

HOW DID DEVELOPED COUNTRIES INDUSTRIALIZE?
The History of Trade and Industrial Policy:
The Cases of Great Britain and the USA

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HOW DID DEVELOPED COUNTRIES INDUSTRIALIZE?

The History of Trade and Industrial Policy: The Cases of Great Britain and the USA

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To examine the case of early industrializers, we concentrate in this paper on the history of trade policy in Great Britain and the United States as two examples, and also refer to the cases of Germany and France. Our analysis in this paper indicates that it is a fallacy that early industrializers could have developed their industrial sector without infant industry protection. Indeed in all cases, to develop their industries, they went through an infant industry protection phase and heavy government intervention in the foreign sector. Nevertheless, the degree of protection and government intervention varied from one country to another. The United States was the motherland of infant industry protection not only at the intellectual level but also in actual fact. Despite the fact that the Industrial Revolution contributed to the rapid industrialization of Great Britain, its industrial sector benefited from trade protection and other forms of government intervention in the trade flow through the Navigation Act and by means of political power and even military power.

Moreover, government intervention in both cases was not confined, although it was more significant, to foreign trade. The governments concerned intervened in the domestic economy – particularly in the United States – directly and indirectly, to assist capital accumulation, institutional development and infrastructural build-up and to provide training, research and development (R&D), etc. In neither case can trade policy alone explain industrial and export success. In both countries, capital accumulation, infrastructure and institutional development played a significant role. In both cases, as well as France and Germany, agricultural development, often helped by protection and other forms of government intervention, was accompanied and facilitated by the process of industrial development. Moreover, while high domestic savings was crucial in financing their capital accumulation, in both countries foreign investment played a noticeable role at the early stages of their industrial development. Yet, in all countries, even when the industrial sector was mature, protection was used as a means of bargaining power in bilateral trade negotiation and trade treaties.

INTRODUCTION

"Political economy, in matters of international commerce, must draw its lessons from experience."

F. List (1856), 631

There has recently been a lot of discussion in the literature on late industrializing countries, particularly East Asian ones, as there were some common features that the late and early industrializers did not share. There is no general theory of trade and industrial policy. Each country has specific conditions and requires specific policies at any particular period. Nevertheless, one could draw some common lessons at the general level from the experience of early as well as late industrializers through induction. We shall show in this and a separate paper how history will tell us that:

- C With the exception of Hong Kong, no country has developed its industrial base without prior infant industry protection; and there are some similarities as well as differences between early and late industrializers in terms of factors contributing to successful industrialization.
- C In the process of industrialization and export expansion, functional and selective government intervention in trade has been an important factor. Moreover, government intervention for capital accumulation, infrastructural and institutional development, as well as growth of food supply, has also played a significant role in the industrialization of both groups.

Since there is often confusion about the history of industrialization of such early industrializers as Great Britain, the case of this country in particular as a forerunner of industrialization will be reviewed in support of these points, particularly the first one made above as far as earlier industrializers are concerned. Subsequently we shall consider the United States and make a brief reference to Germany and France. It will be seen that, in the process of catching up, the late industrializers have shown many common features with the early ones.

I. EARLY INDUSTRIALIZERS: THE CASE OF GREAT BRITAIN

Many writers attribute the industrial development of Great Britain basically to technical changes during the Industrial Revolution (1760-1830). Alfred Marshall's motto on trade and industrialization was "the many in the one, the one in the many" ("many tendencies have gone to the making of each industry and each economic situation" and "almost every important tendency is so far modified by the conditions under which it operates") (Marshall, 1920). Nevertheless, he refers in passing to the role of trade policy, misinterpreting List's concept of "nationality". To Marshall, the "spirit of economic nationality in England is a sort of cultural issue related to patriotism" and a "pride in their [Englishmen] work, as in their military" (*ibid.*, p. 32). Hence, the roots of success of industrialization in the 19th century are "some fundamental character of Englishmen". Moreover, while attributing the success in "massive industries" to the "age of steam", he argued that around the 1860s "Later on she [England] obtained further advantage through her policy of free trade and opening of her market to the world" (*op. cit.*, pp. 10 and 89).

Marshall's interpretation of trade liberalization gives the impression that he believed that the earlier policies of trade restriction were a disadvantage and detrimental to the industrial development of Great Britain.¹ This is a view shared by Adam Smith and other liberal and neoliberal economists advocated

¹ It should be mentioned that although elsewhere Marshall (1923, p. 218) referred to some advantages of infant industry protection in an "undeveloped country", on the whole he rejected the argument.

earlier in 1776 (Smith, 1776), who argue that Great Britain achieved its industrialization despite its protectionist policies. It is true that inventions and innovations during the Industrial Revolution were main contributing factors to the process of acceleration of the industrial development of Great Britain (Craft, 1995). Nevertheless, List (1856) correctly argues that the process of industrialization had its roots in early times, i.e. a few centuries before, initiated by Elizabeth I (1553-1603) with trade restrictions, and later on continued by James I (1603-1625) and Charles I (1625-1649). In fact, before the Industrial Revolution substantial industrial activities existed in Great Britain. According to an estimate, in 1700 this sector accounted for 18.5 per cent of the male workforce and 20 per cent of total income of the country (Craft, 1995, table 3.1). Tariffs which were initially low were sharply increased in the 1690s, although mainly for revenue purposes (Davis, 1966). Initially Great Britain adopted protectionist policies which facilitated processing of woollen cloths. While earlier on wool had constituted the main export item of the country, protection resulted in manufacturing and later on in export of woollen cloth (List, 1856, ch. IV). The process of protection continued well into the Industrial Revolution and beyond until around the 1860s. This was in spite the theoretical argument surrounding the controversy over free trade and protection initiated by Adam Smith in 1776, when he published his book "*An Inquiry into the Nature and Causes of the Wealth of Nations*". As of 1820, Great Britain showed the highest rate of tariffs on imports of manufactured goods (50 per cent) in Europe (see table 2). Moreover, English agriculture was heavily protected and her navigation enjoyed mild protection (Bairoch, 1993, p. 19).

A. Some common features with late industrializers: trade policy

The process of infant industry protection and industrialization of Great Britain, as a leading industrial country, has certain features in common with late industrializers that are worth emphasizing. As far as trade policy is concerned, three points are relevant. First, infant industry protection was selective. The process which started with protection of woollen products, cotton products and iron, was extended later on to other metals, wrought leather, ship-building and fisheries, and subsequently to flax, and silk. Local production was usually protected *vis-à-vis* imports. For example, imports of silk and cotton were prohibited from India which had advantages over Great Britain in terms of raw materials and working experience. The protection included not only quantitative restrictions but also penalties on consumption. When ship-building was developed, Great Britain secured for her own vessels sea transport and fisheries through the Act of Navigation (effective in 1651), which was an instrument of protection. Subsequently, the industries mentioned above became "the centre of the industrial, commercial and maritime power of England" (*op. cit.*, p. 112).

The selection of cotton products and iron in particular made Great Britain the "workshop of the world" (Deane, 1965, p. 87). In 1780, "the cotton industry was backward, small and unable to compete with Indian calicoes or muslins in either quantity or price unless protected" (*ibid*, p. 88). The choice of the cotton industry for protection was not only due to the availability of new machinery introduced owing to technological change but also to the availability of cheap labour (women and children) in general and skilled labour in particular, as well as its potential to act as a leading industry in production and export. By 1815, cotton textiles accounted for 40 per cent of Great Britain's total exports; the ratio reached 50 per cent in 1830 (*ibid*, p. 94). As the first country to reap the benefits of technological change, Great Britain enjoyed the innovator's profit.

The cotton textile industry did not initially provide many linkages with the rest of the economy. Cotton was imported and textile machinery developed in the second quarter of the 19th century. Nevertheless, it acted as a leading sector in the sense of pioneering industrialization. Further, innovations which contributed to productivity enhancement in the cotton textile industry spread from this industry to others. By contrast, the iron industry, chosen for industrial expansion in the last quarter of the 18th century, provided strong forward and backward linkages. Raw iron was produced at home and iron was the input to steel production, steam engines, etc. (Deane, 1965, ch. 7). In fact, the steam engine was first used in the iron industry itself as well as in the cotton textile industry.

Secondly, only after the Industrial Revolution was well established and when Great Britain had consolidated its industrial base did it start to follow around 1850 a free trade policy after some gradual tariff reduction. In 1786 Great Britain reduced – but only with France – some of its tariffs on trade on a limited basis through the Eden Treaty, but the war with France, which began in 1793 and continued until the early 19th century, led to the reversal of the situation (Deane, 1965, p. 203). The war ended in 1815. In the 1820s, trade expanded and manufacturers recovered some confidence. Hence, Huskisson reduced some tariffs moderately in 1824-1825. Nevertheless, in 1826 Great Britain was still more protectionist than she had been before the war of 1793. Import duties were about 53 per cent in the late 1820s, as compared with 57 per cent in the early 1820s and less than 30 per cent at the end of the 18th century (*ibid*, p. 204). Some trade policy reform and "liberalization" began in 1833, but it was during the 1840s that import duties on a large number of items were reduced (1842 and 1845), the Corn abolished (1846) and the Navigation Act repealed (1849) (Kenwood and Lougheed, 1994, ch. 4). Further tariff reduction took place in the 1850s, and the 1860s was the beginning of completely free trade. At this time, Great Britain was in an advantageous position *vis-à-vis* other countries not only because of the development of its industrial base but also because of the destruction of the industrial basis of its competitors in Europe (Marshall, 1920, pp. 90-91). In fact, one could argue that the protection of infant industries in Great Britain lasted too long. At any rate, in the mid-19th century its industries were mature enough to compete in the internal as well as international markets. Trade liberalization intensified the pattern of specialization

in production and export of manufactured goods, for which the country had attained a comparative advantage. Moreover, it led to the growth of imports of agricultural goods. In fact, while agricultural production doubled between 1800 and 1860, it stagnated during the period 1860-1913 (O'Grada, 1995, p. 145). Generally speaking, it was in the interest of Great Britain at the time to open up its doors to raw materials and agricultural products imported from abroad and to intensify specialization in production of manufactured goods. The manufacturing sector enjoyed increasing return to scale, while agriculture was characterized by diminishing return (Furtado, 1970, p. 28). The intensification of trade liberalization after the 1850s took place at a time when transport costs were declining considerably as a result of the technological change which allowed an increase in the size of vessels.

From a static comparative advantage point of view it was also in the interest of countries exporting raw material to follow the free trade policy of Great Britain and to export raw materials to Great Britain in exchange for manufactured goods. Great Britain's advocacy of universal free trade was on the basis of the perception that it would provide the country with export markets and access to raw materials, as discussed in the last section of this chapter. The free trade policy of Great Britain was followed both in the continent and elsewhere for over at least two decades. On the continent, the industrial base of European countries was damaged by the war, so they needed foreign sources of supply. Moreover, they were in search of cheap raw materials. The commercial treaty signed with France (1860) allowed Great Britain access to other markets through a most favoured nation (MFN) clause, because France had signed treaties with other countries (Marshall, 1920, pp. 89-91). In short, Great Britain began its trade liberalization after over two centuries of protection, and even then liberalization only took place gradually over a period of almost 30 years. Moreover, to exploit foreign markets, Great Britain also advocated free trade, or enforced it, in other countries and in its colonies. The process of trade liberalization elsewhere helped her to increase exports and the output of her industrial sector. It should be added that Great Britain began to reverse its trade policies in 1881, when the "Fair Trade League" was introduced. In the early 20th century, proposals were made under the "Tariff Reform League" to protect some industries

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