

# What Economic Path for China?

by William Jones

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**The Myth of Free Trade: An Inquiry into British and American Industrialization**

by Mei Junjie

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Dec. 20—Dr. Mei Junjie, the author of *The Myth of Free Trade*, is a senior fellow of international political economy at the Shanghai Academy of Social Sciences (SASS), and since 2000 has served as director of the SASS Center for World Economic History. He is also the founding executive director of the SASS Institute of China Studies. He received his Ph.D. in international economics from SASS, an M.S. in the politics of the world economy from the London School of Economics, and an M.A. in world modernization studies from Peking University.

Mei was a Chevening Scholar of the British Foreign and Commonwealth Office and a visiting researcher at Stanford University. He has taught international trade policy at Shanghai Maritime University, conducted policy analysis at the Pudong Institute of Development Studies, and taught language students at Nanjing University.

Dr. Mei has published extensively on issues of international political economy, his best-known work being the one abstracted here, *The Myth of Free Trade: an Inquiry into British and American Industrialization* (Xinhua Publishing House, 2014; Shanghai Sanlian Press, 2008). He is co-editor-in-chief of the book series



*Author Mei Junjie, senior fellow of international political economy at the Shanghai Academy of Social Sciences*

on “World Economic History” published by the prestigious Commercial Press in China, and is also the editor-in-chief of the book series on “Global Economic Strategists” issued by the Shanghai Far East Publishing House.

Mei has translated numerous works into Chinese such as *Industry and Empire* (Eric Hobsbawm, 1999), *Against the Tide: An Intellectual History of Free Trade* (Douglas Irwin, 1996), *Count Sergei Witte and the Twilight of Imperial Russia* (Sidney Harcave, 2004), and *Jean-Baptiste Colbert* (Ines Murat, 1980). He is now engaged in a project to translate some of the works by and about Friedrich List, the German-American economist who had some influence on Chinese economic policy in the last century, as he did in many other countries.

## **China Seeks Its Own Path to Development**

China currently finds itself in a stage of dramatic transformation. The world has been astonished by the rapid economic development of China over the last 30 years, since the initiation by Deng Xiaoping’s “reform and opening up” policy. China re-entered the world economy, so to speak, as a cheap-labor producer for the world market, but has in the process transformed itself into something much more important. Meanwhile the financial collapse of the world economy has destroyed the export market for which China produced. China thus finds itself in a situation where it must carve out a new path, or as they call it “a new normal.” This has occasioned a major debate in China over the economic policy it must adopt.

While tremendous pressure has been placed on China by forces in the West to simply open its markets to “free trade,” as implemented with such devastating results by Russia in the 1990s, Chinese policy makers have been very reluctant to travel that route. Nevertheless, there is a significant faction of Chinese economists who are pushing in that direction, foolishly believing that eliminating all government “interference” will suddenly unleash a wave of innovation and creativity. The late Milton Friedman, that gadfly of “free trade unlimited,” has his followers in the People’s Republic of China.

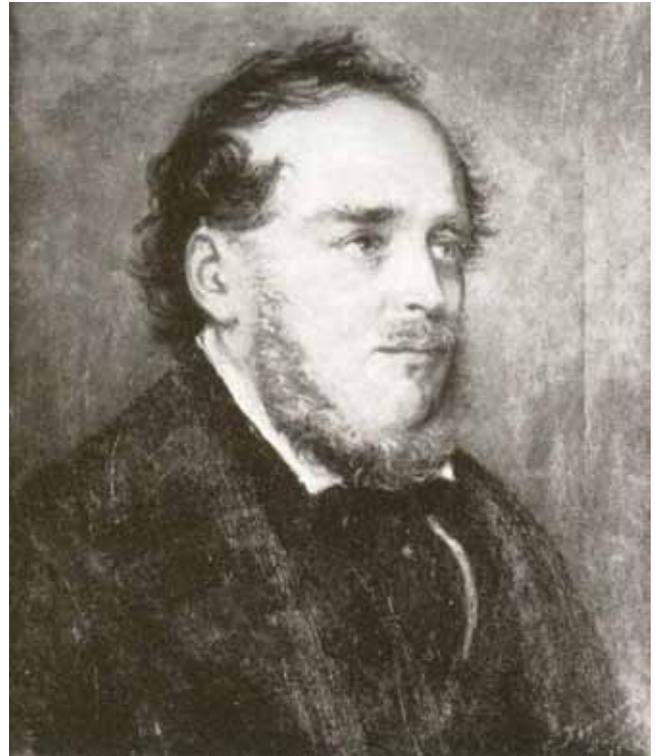
And yet, while there are still those who long for the days of the old “command economy” before “reform and opening up,” it is clear that those days (which can be viewed as “prosperous” only under a very thick film of nostalgia), are definitely not coming back. While the nation will continue to rely on state direction of the economy, there will be a transition away from the traditional state-owned enterprises, which still remain a mainstay of the Chinese economy, toward the creation of a *Mittelstand*, namely, small and medium-sized companies which have always proven to be the mainstay of innovation.

### **New Interest in the ‘American System’**

In seeking a “China path” toward reaching the goal of a moderately well-off society by the middle of this century, there has been renewed interest in the “American System” and its economists, such as Alexander Hamilton and Friedrich List, and its more recent representative, economist and statesman Lyndon LaRouche. A number of economists, such as Professor Mei Junjie, are looking at the work of these exponents of the American System to extract from them lessons for China today.

Other leading economists, such as Professor Ding Yifan, have relied on LaRouche’s notion of “physical economy” to develop his own concept of a “knowledge-based economy,” which is now generally regarded as a key element in China’s new economic strategy. The work of List is particularly relevant now, because of the crucial role his work played in the Bismarck reforms; China looks upon Germany, and its hitherto successful development of a *Mittelstand*, as a model for what it would like to develop.

List’s understanding may well have also played a role in China’s “One Belt, One Road” policy, given



*German-American economist Friedrich List*

that List has been more of a guiding figure for Chinese economists than even Adam Smith. For List, more than anyone, understood the strategic and economic significance of the railroad as a stimulus to economic development.

The development policy now being pursued by the Chinese government would surely bring a smile to the lips of this German economist, who spent most of his life teaching European leaders the importance of the railroad as a transmission belt for science and technology. List also envisioned the development of a continental railroad “landbridge” that would bring together the nations of the Eurasian continent—as has been developed by China. Many of List’s insights in this regard could still be very stimulating for Chinese planners as the Silk Road Economic Belt moves forward.

We look forward to the work that Professor Mei is now pursuing in translating into Chinese some of the works of and about Friedrich List. We are confident that this body of knowledge will help inform Chinese policy makers in formulating their own blueprint for development, as all the other models put forward have already proven themselves to be such dismal failures.



*Free trade in action: British ships bombard Hong Kong harbor during the First Opium War.*

The following abstract of the *The Myth of Free Trade*, kindly provided by Professor Mei, has been edited.

*William Jones may be contacted at [cuth@erols.com](mailto:cuth@erols.com)*

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## **Abstract: The Myth of Free Trade**

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by Mei Junjie

It is generally believed that removing trade barriers will increase the welfare of the trading parties concerned and that trade liberalization, or even free trade, is a sure way for developing countries to reduce poverty and achieve economic prosperity. Indeed, the policy recipe known as the “Washington consensus” has invariably included recommendations to open markets and deregulate. Underlying this economic school of thought is a widely accepted belief that it was Adam Smith, the acknowledged protagonist of liberalism, who laid the foundation of the British industrial revolution and, more broadly, that the modern rise of the western world has been due to free trade and *laissez-faire*. Such a liberal mindset has also found its way into the academic and policy-making circles in China.

However, nothing could be further from the truth. The liberal economic thinking, including its interpretation of history, is erroneous and misleading. This book empirically surveys the history of British and American industrial development over several centuries and reveals the falsity of the liberal claims. Evidence shows that, contrary to the tenets of the free trade doctrine, both Britain and America engaged in long-term and highly protectionist trade practices during their industrialization. It was only after trade protection had afforded them

predominant industrial superiority that they turned to free trade. The main findings of the book are as follows:

The prevailing notion that liberal economic theories and practices enabled Britain to attain its industrial supremacy is not supported by the facts. Free trade did not motivate the British industrial revolution. Instead, it was Britain’s industrial supremacy, nurtured by protectionism, that canonized the free trade doctrine. Adam Smith and his doctrine, while displaying little intellectual originality, came to be revered decades after his death chiefly because the British needed new leverage for pursuing their national interests. By creating such an ideology, free traders hoped to cajole the less-developed countries into an asymmetrical economic relationship with the more developed Britain.

The woolen goods production grew into the staple industry in Britain thanks to the persistent restrictions placed on the free export of British wool and the free import of foreign woolen products. Likewise, the British linen and silk industries were developed through an “artificial” process of import substitution, even though Britain had no comparative advantage whatsoever in these fields. As to the cotton industry that finally cata-

pulted Britain into the industrial revolution, it began and prospered wholly behind the walls of prohibitions and high tariffs in obvious defiance of the principle of comparative advantage.

It is, therefore, reasonable to conclude that the British industrial revolution was actually begotten by trade protectionism, although it has often been argued otherwise by classical and neoclassical liberal theorists.

Although conventionally idealized as the “first industrial nation” to have modernized in an organic way, Britain, in fact, rose from underdeveloped conditions and modernized by inorganic means. Its emergence involved three revolutions. They are:

1. The revolution in economics that provided for mercantilism, a sophisticated policy tool of trade protection, wealth accumulation, industrial promotion, employment creation, state intervention, and overseas expansion all combined;

2. The revolution in proto-industrialization driven by a massive inflow of skilled labor, advanced technology, and equipment from the Continent, reflecting the dynamic interactions within the European multistate system; and

3. The revolution in finance, accelerated by the Dutch contribution, which remarkably enhanced the British state capabilities.

The British policy shift to free trade in the first half of the Nineteenth Century was by no means the result of intellectual enlightenment. As a natural outcome of the industrial supremacy that Britain now enjoyed, the free trade policy was aimed at establishing an international hierarchical order centering on Britain and serving British interests. However, the era of free trade in Europe was short-lived, since a great depression followed on the heels of the free trade movement. One country after another soon resorted to protectionism, which indeed saved them from economic difficulties and narrowed their gap with Britain.

In the meantime, free trade expanded to other parts of the world. But, insofar as it was a sort of compulsory liberalism accompanied by gun-boats, free trade in this context meant little more than colonialist and imperialist exploitation of the weak.

As an offspring of Britain born in the heyday of mercantilism, the United States of America embarked upon a road of protectionism unparalleled in terms of high tariff levels and long-term consistency. Alexan-

der Hamilton should be given adequate credit for formulating the “American System,” characterized by trade protection and state intervention for industrialization. Before the Civil War, and especially after it, American industries (ranging from textiles to petroleum) underwent periods of effective protection, which enabled the country to overtake leading European powers. Only after the United States had gained overwhelming competitive advantage in most key industries did it begin to embrace the free trade doctrine in the first half of the Twentieth Century. The American experience demonstrates once again that protectionism and free trade are but two means, used in succession, to serve the end of enhancing industrial competitiveness.

The United States, since the end of the Second World War, has led the world in taking a road of trade liberalization (freer trade vs. free trade). However, even at the pinnacle of its strength, the United States did not abstain from exploiting restrictive trade legislation and policies designed to promote its security, and its political and economic interests. The relative decline of its industrial dominance in the face of the newly industrializing countries reinforced the American protectionist instinct, resulting in a proliferation of non-tariff trade barriers or even “aggressive unilateralism” under the banner of so-called “fair trade.” Given these and various other double-standard trade practices by the United States, the high-sounding promise of the free trade doctrine remains as elusive as ever.

The glaring discrepancy between the free trade doctrine and the actual Anglo-Saxon practice can be accounted for by flaws in the doctrine itself. Numerous assumptions employed by free trade theorists constitute the grave weakness of the theory, rendering it largely inapplicable to the real world. A historical survey shows that valid cases against free trade have been made on grounds of terms of trade, infant industry, increasing returns, domestic distortion, and imperfect competition.

All of these challenges, in exposing loopholes of the free trade doctrine, point to the same conclusion suggested by the Anglo-Saxon experience—namely, that for any country with potential, the royal road to plenty and power is not free trading based on the principle of comparative advantage, but rather constant industrial upgrading to sustain a country’s international competitive advantage.