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ABSTRACT

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Even if a democracy were more likely to pursue free trade than an autocracy (an unproven generalization), the simultaneous spread of democracy in the world would not necessarily yield a reduction in protection, but might in fact cause an increase. The reason for this paradoxical outcome is the fact that democratic convergence creates power profiles identical across nations. Similar regimes tend to empower the same classes of producers, with the result that if trade is based on relative comparative advantages, and countries specialize on the basis of factor endowments, democratic convergence (or any type of regime convergence for that matter) empowers as many free traders as protectionists, with negative consequences for trade; only if trade is fueled by scale economies, and countries specialize along product lines, then may political convergence not hurt trade. Empirically, I show that this model helps explain the timing of 19th-century European trade liberalization better than existing explanations; it also helps understand the easiness with which liberalization proceeded in the postwar era; and it casts a new light on the difficulties presently encountered, with democracy spreading whereas product specialization is on the retreat.

Democratic Convergence and Free Trade

Suppose three hypothetical worlds: a first one, in which regimes are converging around the democratic ideal; another in which convergence is around autocracy; and a third one in which regimes are becoming less alike. In which world, ceteris paribus, are governments most likely to liberalize their trade policy?

A common answer is the first; the all-out democratic world is the most likely of the three to be open. The rationale goes back to Kant, Bastiat, and the British radicals, who believed that republics (the closest approximation to democracy then) were more likely to engage in trade than absolutist monarchies.[1] The liberal view has been criticized, not so much on the grounds that autocracies are more likely to withstand openness than democracies than on the grounds that regime type does not affect a country's propensity to engage in commercial intercourse.[2] Echoes of the liberal creed can still be heard though, in the form that democracies are less likely than autocracies to resort to protectionist measures when confronted with a challenge.[3]

Weighing the respective propensity of democracies and autocracies to liberalize trade may not be, however, the most appropriate way of tackling the question. Equally important, if not more, is the effect of regime convergence on trade liberalization. Irrespective of whether a particular regime promotes or impedes trade, it empowers a certain class of producers. Similar regimes tend to empower the same classes of producers. For instance, absolutist regimes empowered land at the expense of labor and capital. In contrast, democratic regimes empower the numerous factor. Empowered producers press their policy preferences on their governments. These preferences are determined by the relative competitiveness of these producers in world markets. Thus, if labor is competitive and export-oriented in one country, labor is import-sensitive and protectionist in another. By empowering labor in all countries, convergence toward democracy empowers as many free traders as protectionists. Since it takes two to trade, by empowering protectionists in countries which otherwise would be purchasing foreign goods, regime convergence impedes trade. Trade may be better served by a greater diversity of regimes.

I will show that this line of reasoning illuminates the timing of 19th century trade liberalization. This liberalization did not happen in the wake of the Napoleonic wars under the Concert of Europe, when cooperation among victors was at its highest. Nor did it happen during the revolutionary years (1830-1848), when liberal movements and liberal ideology, of which free trade was an offshoot, crested. Instead the general trend toward openness started in 1850, quickened in the 1860s, and wound up in 1877, spanning an era of low institutionalized cooperation among nations and, with the exception of Britain, Belgium, the Netherlands, and Switzerland, of generalized liberal retrenchment at the domestic level. The reason for this seemingly paradoxical outcome, I will argue, lies in the complementarity afforded by greater regime divergence. Given the protectionist orientation of industrialists on most of the continent, it was the restoration, not the dilution, of land rule in the large continental countries that was key to the surge in cross-Channel trade. Free trade, a liberal economic idea, required a dose of absolutism, a nonliberal political regime.

But if taking into account regime alignments casts new light on 19th-century free trade, it seems at a loss to account for the post-World War II era, when the generalization of democracy among OECD countries co-existed with the deepening of trade. As I will show, this negative result rests upon an initial assumption, which, in fact, turns out to be of bounded application: that trade has negative distributive consequences eliciting protectionist responses. We know from economics that not all types of trade bear negative distributive effects. Inter-industry trade, which is fueled by an asymmetry in factor endowments, does have strong distributive consequences, whereas intra-industry trade, which is fueled by scale economies, does not. Relaxing the distributive assumption suffices to mitigate the negative consequences of regime convergence. As we shall see, postwar trade among OECD countries was mainly of the intra-industry type. Therefore, the postwar democratic convergence among OECD countries did not harm trade, because the presence of scale economies allowed all democracies to engage in intra-industry trade.

Hence the following generalization: absent scale economies, democratic convergence impedes free trade; only in the presence of scale economies may democratic convergence sustain free trade. This proposition is used to revisit the two eras of free trade in modern history: 1860s-1870s and 1945-present. The present approach offers an alternative to ideational accounts[4] and hegemonic stability.[5]

The paper is organized as follows. I first lay out the proposition that regime convergence empowers the same categories of producers. I then contrast the distributive consequences of inter- and intra-industry trade. I revisit the two free trade eras of modern history: 1850s-1870s and 1945-present. In the conclusion, I draw consequences for the recent wave of democratic convergence opened up by the collapse of the Soviet bloc.

Regime Convergence and Empowered Producers

The first order of business is to ground in logic and history the assumption that similar regimes empower similar producer coalitions. Marx argued that liberal regimes empower capitalists, and that only a socialist regime would empower labor.[6] Liberals disagreed with Marx's reduction, contending instead that liberal democracies do not necessarily discriminate on the basis of wealth, whereas communist regimes do discriminate against workers as much as against any other categories of producers. The historical reality is more nuanced than Marx claimed, but not to the point of making regimes neutral, as liberals contend. Similaı regimes at a given point in time do empower similar classes of producers. I will first offer a logic for this claim, and then a categorization of regime types with their respective producer coalitions encountered in the last two centuries.

Regimes differ with respect to the number of people who effectively take part in the policymaking process. For the sake of simplification, assume two generic groups--a group of "insiders," who participate in the policy process, and a group of "outsiders" who don't. In all regimes, individuals belong to one group or the other. In autocracies, the outsiders are the excluded, that is, those who do not belong to the ruling class. In regimes with partial franchise, the outsiders are the formally excluded--the non-enfranchised. In democracies, where everyone is enfranchised, the outsiders are the "self"-excluded--those who abstain from voting out of lack of information or interest. Having thus ranked regimes on an autocracy-democracy continuum, the definition of regime convergence logically follows: regimes converge when they are located around the same point on the continuum defined by the insider-to-outsider ratio.

The identity of who gets included and who does not is not random, but reflects socioeconomic power (wealth and networking capital). Whenever the regime becomes more inclusive, the next group of individuals to be anointed, those who shift from the statute of outsider to that of insider, is always the next most organized group in society. This is true by definition in those cases where the initial motive for inclusion is the capacity of these new classes of individuals to credibly threaten insiders with revolt or revolution should they remain excluded. This is also the case when outsiders are coopted by one subset of insiders in order to help defeat another subset of insiders. For example, the Tory-Whig rivalry in Victorian England led each side to concede the franchise to the other side's enemies--the Whigs to tenants and small farmers, the Tories to artisans and industrial workers. Even there, the next group to be included was always picked among the wealthiest and best organized in its category. The order of inclusion is thus the same in all cases: the next included is always the next best organized among the excluded.

The next best organized social group tends to be identical across societies at any given moment in time. The reasons for this identity in stratification are systemic. At any point in time, some sectors are leading, others declining. With a few exceptions which I will consider later, leading sectors tend to appear in all economies simultaneously. Agriculture and commerce dominated the 18th century. Cotton textile was the leading sector of the first half of the 19th century; steel and railways led the mid-century; electrical machinery and chemicals became dominant around the turn of the century; light machinery and automobiles led the interwar and the immediate postwar.[7] Electronics and telecommunications are today's carrying sectors. The reason for this simultaneous development is a combination of technological emulation and the presence in every economy of a domestic demand sufficiently large to justify investment in new products. The fact that these sectors cannot be competitive in all countries simultaneously is not a hindrance, as non-competitive sectors can, and do, obtain protection from their governments.

Furthermore, leading sectors often have military applications: cotton textiles to clothe the mass armies conscripted after the French revolution, the railways and automobiles to dispatch troops; high-tech to fight the wars of the future. Governments have vested interests in promoting these industries against all odds--the Italian steel industry in a coal-less economy probably was the most glaring example. The combination of economic and military competition led to the formation of relatively similar economies and societies across nations.

There were some exceptions, of course. The Netherlands and Denmark had no major industries up until World War I. Their specificity did not stem from smallness or the absence of natural resources, as much as from an early specialization which they managed to maintain until the turn of the century thanks to particular circumstances: the Netherlands initially was a country of wealthy merchants, specialists in transit trade; while successive military defeats reduced Denmark to being an agrarian island, which could afford to remain so temporarily thanks to the proximity and openness of the British market.[8] But these were passing exceptions; by the end of World War I, both countries had caught up in the industrial field. Current exceptions include most developing countries, whose endowment radically differs from OECD countries.

Generally speaking, therefore, economic and military competition account for the likeness in economic make-up among so-called "First World" countries at a given point in time. From this likeness, it logically follows that regime convergence, whenever it occurs, has the effect of empowering similar classes of producers.

This logic can be seen at work during the last two centuries. At the risk of simplifying the regime diversity that characterized the last two centuries, one can say that regimes fell into four broad categories, determined by the intersection of two dichotomies: the degree of democratization (democratic v. autocratic) and the scope of producer organization (sector v. factor). Democracy is defined as a regime that meets the following two requirements: (1) the government is the expression of the electorate directly (presidential) or via a lower chamber (parliamentary sovereignty), and (2) the electorate includes most of the directly taxable wealth--in the 19th century, this included at least property owners and leaseholders.[9] The scope of producer organization can either be the factor (land, labor, and capital) or the sector (crops, industries).

Crossing these two dimensions yields four regime types (Table 1). The absolutist monarchies of the 19th century empowered landowners, a class of producers owning a factor of production, along with commerce at the expense of the other two factors of production--labor and capital. In contrast, the constitutional monarchies, which were regularly formed in reaction to revolutionary pressures throughout the continent, were more inclusive. Rather than being class-based, constitutional monarchies were logrolling arrangements between the best organized sectors in agriculture and industry. Excluded from such arrangements were minor crops, small industrial sectors, unorganized crafts and professions, and the factor labor as a whole. Democratic regimes, like nondemocratic ones, also fall into two categories. Logrolling democracies empower all organized interests, irrespective of their factor of allegiance--major crops, large industries, and powerful trade unions. Competitive democracies, in contrast, are usually cleft along factor lines (the urban-rural cleavage of the 19th century mobilized land against capital and labor; the employer-employee cleavage of the 20th century mobilized labor against land and capital). Of necessity, competitive democracies empower the median voter, who is always a member of the numerically dominant enfranchised factor (capital in the first half of the 19th century, land in the second half, labor in the 20th century).

[Table 1]

The four regime types line up on the continuum defined by the insider-to-outsider ratio, with absolutist monarchy excluding labor and capital, constitutional monarchy excluding labor and minor sectors an crops, logrolling democracy excluding minor sectors and crops, and competitive democracy including all producers (Graph 1).

[Graph 1]

Regime Convergence and Trade Flows

Back to the initial question: Given any initial mix of regimes, what would be, holding everything else constant, the impact of regime convergence on trade flows? Regime convergence creates power profiles identical across countries. Consider the example of convergence around absolutist monarchy. Absolutist monarchies empower land at the expense of capital and labor. Whether the result is good or bad for trade depends on the type of specialization sparked by trade: by factor endowments or by products. In a nutshell, the argument of this section runs as follows: If trade causes trading economies to specialize on the basis of factor endowments, then in about half of them, trade will benefit landowners, whereas in the other half, it will harm them. Having power in at least one half of the trading universe under conditions of regime convergence, the thus-threatened landowners will use that power to discourage trade. If, in contrast, trade triggers product specialization, with one absolutist monarchy specializing in lumber, another in timber, still another in paper products, and so on, then all monarchies will benefit from, and welcome, trade. Let me develop.

Economists have isolated two very different rationales for trade. On the one hand, trade may be caused by differences in factor endowments--this is the Heckscher-Ohlin model of international trade. For instance, if Prussia is land abundant and capital poor, whereas England is land poor and capital abundant, then capital-intensive products (manufactures) are more cheaply produced in England than in Prussia, whereas land-intensive products (foodstuffs) are more cheaply produced in Prussia than in England. In the event of trade, Prussian consumers prefer English manufactures to those produced indigenously, while English consumers prefer Prussian to home-grown foodstuffs. The upshot is a specialization of the two economies on the basis of factor endowments--Prussia produces foodstuffs, England produces manufactures.

On the other hand, trade may be fueled by the presence of increasing returns to scale--decreasing unit costs associated with longer production runs. This second model is known as the imperfect competition model of international trade.[10] If a firm can increase its profit margin by expanding the scale of production, it will keep expanding production until it services the entire market demand for its product. The upshot is a monopoly, which rival firms cannot contest by entering the line of product, unless they can immediately out scale the incumbent firm. What rival firms can do, rather, is to produce a different product and, given that consumers value product diversity, reveal a demand for it through advertising. As a result, trade induces specialization by product, but not necessarily by industry, each country maintaining a presence in every industry. In sum, trade occurs within industries (it is usually referred to as "intra-industry" trade) rather than between industries ("inter-industry" trade) as in the Heckscher-Ohlin model.

The two types of trade have radically different wealth effects. As said, with trade of the inter-industry type (Heckscher-Ohlin), a country will export the goods that use intensively its abundant factor and import the goods that use intensively its scarce factor. An increase in the price of any good causes an increase in the real return to the factor used intensively in producing that good, and a fall in the real returns to all other factors. Therefore trade, by raising the price of exportables, benefits the abundant factor and hurts the scarce factor, whereas protection, by raising the prices of importables, benefits the scarce factor and hurts the abundant factor.[11] Trade allocate the gains and losses from trade along factor (land, labor, capital), and thus class, lines.

Trade gains and losses can also be allocated along industry (or sector) lines, as in a variant of the Heckscher-Ohlin model--the so-called "specific-factor" model.[12] Responsible for class redistribution in the original specification is the assumption that factors are mobile across industries. All industries are said to draw indiscriminately from the same factor pools, with the result that factor prices in each industry reflect supply-demand conditions in each factor market nationwide. If, instead, factors are industry specific, that is, are imperfectly substitutable across industries or cannot be as gainfully employed in a different industry, then factor prices no longer reflect nationwide supply-demand conditions, but are determined by supply-demand conditions specific to each industry. This variant of the Heckscher-Ohlin model allocates the gains and losses from trade along industry lines. The fate of factor owners is not identified with the fate of their respective factor nationwide, but with the fate of their respective industry of employment. The difference between these two specifications, however important it might be for the modelling of policy processes,[13] should not make us lose from sight the shared trait that makes these models two instances of the inter-industry-trade family--trade strictly develops along comparative advantages, redistributing income from scarce factors (or industries employing scarce factors) to abundant factors (or industries employing abundant factors).

In contrast, intra-industry trade (imperfect-competition model) does not entail redistributive effects of such proportion. In that model, trade does not strictly develop in accordance with comparative advantages, but can also occur between similarly endowed countries, with little or no wealth effects.[14] To understand why, it is important to keep in mind the distinction between factor, industry, and product: the industry is a group of products, and factor endowments are the same for all the products within a given industry. The reallocation of resources induced by product-specialization is factor neutral, each factor of production moving from a "lost" product to a "captured" product within the boundaries of a given industry, and thus in equal proportion, given the invariance in factor endowments. Factor neutrality implies zero distributive effects. That reallocation, further, is almost costless in comparison to that triggered by sector-specialization, factors being more mobile within the boundaries of their industry of employment than across industries.[15]

A caveat is in order. The fact that intra-industry trade has no redistributive effects does not necessarily imply that there are no redistributive effects. Scale economies have a negative side-effect--free trade's lost Pareto efficiency. Under scale economies, specialization does not reflect factor endowments, but first-mover advantages--the first firm to enter a product-niche locks in. This feature makes it rational for states to financially help their nationals capture those niches. This is the strategic dimension of new trade theory. A subsidy to a domestic firm, by deterring investment and production by a foreign firm, can raise the profits of the domestic firm by more than the amount of the subsidy.[16] Socially desirable in theory, trade promotion is in practice likely to be hijacked by firms in presumed growth sectors, seeking to extract more rents than socially desirable. This is all the more probable that the costs of collective action incurred by single firms (the lobbying units in imperfect competition) are lower than those incurred by industries or factors (the lobbying units in perfect competition).[17]

Therefore, intra-industry trade may indirectly elicit as many wealth effects as inter-industry trade would, though with two important differences with respect to the identity of the winners and losers and the impact on trade. First, rents are sought by firms rather than industries, and by firms involved in high-growth activities rather than traditional sectors. Conversely, the direct losers are consumers, and taxpayers, that is, groups much more diffuse and politically inept than the scarce factors and/or import-sensitive sectors victimized by inter-industry trade. Second, to the extent that protection helps firms capture scale economies, protection promotes rather than hurts trade.[18]

It is now possible to see how regime convergence has opposite consequences for trade policy depending on whether trade is of the inter-industry or intra-industry type. If trade is of the intra-industry type (to start with the simpler case), mainly propelled by scale economies, then trade can only cause product specialization, without prejudice to factor holders' relative wealth and power. Surely, taxpayers and consumers may suffer from socially undesirable rents and subsidies accruing to single monopolistic firms, but they do not constitute an effective opposition. Factor holders being demobilized, trade policy is indifferent to the type of the regime.[19] Regime convergence and divergence per se have no effect on trade--other variables will prevail.

In contrast, if trade is of the inter-industry type, mainly propelled by relative comparative advantages, trade threatens to spur a specialization on the basis of factor endowments. Having power in about half of the trading universe under conditions of regime convergence, the thus-threatened factors will use that power to discourage trade. Under conditions of inter-industry trade, therefore, regime convergence will never promote trade, but may actually reduce it. Conversely, regime divergence will never reduce trade, but may actually promote it.

A simple proof of this last proposition, while controlling for factor endowment, can be found in Table 2 for the two extreme regime types--absolutist monarchy and competitive democracy. Assume two factors of production, land and capital, and two countries, Land-Rich and Capital-Rich. Further assume without loss of generality that an autocratic regime empowers land, whereas a democratic regime empowers industry. This two-country world economy defines four possible states of the world: both countries are democratic, both are autocratic, one is democratic while the other is autocratic, and vice versa. Each cell shows trade flows between the two countries, coded as "high" or "low." The table also shows two sets of four arrows each; solid arrows (numbered 1, 2, 3, 4) represent all the possible cases of regime convergence, whereas broken arrows (numbered 5, 6, 7, 8) represent all the possible cases of regime divergence. In each set, two arrows (numbered 1 and 2, 5 and 6) leave the initial trade flows unchanged. The last two arrows of each set, however, point in opposite directions--two convergence (solid) arrows (3, 4) cause a decline in trade flows, whereas two divergence (broken) arrows (7, 8) cause an increase in trade flows.

[Table 2 here]

No particular proof is required that includes the other two regime types (constitutional monarchy and logrolling democracy). A logrolling democracy is protectionist by definition, because it empowers protectionist sectors (among others). A constitutional monarchy could support openness in only one case: if both land and capital were abundant factors. This combination could be treated analogously to the case of land-abundant absolutist monarchy. It has no empirical relevance here, however, as it does not figure in our sample of countries.[20]

Hence the following proposition: Under conditions of inter-industry trade regime convergence will never promote trade, but, depending on the particulars of the case, may actually reduce it. Conversely, regime divergence (defined as a mix of the two extreme regime types) will never reduce trade, but depending on the case may actually promote it.

The Determinants of Trade Type

Given the role played by trade type in determining the impact of regime type on trade flows, it is important to identify the conditions under which intra-industry trade will emerge. Assume for the sake of simplification that the relative proportion of intra- and inter-industry trade is the sole function of scale economies. Scale economies reflect the technology of production. Technology of production, which, for our purposes, may be taken as exogenously given, is a necessary condition for the development of mass production.

Yet, since actual investment in large-scale production is unlikely to occur unless the product can be sold at a profit, another necessary condition is mass (worldwide) marketing.[21] Worldwide marketing, in turn, requires access to foreign markets, which trade restrictions might impair. True for any type of trade--intra- or inter-industry--this proposition is more true for intra-industry trade, with its large fixed-cost requirements, than for inter-industry trade, with relatively smaller fixed-cost requirements. Therefore, the intra-inter-industry ratio is not merely a positive function of technological advance, but of trade openness as well.[22]

If trade type depends on trade openness, one must ask whether it is a variable that is endogenous to the present model, for, were it so, one would face a case of circularity, since the present model derives trade openness in part from trade type (regime type being the other independent variable). The answer is in the negative. Following the groundbreaking work of Beth and Robert Yarbrough, it seems that mere openness (assuming the technology condition met) may not be sufficient for intra-industry trade to develop.[23] Openness must also be irrevocable. Without a long horizon, firms will not risk sinking the fixed costs otherwise required for the capture of worldwide scale economies. Firms will not invest in facilities of which the expected value is dependent on permanent access to foreign markets short of adequate guarantees. Governments can credibly commit to keep access open through long-term, binding trade agreements. Whether they do so or not is exogenous to the policymaking model developed here. In sum, the intra-inter-industry trade ratio reflects the simultaneous play of three variables, among which, one, free trade, is endogenous to the present model, and two, technological advance and the existence of an international trading regime of some sort, are exogenous.

Historically, the technological condition for scale economies was potentially met about half-a-century earlier than the regime condition. By the turn of the century, leading economic sectors (steel, machinery, refining and distilling) recorded technological breakthroughs, making world scale production a technological possibility. Mass marketing, however, lagged behind, being slowed down by narrow domestic markets (U.S. excepted), backward imperial markets, and chronic uncertainty about access to foreign markets, with the overall result of stalling the trend toward worldscale production. It is not until the GATT that stable access to foreign markets became a reality. The GATT success reflected two simultaneous changes in the international power structure: U.S. economic hegemony after World War II and the consolidation of capitalist countries into a tight security bloc during the Cold War[24]--two events exogenous to regime type.

The Liberalization of Trade in the 19th Century

There is not enough variation in the trade type variable to enable a systematic test of the propositions presented above. More humbly, I plan to show that a plausible case can be made that the two most important instances of world trade liberalization in modern world history fit the present description. Further, I will show that the present model helps illuminate historical facts that, until now, had remained obscure or, in light of the present analysis, are from now on puzzling. One of these facts is the timing of trade liberalization in 19th-century Europe. Another is the easiness with which OECD countries managed to promote openness. I start with the 19th century.

Two explanations have been offered to account for the breakout of free trade in the 19th century--hegemonic stability and liberal ideology. The vices and virtues of hegemonic stability theory have been so well and so often sung elsewhere that brevity is apropos.[25] The theory makes free trade a function of hegemony. However, there is a discrepancy between British diplomatic activism (a behavior that a hegemon is expected to engage in according to the theory) which occurred in the 1820s and 1830s, and the advent of free trade, which occurred twenty years later, and was instigated by France, not Britain. Although British technological advance played a crucial role in shaping the pattern of 19th-century trade--indeed it drew the pattern of specialization along which trade unfolded once freed--it was insufficient in precipitating openness in the first place.

The liberal ideology approach has received less attention. Charles Kindleberger argued that free trade triumphed thanks to the diffusion throughout the continent of Manchesterian doctrine--a creed in the superiority of free trade.[26] Although Kindleberger did not make explicit the mechanism of diffusion of the free trade idea on the continent, it can be reconstructed in analogy to his analysis of its triumph in Britain. The free trade doctrine spread, we are told, along with the liberal creed--a philosophical and political program with implications far beyond trade. The liberal ideology entailed the upsetting of the old aristocratic order. Free trade and the reform of the franchise were both expected to dilute the power of the gentry, free trade in the economy, the franchise in parliament. For the free trade doctrine to spread to the continent, a similar linkage with the rise in power of liberal movements should have been at work. The triumph of free trade should have accompanied the triumph of liberalism. In reality, the two were unrelated. Free trade did not break out when liberal movements on the continent were on the ascent in the 1830s and 1840s, but when they were on the retreat, during the restoration of Conservative, pro-agrarian rule in the 1850s and 1860s. It is, I argue, this growing regime divergence between liberal Britain and a reactionary continent that was a necessary condition for the advent of free trade in the middle of the century.

To show this, we need to consider two variables--the distribution of factor endowments and the distribution of regimes. Throughout most of the 19th century, trade was of the inter-industry type. The state of technology did not allow for mass production. Trade essentially reflected dissimilarities in factor endowments.[27] Britain was capital abundant and had an edge in capital-intensive industries such as semi- and coarse manufactures (yarn, iron). Lagging continental Europe was capital scarce and maintained an advantage in agriculture (grain, timber, wine) and skilled crafts (silk, etc.).[28] On the continent, three nations were capital abundant in relation to the rest: two early continental industrializers, Switzerland and the Belgian part of the United Netherlands (Holland-Belgium), and a late-industrializer yet a nation of merchants with plenty of cash, the Dutch part of the United Netherlands. Prussia, the Austrian empire, Italy, Denmark, Sweden, Norway, Russia, and, to a lesser extent, France, were abundant in land and labor. The United States, Canada, Australia, and New Zealand were abundant in land only.[29]

Regime distribution changed over time, delineating four separate periods--the first restoration (1915-29); the revolutionary years (1830-49); the second restoration (1850-1874); and the Long Depression (1875-1894). The first period was characterized by the coexistence of two regime types--land-based absolutist monarchies and logrolling constitutional monarchies. Absolutism was triumphant in Prussia, Russia, and the Austrian empire, and to a lesser extent in Scandinavian countries, which were ruled by an oligarchy of bureaucrats related to mercantilist interests.[30] In contrast, monarchy was constitutional in Britain and its colonies, France, and Holland-Belgium. A third type of regime, democracy, was also present though residual (Switzerland and the United States).

During this first period, demands for trade with Britain came from the absolutist monarchies in which policymaking was class-based, land was abundant (with a domestic market too narrow to be self-sufficient), or the mercantile interests were concentrated and powerful. Included in this category were Prussia, Denmark, and Poland(Russia) on account of grains, Sweden and Norway on account of timber, and Scandinavian nations at large on account of shipping. The Austrian empire and Russia were autarkic, on account of the gigantic size of their domestic markets.

In contrast, constitutional monarchies (Britain, Holland-Belgium, France) and the United States (a logrolling democracy) indulged in protection. In Britain, the King's minister consistently tried to accommodate manufacturers' demands for free trade by repealing all prohibitions and reducing tariffs on manufactured goods, yet without undercutting the landed gentry's and the merchants' rents generated by the Corn Laws and the Navigation Laws respectively. In the low countries, the King sought to rally behind his crown both the Dutch merchants who wanted free trade and navigation laws, and the Belgian industrialists who wanted protection, through a mix of low tariffs and direct subsidies to manufacturing (an indirect form of protection).[31] The British colonies (mostly Canada, since Australia and New Zealand were barren territories still) enjoyed privileged access to the British market, while levying tariffs on neighbor's exports (the Canadian eastern provinces levied a tariff on U.S. wheat). Tariff protection was also present in France, where the industrial bourgeoisie was already part of the ruling coalition while a large component of the landed gentry, the owners of large wooded estates supplying charcoal to the iron industry, were already vested in industry.[32] Protectionism triumphed in the United States with the 1824 tariff, a textbook case of pork-barrel politics.[33] Swiss tariff policy was the exception, perhaps on account of the lilliputian size of its cantons, which, during the 1815-1848 period, controlled the power to tax.[34]

In sum, although absolutist monarchies wanted to export their wheat and timber, the only foreign market for these items, the British constitutional monarchy, was protected by tariffs and imperial preferences. Unable to procure sterling, absolutist monarchies thus had no incentive to lower their industrial tariffs.

The liberal revolutions of the second period modified regime alignments. Two successive waves of popular unrest occurred, the first in 1829-1834, the second in 1848. They affected all of Europe West of Russia including North America. They were the offspring of the income-distribution effects generated by industrialization, and mostly felt in periods of economic downswings (1830 and 1847), and of a failure in 1846 of both the grain and potato crops, responsible for the last major famine in Europe.[35] In response to the revolutionary upheavals, six countries (Britain in 1832, Belgium in 1847, Canada, France, Denmark, and the Netherlands in 1848) established parliamentary rule and extended the franchise to property-owners and leaseholders at the least, raising to eight the number of democracies. Moreover, both old and nen democracies were then competitive; in response to the crisis, they registered record mobilization levels, and evinced the first manifestations of party politics. Among the nondemocracies that weathered the storms (Prussia, Austria, Sweden-Norway), none managed to maintain prior class purity, being forced instead to coopt bourgeoisies and turn into constitutional monarchies. Only Russia was spared from domestic disturbance, and remained absolutist. In sum, the crisis reduced the preceding regime variety to two categories: competitive democracy and consitutional monarchy.

During this second period, the establishment of parliamentary (democratic) rule was generally favorable to trade liberalization. This coincidence between regime and policy is certainly in keeping with an ideology-based account, as it came about not only in capital-rich countries (Britain, Belgium, the Netherlands, and Switzerland), but also in land-abundant Denmark, Canada, and the United States.[36] Only the French Second Republic failed to match political liberalism with trade liberalization.[37] But while the growing strength of liberalism was generally favorable to free trade in democracies, it had opposite consequences in nondemocracies (Prussia, Austria-Hungary, Sweden).

Even though the opening of the British market to grain and timber was a boon to most continental agrarians, the political instability of the revolutionary years weakened the power of land. Indeed, although the surge in political unrest forced monarchs on both sides of the channel to dilute the political monopoly of land, reverse factor endowments implied reverse policy consequences--free trade for Britain, protection for the continent. The political rise of the bourgeoisie put the gentry on the defensive and made it unlikely to adopt a trade liberalization that could upset new industries and exacerbate revolutionary fervor.[38]

Norway was an exception to that trend. Although a nondemocracy, it responded to popular unrest by reducing several tariffs on manufactured articles. Part of the reason is that the challenger group in Norway (as in Denmark) was not the industrial bourgeoisie, but the small farmers, whose protective tariffs were spared by the tariff reductions.[39]

The trend toward free trade, which was characteristic of the third period, started in the 1850s, not in the 1860s as usually believed. The mid-century trade liberalization was not attributable to the triumph of liberal ideas and institutions on the European continent. Liberalism outlived the second restoration in a handful of countries only: Britain, Belgium, the Netherlands, and Switzerland. In these four countries, liberals articulated the preferences of capital, the abundant factor, and pressed for free trade. The rest of the continent, however, experienced another restoration of autocratic rule. Protectionist bourgeoisies in Germany progressively lost the ground conquered in 1848 to the landed elites.[40] The Austrian empire followed the same trajectory. The simultaneous restoration of land rule allowed Prussia and the Austrian empire to engage in a "free-trade war" for the allegiance of the German states. Austria lowered her duties with Prussia and other Zollverein countries in 1851 and 1853.[41] Even in Denmark, the absolutist reaction of 1864 was associated with a repeal of the 1863 industrial duties, adopted to federate the Duchy of Holstein (eventually seized by Prussia and

Austria).[42] In sum, given the protectionist orientation of industrialists on most of the continent, it was the restoration of land rule, not its dilution, that was key to the growth of trade between Britain and the continent.

The conclusion of the 1860 Anglo-French tariff agreement is further evidence of the antiliberal origins of free trade. For several decades, owners of large wooded estates and producers of charcoal iron together had established a lock on the French parliament, effectively blocking all free trade initiatives emanating from disparate export interests such as the Bordeaux wine growers, the Lyon silk weavers, shippers in port cities, and the Parisian crafts. In 1851, Louis Bonaparte established a dictatorship. His free trade orientation reflected the preferences of a small coterie of bankers and Saint Simonian ideologues, as well as his military ambitions. In 1860, presented with a unique diplomatic opportunity, Napoleon plotted his "economic coup d'état," opening the French market to Britain and Prussia in exchange for these countries' assent to his annexing Nice and Savoy at the expense of Austria.[43] Free trade managed to outlive the despot in part by decimating uncompetitive industries, and in part by tying the hands of future Republican chambers to a web of treaties.

The treaty formula was in tune with the reactionary pitch of the time. It not only offered the advantage of bypassing parliaments, if not altogether, at least through the negotiating stage, but it also took the tariff off the parliamentary agenda for the duration of the agreements--ten years at a time. The quasi-expropriation of legislatures is believed to have been essential to the passage of treaties not just in France, but also in Sweden.[44] In both countries, the return to protection in the next period would be intimately associated with the reaffirmation of parliamentary sovereignty over executive discretion.

Russia was no exception to the trend toward greater openness. In the wake of the Crimean debacle (1853-56), the still-absolutist Czar abolished serfdom and reduced the duties on machinery and raw materials necessary to the building of the railway system, which had proven so wanting during the war. The railway-building boom of the 1860s opened western European markets to grain grown in the distant eastern provinces. Russian heavy industry, which until then had used serf labor, fell by the wayside after the emancipation of 1861.

With France under the heel of a free trader, Denmark, Germany, and the Austrian empire experiencing a restoration in aristocratic rule, and Russia shedding its autarkic posture, the conditions for European free trade were finally realized. These conditions were regime divergence and class-based (or dictatorial) rule--the conjunction of liberal hegemony in land-scarce countries and the restoration (or continuation in Russia) of absolutism in land-abundant economies, plus a dictatorship committed to free trade in France.

The fourth period is marked by the simultaneous end of regime divergence and trade openness. The mid-century regime divergence, wich was so benevolent to trade, did not last. The onset of the Long Depression of 1874-1994 weakened absolutist rule, obliging monarchs to bring protectionist bourgeois elements into the ruling coalition (Germany, Sweden, Russia). The crisis also terminated democratic competition, obliging bourgeois and agrarian parties to contrive a protectionist logrol (France in 1892, Switzerland in 1902, Norway in 1896), along with an understanding to rigg elections in Spain and Italy. It is impossible to prove, however, that the the end of mid-century regime divergence was the sole reason for the surge in protection. A realignment in factor endowments, which occurred in the 1860s, but was not actually felt until the 1870s, was also favorable to a systemwide rise in protectionism. The opening of new lands in the United States, Canada, Australia, and Russia, combined with the decrease in transport costs, nixed the comparative advantage enjoyed by agriculture on the European continent and turned agrarians into the willing partners of "iron-and-rye" protectionist coalitions. There is one case, however, in which this spurious simultaneity in regime and endowment change was absent--the Austrian Empire. The Austrian monarchy was the first to renounce absolutism, twice actually, subsequent to military defeats. The 1859 defeat at the hands of the French and Piedmontese caused a brief constitutional detour lasting until 1864, while the 1866 defeat at the hands of the Prussians ended absolutism for good. On both occasions, the cooptation of bourgeois elements had the expected negative trade effects: Austrian industrialists used their newly gained constitutional powers to block the signing until 1865 (and the implementation after 1866) of the 1865 Tariff Treaty with Britain, forcing Vienna to beg London to agree to a much-watered down version in 1869.[45]

<u>The Liberalization of Trade in the Postwar Era</u>

Only afer World War II were the two conditions for the headway of intra-industry trade--large-scale production technology and worldwide marketing--simultaneously met. Surely, intra-industry trade had existed before in the form of reciprocal dumping. Reciprocal dumping required no scale economies beyond what is necessary to have a monopoly or a cartel in each country.[46] Since the late-19th century, cartels used the domestic market as a springboard for the conquest of foreign markets through means of systematic dumping abroad bankrolled by monopolistic pricing at home. Although the best documented cases of systematic dumping were U.S.Steel and the German cartels, about every national steel industry was a part to the game. Dumping was common practice in industries blessed with nationwide scale economies.[47] Reciprocal dumping was the first sign that industrial capitalist countries were becoming alike in terms of relative factor endowments--all were capital abundant. However, scale economies had not reached the scope required to make product specialization a reality yet. The high barriers to trade that cartels exacted checked the further advance of scale economies and the product specialization that would have otherwise evolved. Rather than specialize, firms in high-growth industries tried alternative strategies such as worldwide cartelization, horizontal diversification, colonial expansion, and implantation in protected markets. The 1920s and 1930s saw no change in trade parameters: trade remained of the inter-industry type. Although improvements in production technology raised scale economies, World War I aborted any product specialization achieved in the 1910s (while the Great Depression of the 1930s contracted trade).

It is not until World War II that marketing, and thus production, on a world scale became viable corporate strategies. Western nations committed themselves to developing a multilateral process of trade liberalization, with the effect of securing long-term access to foreign markets for domestic producers. The postwar trade regime owed a lot of its success to World War II and the Cold War, which superimposed security concerns upon economic ones. The distinction between friends and enemies was sharply drawn. The founders of the Atlantic Charter, the GATT, and the European communities all had clear enemies in mind: Germany until 1945, the Soviet Union after 1946. Between OECD countries, trade was used as a means of consolidating the NATO military alliance,[48] while within each OECD country security was invoked to overcome protectionist opposition.[49]

However, the security logic, which led to the alliance of democracies against communist regimes, worked at cross-purposes with the free-trade logic, which called for the presence of different producer groups in positions of power. In Britain, France, the United States, and their military allies, policymaking was democratic. Their regimes empowered the numerous factor--labor--irrespective of whether the democracy was of the logrolling or competitive type. In competitive democracies like Britain, Germany, and New Zealand, labor was empowered as the median voter, for whom parties competed; in logrolling democracies like France, Italy, Sweden, Norway, Denmnark, Australia, and Japan, labor was empowered as an interest group, the trade unions of labor-intensive sectors.[50] Although trade was desirable from a security perspective, it was unlikely from a political perspective.

Unable to endure the wealth effects that a rise in trade of such magnitude would invariably entail, GATT members promoted intra-industry trade at the expense of inter-industry trade. They engaged in intra-industry tariff cuts, limiting import concessions to those foreign industries that reciprocated with concessions on exports, so that the adjustment costs for any industry as a whole were low.[51] They used imperial preferences, import quotas, and VERs to maintain industrial diversity. And several among them resorted to supply-side protection (planning, industrial policy), using subsidies and other product-specific instruments not covered by the GATT, to secure a national presence in growth sectors.

The upshot of this carefully managed liberalization was a moderate rise in trade accompanied with little specialization, and thus few wealth effects.[52] Hufbauer and Chilas compared interwar with postwar degrees of trade specialization in eight countries and found no significant increase in trade specialization.[53] Further studies recorded a rise in intra-industry trade in most industrialized countries throughout the fifties and sixties.[54]

The postwar trend toward a rise in intra-industry trade countenanced three exceptions, which, as a result of being exceptions, have prompted many disputes. A first exception concerns agricultural trade. For Australia and New Zealand, two countries for which trade still meant, after 1945, an exchange of primary goods for manufactures, the growth in postwar trade was not accounted by a rise in intra-industry trade, which remained inferior the OECD average.[55] As a result, these countries kept their tariffs higher and longer than their trade partners. A second exception concerns trade with NICs and LDCs. GATT trade liberalization induced inter-industry trade with less advanced economies. Although, in theory, supply-side instruments could also be used to cushion trade-induced wealth effects on traditional industries, some countries found it politically wiser to reimpose demand-side restrictions in the form of quotas and VERs--"managed trade." The 1962 multifiber agreement, for instance, slapped multilateral quotas on textiles.[56] A third exception is Japan, the OECD economy with the lowest level of intra-industry trade. The alleged causes for such a low level vary from high energetic dependence with oil accounting for most imports, different consumers' taste disqualifying foreign producers, and old-fashioned protectionism. This low level of intra-industry trade caused severe frictions with other OECD countries, the United States especially, which accused Japan of unfair competition and extracted voluntary restraints. Japanese competition was responsible for the high levels of protection found in the steel and automobile sectors of the West.

The promotion of intra-industry trade in the postwar era can account for the simultaneity in the postwar era of facts that seem contradictory in light of prewar experience: the growth of trade in spite of similar endowments, similar regimes, and increasing subsidies and NTBs.

Recent Developments

The postwar trend towards increased intra-industry trade tapered off in the late 1970s for a range of countries and industries.[57] Various reasons have been alleged. One is a reduced consumers' taste for variety, compounded by an increased variety in consumers' taste.[58] The slower growth registered since 1975 may have reduced consumers' taste for variety (presumed to be a function of income). Simultaneously, the greater importance assumed by Asian markets in world trade in the last twenty years may have had the overall effect of increasing the variety in consumers' tastes, segmenting the world market along geographic rather than product lines. The Japanese government, for instance, claims that Japan imports few Western-made products because of a dissimilarity in taste between Asian and Western consumers (whether taste dissimilarity reflects a deep-seated cultural differences or is contingent on protectionist retailing and marketing practices is unclear though).

Another reason is the renewal of the supply side tool kit--the replacement of subsidies by deregulation and privatization. Following the oil shocks and the subsequent inflationary crisis, the world economy went through a depression (1979-83), followed by slow growth since. The crisis turned existing subsidies to industry (especially traditional) into budget busters. Coalitions of taxpayers and competitive sectors successfully revolted against state intervention in industry.

The strategic dimension of intra-industry trade was an additional incentive for the scrapping of subsidies. In response to the crisis, governments increased export subsidies to particular firms, in order to maintain market share at the expense of competitors. The competitors' respective governments, however, retaliated with equivalent subsidies. For instance, in 1986, the U.S. Congress authorized funds to build a "war chest" for export credit. To avoid a self-defeating and unsustainable subsidy escalation, European governments preferred to cut their losses; they agreed to a general limitation of export credits with the United States.[59]

Fearing retribution from both voters and trade partners, governments looked for cheaper and retaliatory-free supply-side policies. They phased out product subsidies, compensating firms with measures destined to reduce their costs of production--deregulation and privatization. Low growth and high unemployment rates among blue-collar workers, with their crippling effects on trade-unions market power, enabled firms to cut wage costs as well. The greater generality of these new measures lowered the risk of international retaliation.

The impact of this policy revolution was to slow down the trend toward intra-industry trade. While deregulation and privatization improved the competitiveness of firms, their effects are less particular than subsidies, and thus less useful in product targeting. National economies since the 1980s have a lower likelihood to maintain a significant presence in all sectors of industry. Over time, the phasing out of subsidies is likely to cut into intra-industry trade while raising trade-induced wealth effects.

These changes adumbrate a return to the trade politics of the pre-World-War-II era. An early sign of this transformation is the ongoing realignment already visible in some of the most politically competitive capital-abundant OECD economies: right and left are re-positioning themselves along the trade cleavage, the right on the side of free trade, the left on that of protection. The first open manifestation of this trend was the 1989 Canadian debate on the North-American treaty. The 1993 U.S. Congress vote on NAFTA also was abnormally partisan, with many industries showing an internal split pitting labor unions, opposed to the agreement, against management and share-holders, supporting it.

Conclusion

The goal of this paper has been to offer an argument supported by preliminary evidence for two complementary claims: if trade is propelled by factor endowments, similarity in political regimes, like similarity in factor endowments, chokes trade; conversely, if trade is propelled by scale economies, it may develop in countries with similar factor endowments and regimes.

The claim that a democratic world is likely to be open does not hold. Democratic convergence impacts world trade negatively if trade is of the inter-industry type. Hence, contrary to the belief that the free trade system in mid-century reflected a more general spread of liberal ideas, I argued and showed that it rested instead on a particular mix of democratization in Britain and reaction on the continent. Trade would not have expanded had continental landed aristocrats shared power with rising industrialists at the same pace as their British cousins. Free trade, a liberal economic idea, required a dose of absolutism, a nonliberal political idea. Absent scale economies, regime convergence undermined trade. In contrast, the postwar democratic convergence among OECD countries did not hurt trade because similarity in endowments, combined with the presence of scale economies, allowed these countries to engage in intra-industry trade--a form of trade with few, if any, wealth effects.

Following the collapse of the Soviet bloc, democracy is now spreading to economies that are not capital abundant and, thus, that cannot easily fend off the wealth effects induced by trade by pursuing intra-industry trade. It would be a mistake, therefore, to predict that the spread of democracy to Eastern Europe is good for world trade. If anything, the current wave of democratization endangers trade. Only in the presence of scale economies can democratic convergence sustain trade.

Notes

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6. In the Manifesto of the Communist Party, for instance.
7. James R. Kurth, "The Political Consequences of the Product Cycle: Industrial History and Political Outcomes," International Organization 33, 1 (Winter 1979), 1-34.
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9. The regimes that met these two requisites (and periods during which they did) were the United States

(1787-), Britain (1832-), Belgium (1847-), Switzerland (1848-), Denmark (1848-1864, 1901-), France (1848-1851, 1871-), the Netherlands (1848-), Canada (1848-), New Zealand (1853-), Australia (1856-), Spain (1868-1874; 1931-36; 1977-), Norway (1884-), Sweden (1905-), Italy (1912-1922, 1945-), Germany (1919-1933, 1945-), and Austria (1919-1934, 1945-). Russia remained autocratic throughout.

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11. A. V., Deardoff and R. M. Stern, eds. 1994. The Stolper-Samuelson Theorem: A Golden Jubilee (Ann Arborr: The University of Michigan Press, 1994).

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14. P. R. Krugman and M. Obstfeld, International Economics: Theory and Policy, second edition (New York: HarperCollins, 1991), 140.

15. The no-wealth-effect result only applies to intraindustry trade between similarly-endowed economies, not to intraindustry trade between dissimilarly-endowed economies. In practice, however, the latter is a rare occurrence; there is a strong correlation between trading partners' factor endowments and trade type (Krugman and Obstfeld, 141). For this reason, I will overlook the case of intraindustry trade between dissimilarly-endowed economies.

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17. Firms belonging to the same industry do not have a common trade interest; some firms capture a niche while others are displaced by foreign competition. The collective action aspect is also emphasized by Michael Gilligan, "Trade policy Coalitions with Intra-Industry Trade," Paper delivered at the Annual Meeting of the APSA, Chicago, 1995, who argues that trade lobbying in the U.S. is

carried out by single firms.

18. Krugman and Obstfeld, 271.

19. The point is that taxpayers and consumers are difficult to organize. The fact that they are also producers is immaterial, absent wealth effects mobilizing them as producers.

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TABLE 1: REGIME TYPES

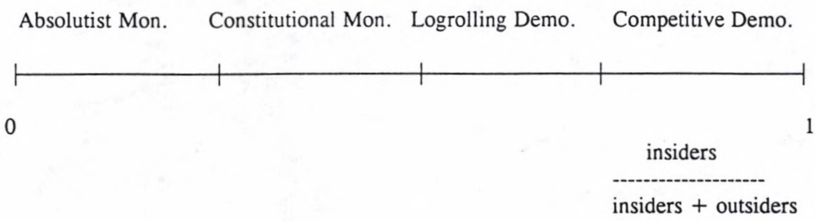
		DEGREE OF DEMOCRATIZATION	
		AUTOCRATIC	DEMOCRATIC
SCOPE OF ORGANIZATION	FACTOR	absolutist monarchy	competitive democracy
	SECTOR	constitutional monarchy	logrolling democracy

TABLE 2: EFFECT OF REGIME CONVERGENCE ON TRADE FLOWS
IN A TWO-COUNTRY WORLD ECONOMY

LAND-RICH \ ***K-RICH***	DEMOCRATIC (scarce land in power)	AUTOCRATIC (abundant capital in power)
	$\xleftarrow{\ 3\ }$ (solid); $\xrightarrow{\ 7\ }$ (broken)	
DEMOCRATIC (scarce capital in power)	LOW TRADE FLOWS. reciprocal taxation.	LOW TRADE FLOWS. K-rich is open to L-rich foodstuffs but cannot afford any in the absence of currency earnings; L-rich taxes K-rich manufactures
	$\uparrow$ 2 (solid); $\downarrow$ 6 (broken)	$\uparrow$ 8 (broken); $\downarrow$ 4 (solid)
AUTOCRATIC (abundant land in power)	LOW TRADE FLOWS. K-rich taxes L-rich food-stuffs; L-rich is open to K-rich manufactures, but cannot afford any in the absence of currency earnings.	HIGH TRADE FLOWS. reciprocal trade.
	$\xleftarrow{\ 5\ }$ (broken); $\xrightarrow{\ 1\ }$ (solid)	

Note: the solid arrows (1, 2, 3, 4) represent cases of regime convergence, the broken ones (5, 6, 7, 8), cases of regime divergence.

GRAPH 1: REGIME TYPES RANKED ACCORDING TO INCLUSIVENESS



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