitive sector have much to gain *personally* and nothing to lose, even if the liberal contention about *national* welfare should turn out to be wrong. They will typically urge those who will immediately lose—agricultural workers or wine producers—to patiently wait for growing employment opportunities in the most competitive sector to trickle down to them.

But those who will immediately suffer the dislocation are more concerned with the distributional effects of free trade than with its aggregate effects. They are likely to be more skeptical of liberal theory simply because for them the stakes are so much greater. And they will be as attentive to the short term as to the long term, worrying about how long and painful the transition may be even if the future is fully as bright as liberal theory promises. After all, it is far easier for a theorist to move a column of figures from "wine" to "cloth" than it is for a worker who has devoted his life to farming to pack up and move to a strange town in the hopes that he might find a job in an unfamiliar industry that requires skills he does not possess. He would not be persuaded by the liberal theorist's contention that his loss of income was temporary or that his loss of security and way of life was illusory because it could not be measured in terms of the aggregate consumption that defines "gains from trade." Skepticism that the dislocations to individuals are warranted by aggregate gains are given credence by modern analysis. Dani Rodrik notes that "in the standard models used by international economists, the distributional consequences of trade typically dwarf its net contribution to national income. Under typical parameters, lowering of a trade restriction will result in $5 or more of income being shuffled among different groups for every $1 of net gain."[29].

In the case of the Corn Laws, the natural opposition of agricultural workers to a removal of protection for their sector seems to have been overcome by three factors. First, they were cross-pressured by their dual roles as both workers and consumers; in the latter capacity they appeared to benefit from lower grain prices. Second, they were not convinced that the benefits of agricultural protection had been passed down from landowners to agricultural workers. The Anti–Corn Law League was especially effective in persuading much of the peasantry that higher grain prices enriched only landowners because it enabled them to increase the land rents paid by peasants. Third, they were reasonably optimistic that job opportunities existed in the industrial sector for workers displaced from agriculture. Because British industry was by far the most productive in the world during this period, and its output was increasing rapidly, industrial employment opportunities were growing. It was possible for peasants to envision a relatively brief transition with a relatively small risk. Confidence in the future of the dominant economy and the dominant industries in the world made the Ricardian arguments seem plausible.

The industrial working class was ambivalent. On the one hand, it had little use for the landowners and the fall in food prices expected from free trade would be very welcome. However, it trusted neither of the two principal protagonists in the debate; the motivations of the Anti–Corn Law League in seeking lower food prices attracted particular suspicion. Supporters of the Corn Laws cited the "iron law of wages"—the contention that desperate unemployed workers always compete for scarce jobs by offering to work for lower wages until eventually wage rates fall to the subsistence level (that is, just high enough to keep them alive). Thus, any decline in food prices brought about by repeal of the Corn Laws would lower the wages necessary to provide subsistence, but that would not benefit workers because wage rates would be driven quickly to that new, lower level.

A placard posted in Manchester conveyed the essence of a position that would be at home in the debate over NAFTA: "Why do these liberal manufacturers bawl so lustily for the repeal of the corn laws?—because with the reduced price of corn they will be enabled to reduce the wages of working men so that they may compete with foreigners who live upon potatoes."[30] Because industrialists did portray lower prices as necessary to meet the competition of producers abroad, the motivation implied by the placard seems well founded. Certainly the sentiment it expresses has been widely shared by workers in more advanced countries: fear that their living standards will suffer when forced to compete with foreign workers whose wages seem to them indecently low. Indeed, after the repeal of the Corn Laws, identical reasoning underlay the rallying cry of protectionist forces in the United States: "Protection against the pauper labor of Europe."[31] Many even doubted that lower wages would be passed along in the form of lower, more internationally competitive prices for final goods; instead, they believed that lower wages would mean only greater profits for capitalists.

The capitalist leaders who led the drive for free trade were not viewed as friends of the working classes because of their strident opposition to acts such as a child-labor law, poor laws to provide relief to the unemployed, regulations to limit the workday, and the legalization of collective bargaining for wages. Particularly during the 1840s when the Anti–Corn Law League directly confronted the Chartists, a working-class organization that favored full manhood suffrage, worker antipathies to capitalists were somewhat greater than toward landowners. However, it appears that mass opinion marginally favored repeal of the Corn Laws by 1846.

It is by no means clear that the position of the working class was decisive, though it unquestionably had some impact even in the absence of democratic representation. Nor had the capitalist class displaced the gentry in parliamentary membership.[32] However, even landed members of Parliament (MPs) had to respond to constituents whose interests were increasingly concentrated in industry and commerce, not agriculture. Agriculture lost its political clout because with the expansion of the manufacturing sector and the growth of towns, it ceased to be the driving force of the economy and the principal source of government revenue.

Still, the final repeal of the Corn Laws owes much to the power of the arguments themselves. In particular, opponents of the Corn Laws were able to counter two claims of fairness raised by protectionists in all debates over free trade, including those of the present era. The first questions the value of free trade policy in one nation when other nations do not reciprocate. The second challenges the validity of eliminating protection for some while retaining it for others.

Protectionists used the reciprocity argument to question the real benefits of *unilateral* free trade. Liberals assumed that repeal of the Corn Laws would bring an increase in both imports of grain and exports of manufactured goods, but Sir Henry Parnell's speech in the House of Commons in support of the 1815 bill noted that neither linkage would occur unless Britain's trade partners would reciprocate by emulating the free trade stance. Parnell thus argued for free trade only on the "supposition that all the nations of Europe should adopt the same common policy."[33]

This reciprocity objection is a common feature of all debates over free trade, but liberal economists are unanimous in finding it to be totally without merit because protection always hurts consumers by increasing the prices of imports. Thus, although Smith acknowledges that "revenge naturally dictates retaliation," he finds the policy unwise: "It seems a bad method of compensating the injury done to certain classes of our people to do another injury ourselves, not only to those classes, but to almost all the other classes."[34]

The sole exception to the principle that retaliation is self-defeating is the allowance that temporary measures designed to induce others to eliminate the objectionable barriers may be justified. On how far in this direction it may be safe to go, sage judgment cannot be found in the analytical ability of the economist, says Smith, but in "the skill of that insidious and crafty animal, vulgarly called a statesman or politician."[35]

The second fairness contention challenges the validity of eliminating protection for some sectors while retaining it for others. Observing that the very manufacturing interests that led the opposition to agricultural protection were very heavily protected by tariffs themselves, Parnell challenged them directly: "If all those who are concerned in manufactures and commerce will consent to adopt the system of a perfect free trade, those who are now advocates for restraints on the importation of corn will willingly abandon on their part all claim to any such protection."[36] This point had a powerful internal logic and a compelling appeal to fairness. In 1815, it carried the day: Because manufacturing interests were unwilling to give up the protection afforded by tariffs on industrial imports, agricultural interests refused to abandon agricultural tariffs.

The first step in breaking this deadlock was taken in the Petition of the Merchants of London, drafted by Thomas Tooke and presented to the House of Commons in 1820 by Alexander Baring. It called for an end to all protectionist measures (allowing, however, for customs duties necessary for government revenue), citing precisely the inevitability of the line of reasoning used by Parnell. Indeed, it went farther, noting that if British producers could be protected from foreign ones, the same argument could be made for each county and that free trade even within Britain would cease. Further, it observed that British protectionist measures were used as an example by other nations; until Britain embraced free trade, neither would others. Thus, Tooke's analysis engaged both of Parnell's objections and paved the way for the gradual dismantling of the protectionist structure of British commercial policy that occurred over the following three decades.

Explanations for Early Trade Policies

Early Mercantilism	Nineteenth-Century Liberalism
1. State of Theory	
Religious and communitarian ethical theory assumed that to achieve the public interest in just prices required state interference in markets.	Materialist, individualist, and utilitarian ethical theory; economic theory emphasizes that comparative advantage enables free trade to increase the consumption of all nations.
2. State of markets	
Thin markets made prices volatile; unstable political relations made trade uncertain; and English producers feared foreign competition.	Lower transportation costs and reduced political risks make potential gains from trade large; technological improvements made English industry dominant over foreign competition.
3. Political power balances	
Parliament was dominated by the Crown, the church, and especially landowners.	Parliament increasingly influenced by industrial and urban interests.

CONCLUSION: THE TRIUMPH OF FREE TRADE

Modest movement toward free trade in industry was launched by the commercial treaty with France of 1786—which eliminated many prohibitions and prohibitory duties—but it accelerated dramatically after 1820. In 1824, the export of native wool was permitted after centuries of prohibition designed to protect the domestic textile industries. In 1825, the duty on foreign cloth was reduced from 50 percent to 15 percent. In 1842, all complete prohibitions were removed and duties on raw materials were reduced to 5 percent, on partially manufactured articles to 12 percent, and on fully manufactured goods to 20 percent. In 1846, the latter was lowered to 10 percent and the textile industries (except silk) ceased to be protected at all. During the same period, the Navigation Acts, which protected British shipping, were weakened in 1815, 1822, and 1825 before being finally eliminated in 1849. Agricultural protection in Britain ended in 1846 with the repeal of the Corn Laws.

Chapter Two Endnotes

1. The phrase actually originates in physiocracy, an eighteenth-century economic theory propounded by François Quesnay, an adviser to Louis XV of France. Although they advanced a very different conception of the economy than liberals—emphasizing agriculture to the near exclusion of industry—physiocrats were, like liberals, free traders. When asked how best the state might foster the creation of wealth in the economy, Vincent de Gournay, an associate of Quesnay, responded, “laissez faire, laissez passer,” literally, “allow it to be made, allow it to be traded.”
2. The term “corn” is synonymous with “grain” and includes wheat, oats, rye, barley, malt, peas, and beans, as well as maize (which Americans call corn).
3. There are also major differences among these strategies. Latin America de-emphasized eventual export success, whereas Japan encouraged cartels among multiple firms instead of granting monopolies.
4. See E. Lipson, *The Growth of English Society: A Short Economic History* (New York: Henry Holt, 1950), p. 54.
5. Import taxes account for about 1.5 percent of U.S. federal government revenues, about average among developed countries. Among less developed countries it is typically much higher.
6. See W. Cunningham, *The Growth of English Industry and Commerce in Modern Times, Volume 2: The Mercantile System* (Cambridge: Cambridge University Press, 1938), p. 503.
7. See N.S.B. Gras, *The Evolution of the English Corn Market* (Cambridge: Harvard University Press, 1915).
8. See Donald Grove Barnes, *A History of the English Corn Laws from 1660–1846* (London: George Routledge, 1930), pp. 5–6.
9. Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* (London: J. M. Dutton, 1910), p. 408.
10. J. Russell Major, *The Western World: Renaissance to the Present* (Philadelphia: J. B. Lippincott, 1966), p. 235.
11. Quoted in Cunningham, *The Growth of English Industry*, p. 387.
12. Similar arrangements were common in Europe at various times. In Russia, for example, they survived virtually intact until the agricultural reforms of 1904.
13. It is tempting to glorify such an ethical stance, but it must be remembered that what was regarded as “suitable for his station” reflected contemporary standards that tolerated massive inequalities in economic standards of living and vast differences in political rights between those of one station and another.
14. See Barnes, *A History of the English Corn Laws from 1660–1846*, p. 34.
15. R. H. Tawney, *Religion and the Rise of Capitalism* (New York: New American Library, 1954), p. 43.
16. See Lipson, *The Growth of English Society*, p. 145.
17. Of course, government was not the only source of interference with markets. As early as the thirteenth century, skilled artisans formed craft **guilds** that developed standards of workmanship to protect the public from shoddy goods, but an elaborate system of apprenticeships also protected established artisans from the competition of newcomers and outsiders. Only members of a craft guild—masters and journeymen—were permitted to be employed in the industry or to sell their goods. Membership in the guild could be attained only after a lengthy period of apprenticeship with a master who would train the newcomer. Modern economists would call these arrangements **oligopolies**, meaning markets dominated by a small number of suppliers who may collude to keep prices high.
18.In the middle of the eighteenth century, a coach took fourteen days to make the trip from

Edinburgh in Scotland to London in the south of England, a journey now accomplished in six hours by train and under two hours by plane.

19.By the middle of the nineteenth century about a quarter of the land was owned by 1,200 individuals with about 6,200 owning another quarter. Only about an eighth of the land was worked directly by its owners; the remainder was farmed by rent-paying tenants.

20. R. H. Tawney, *The Agrarian Problem in the Sixteenth Century* (London: Longmans, Green, 1912), p. 409.

21.While the church now plays a more passive role in most countries, the modern state, especially in its democratic form, has filled the role of a check on the distributional and value allocation propensities of markets. The capitalist market and the democratic state, two institutions that represent distinctive ethical theories, battle for primacy in directing the organization of modern society. Both are necessary, but nations vary in the extent to which each is dominant. See Karl Polanyi, *The Great Transformation*, (Boston: Beacon Press, 1944).

22. Lipson, *The Growth of English Society*, p. 48.

23. Ibid., p. 182.

24. Smith, *Wealth of Nations*, p. 401.

25. Ibid., p. 400.

26. Ironically, the trade in Portuguese wine resulted more from political restrictions than market forces. French wine was preferred by English consumers, but for foreign policy motivations differential English tariffs were negotiated under the Methuen Treaty of 1703 to encourage the importation of port wine from Portugal. See Lipson, *The Growth of English Society*, p. 155.

27. Though effective early in the Corn Law debates, this argument had less power by the 1840s because by this time an industrial sector had already emerged in most of Europe.

28. Even if employment declines somewhat, later liberals have shown that protectionism is less efficient than combining free trade with unemployment compensation. Indeed, this is the approach widely used in Europe today. In this period, however, the state did not maintain such a social safety net.

29. Dani Rodrik, *Has Globalization Gone Too Far?* (Washington, DC: Institute for International Economics, 1997)

30. Quoted in Lipson, *The Growth of English Society*, p. 315.

31. Ibid., p. 320.

32. Even after the Reform Bill of 1832, about 80 percent of the members of Parliament were landowners. See W. O. Aydelotte, "The Country Gentlemen and the Repeal of the Corn Laws," *English Historical Review* 82, 322 (1967):51. However, the landed gentry were becoming less reliant on the agricultural sector because they were rapidly investing in industry and transportation. See Cheryl Schonhardt-Bailey, "Specific Factors, Capital Markets, Portfolio Diversification, and Free Trade: Domestic Determinants of the Repeal of the Corn Laws," *World Politics* 43 (July 1991):545–569.

33. Quoted in Barnes, *A History of the English Corn Laws*, p. 119.

34. Smith, *Wealth of Nations*, pp. 411–412.

35. Ibid.

36.Quoted in Barnes, *A History of the English Corn Laws*, p. 119.