

10 MIHAIL MANOILESCU: AN APPRECIATION AND A CRITIQUE

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Abstract

On the 70th anniversary of the German-language edition of his book published in French in 1929 as *Théorie du protectionnisme et de l'échange international* (followed by an English translation of 1931 with the title *The Theory of Protection and International Trade*), Mihail Manoilescu became a pioneer in the theory of international trade by elaborating on an important market failure that violated the assumption of perfect competition in all commodity and factor markets postulated by the standard neoclassical trade models, in the form of a wage paid in a country's manufacturing sector that exceeds that paid in agriculture. Manoilescu argued that the country would be subject to "unequal exchange" in trade unless it protects its manufacturing sector. Following Manoilescu's lead, a market failure of this type was incorporated in neoclassical trade models by Everett Hagen in 1958 as a prototype of the market distortions that became an important part of the postwar trade literature. It is regrettable that Manoilescu's pro-fascist sympathies subsequently led him to abandon his views in favor of Romania's becoming a supplier of primary commodities to the Third Reich.

Key words: Manoilescu, theory of protectionism, unequal exchange, intersectoral wage differential

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On the 70th anniversary of the German-language edition of his famous book originally published in French in 1929 as *Théorie du protectionnisme et de l'échange international* (followed by an English translation of 1931 with the title *The Theory of Protection and International Trade*), Mihail Manoilescu is remembered as an intellectual who influenced the theory of international trade after his death in ways that he himself would have been surprised to learn about. In his book Manoilescu identified an important exception to the conclusions derived from trade models based on the customary assumption of perfectly competitive markets that underlay the policy of free trade supported by the vast majority of economists. Manoilescu postulated instead an economy where the wage level is higher in its manufacturing than its agricultural sector, as was true of his native Romania and other developing countries. He noted that an economy with a comparative advantage in manufacturing, as shown by the fact that the marginal value product of labor is higher in

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manufacturing than in agriculture, would then find that it could not compete in world markets with countries having uniform wage rates, unless its manufacturing sector was protected by tariffs. Under free trade, since it exchanges agricultural products for manufactured ones, the country is subject to what Manoilescu called “unequal exchange”, importing commodities with a much smaller labor content than that embodied in its exports. The provocative title of Manoilescu’s book on a “theory of protection” underlined his claim to have discovered an intellectually sound case against free trade in specific circumstances.

Economists of Ricardian persuasion such as Jacob Viner, and other economists critical of the classical school such as Bertil Ohlin, reviewed Manoilescu’s book in mostly negative terms.¹ The neoclassical economist Gottfried Haberler saw some merit in its central thesis, but believed that protection was not the best policy response to the market imperfection that Manoilescu identified.² It was not until 1958, many years after Manoilescu’s untimely death in 1950, that Everett Hagen constructed a neoclassical trade model based on Manoilescu’s central assumption of a market imperfection or distortion in intersectoral wages, and showed that protection, while not the best policy response to it, can yield an outcome that is superior to free trade.³ An important methodological difference between Hagen’s article and Manoilescu’s book is that Hagen used a two-sector neoclassical trade model of the type that Paul Samuelson had popularized as the mainstream trade model, using it to elucidate the Heckscher–Ohlin theory of trade, whereas Manoilescu’s book was filled with tortuous arithmetical examples where labor was the sole factor of production.

Thanks to Hagen’s article, it became apparent to the profession that Manoilescu had discovered the first case of what economists now refer to as “market distortions”, whose presence can indeed overturn the traditional conclusions of trade theory that, with monotonous regularity, had prescribed free trade as the best policy on the grounds of economic welfare. Other trade economists followed Hagen’s lead and examined other types of distortion in both product and factor markets, and the policies best suited to offset them.⁴ One important consequence of this literature was that it brought home to economists the important distinction between the policies of *laissez faire* and free trade. The cure of market distortions required the implementation of first-best policies such as subsidies or taxes, on either products or factors of production. While inconsistent with *laissez faire*, these policies needed to be accompanied by free trade in order to reach an *optimum optimorum*. The protection advocated by Manoilescu was indeed superior to free trade in welfare terms, as he had maintained, but represented a second-best policy when compared to the first-best policy of a wage subsidy to labor in manufacturing combined with free trade.

Of course, Manoilescu was not the first intellectual to advocate protection in order to promote industrialization, being preceded in this by the American Alexander Hamilton (1791), the Scot John Rae (1834) and the German Friedrich List (1841) among others.⁵ The best known of these writers is List, who caught the public imagination and that of policy makers in Europe and elsewhere, and led them to adopt his recommended policy of temporary protection. While Manoilescu cites him as a precursor, he takes pains to stress that his own case for protectionism differs from List’s. The latter postulated that protection was a temporary expedient akin to that related to the infant industry case. When the infant industry has grown up, protection can and should be removed in favor of free trade. In Manoilescu’s case, protection must be permanent as long as wages in manufacturing

exceed those in agriculture. In other respects, the two authors had similar ideas regarding the importance of “productive forces” for economic development. This expression, an intriguing key to List’s thinking as was stressed by Schumpeter,⁶ appears in the title of the German translation of Manoilescu’s book being celebrated today: *Die nationalen Produktivkräfte und der Aussenhandel*. Both List and Manoilescu followed the classical tradition of emphasizing the intimate connection between international trade and economic development, so that the latter appears as one of the main “gains from trade”, rather than the static neoclassical gains portrayed in present-day textbooks of international trade.

As Professor Ioan Talpos noted in his announcement of the opening session of this Conference, Manoilescu coined a new concept which he called “quality factor coefficient” and can be considered to be a forerunner of the modern concept of total factor productivity. “The coefficient of quality [Q] was equal to average net production of an industry [P] ... divided by the square root of the product of the number of workers [A] times the amount of fixed capital [C], or $Q = P/(AHC)$ ”. If land [O] used in agriculture is also included as a factor, this formula can be amended “by replacing the square root of AHC by the cube root of AHCHO”.⁷ The square root of AHC and the cubic root of AHCHO can be regarded as Cobb-Douglas production functions with factor exponents equal to $\frac{1}{2}$ and $\frac{1}{3}$ respectively. The division of total output P by this square root or cubic root then yields precisely total factor productivity (TFP) if the production function takes the Cobb-Douglas form and all factors receive the same share of income (admittedly, these are very strong assumptions). Just as economists now attribute a large share of the growth of national income to the growth of TFP, and the differences in the standards of living of different countries to their different levels of TFP, Manoilescu in his book associated potential comparative advantage with those sectors having a high TFP, which he located in manufacturing rather than agriculture.

Although he subsequently revised his 1929 book and saw it translated into several languages including Romanian, it is unfortunate that Manoilescu did not follow up this innovative work with further research on economic growth and international trade. This note ends on a more somber note. Both before and after he wrote his 1929 book, Manoilescu’s interests turned in a political and sociological direction and led him to write books on “neoliberalism”, and then on fascism and the corporative state. He saw corporatism as the paradigmatic political structure for the twentieth century, taking over from the liberalism of the nineteenth century. He was thus attracted to the fascist or semi-fascist regimes that were being set up or consolidated in Italy, Portugal, Spain, Germany, Brazil and elsewhere, and traveled to some of these countries to expound his own theories on corporatism. His marked pro-corporatist and pro-fascist sympathies had the unfortunate consequence of discrediting his economic views in the eyes of the economics profession, particularly after the end of World War Two. Manoilescu even re-interpreted some key findings of his 1929 book on protectionism to make them consistent with his recently acquired corporatist views. Thus, toward the end of his 1934 book *Le siècle du corporatisme: doctrine du corporatisme intégral et pur*, he stated:

Profit is an individualist notion. Productivity, which we personally made the basis of our protectionist theory and the international exchange just cited, is a corporatist notion. The export of commodities of low productivity, such as wheat, is a negative operation from the national point of view, and hence an anti-corporatist operation.

The corporatist organization of a nation forces us, therefore, to direct production and foreign trade toward articles that allow us to acquire the greatest possible amount of work from abroad, with the least possible work of our own nation⁸.

It is also surprising that Manoilescu became an advocate of Romania's participation in the German-sponsored *Grossraumwirtschaft* or Greater Economic Space, in which his country abandoned the protectionism that he had supported in his 1929 book in favor of becoming a supplier of primary goods to the Third Reich⁹. Did Manoilescu suddenly see merit in Romania's participation in a customs union under German leadership? This is unlikely since the theory of customs unions emerged only in 1950 with Jacob Viner's book *The Customs Union Issue*. More probably Manoilescu's political leanings led him to abandon his long-held economic views, adversely affecting Romania's gains from international trade and in fact forcing the country to become a cog in the German war machine.

Endnotes

1. The best-known reviews were Jacob Viner, "Mihail Manoilescu on the Theory of Protection", *Journal of Political Economy* (40:1), 1932, 121-5; and Bertil Ohlin, "Protection and Non-Competing Groups", *Weltwirtschaftliches Archiv* (33:1), 1933, 30-45.
2. Gottfried Haberler, *The Theory of International Trade* (1936).
3. Everett E. Hagen, "An Economic Justification of Protectionism", *Quarterly Journal of Economics* (72:4), 1958, 496-514.
4. These are admirably set out in Jagdish Bhagwati, "The Generalized Theory of Distortions and Welfare", in J. N. Bhagwati et al. (eds), *Trade, Balance of Payments, and Growth: Papers in International Economics in Honor of Charles P. Kindleberger*, Amsterdam: North-Holland, 1971, 69-90.
5. Alexander Hamilton, "Report on the Subject of Manufactures" (1791), in Syrett, H. C. et al., *The Papers of Alexander Hamilton*, Vol. X, New York: Columbia University Press, 1966; John Rae, *Statement of Some New Principles on the Subject of Political Economy, Exposing the Fallacies of the System of Free Trade, and of Some Other Doctrines Maintained in the "Wealth of Nations"*, Boston: Hilliard, Gray, and Co., 1834; Friedrich List (1841), *The National System of Political Economy*, trans. S. S. Lloyd, London: Longmans, Green, and Co., 1885. On the nationalist trade policies advocated by these authors, see my book *Comparative Advantage in International Trade: A Historical Perspective*, Cheltenham: Edward Elgar, 1998, chapter 5.
6. Joseph A. Schumpeter, *History of Economic Analysis*, New York: Oxford University Press, 1954, 505.
7. As reported in Joseph L. Love, *Crafting the Third World: Theorizing Underdevelopment in Rumania and Brazil*, Stanford: Stanford University Press, 1996, 253.
8. I have translated this passage from the Portuguese language translation of Manoilescu's 1934 book titled *O Século do corporativismo: doutrina do corporativismo integral e puro*, Rio de Janeiro: Livraria José Olympio, 1938, 280-1.
9. See on this the excellent book by Joseph L. Love mentioned in endnote 7, whose chapters 5 to 7 are primarily devoted to Manoilescu's life and writings.