FREEDOM TO TRADE, FREE TRADE AND LAISSEZ-FAIRE: ECONOMIC LIBERALISM IN 19TH CENTURY LATIN AMERICA

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(A). INTRODUCTION

Liberalism in Europe had many dimensions, one of which – especially in the United Kingdom – was the degree to which the market should guide all economic decisions. In Adam Smith's Wealth of Nations, the 'hidden hand' of the market was seen as leading to a big improvement in welfare when compared with the myriad rules and regulations imposed by central governments on their citizens. When David Ricardo developed the Law of Comparative Advantage in his Principles of Political Economy and Taxation, it became a rallying cry for liberals of all persuasions. The end of the tariff on basic grains in 1846, better known as the abolition of the Corn Laws, was considered a major achievement of liberalism in Great Britain and a model for liberals elsewhere.

It might have been expected therefore that liberalism in Latin America would have paid equal attention to trade policy, the end of state monopolies and the promotion of competition. Smith and Ricardo were well known in Latin America and their works were widely read. However, liberalism in 19th century Latin America focused primarily on relations between Church and State, the degree of personal freedom from state interference and the constitutional arrangements between central and local governments. The arguments for economic liberalism were much less compelling in Latin America. Indeed, Liberals in power were often less 'liberal' than their Conservative opponents.

There were many reasons for this, but the most important were the limitations imposed on economic policy by the demands of state finance, the behavior of trade partners and the difficulty of finding fiscal alternatives to tariff revenues. Thus, unrestricted free trade was seen as a distant goal by all but the most ideologically committed liberals and economic policy focused on much more limited objectives.

The first of these was 'freedom to trade', meaning the right to trade with any partner in the world even on unequal terms. Once that was achieved, the goal became an international trade that was exempt from discriminatory policies by the partner country rather than subject to zero or low tariff rates in Latin America. This was 'free trade' Latin American style and it had been largely achieved by the second half of the 19th century with a large degree of consensus among all members of the political elite.

What remained was a series of arguments about the markets for labour, land and capital where there were genuine differences among the elites and where Latin American liberalism partially found a voice. This was not *laissez-faire* in the classic sense, but a debate about the degree of state interference in the factor markets to maximize the opportunities for economic growth and development. Not surprisingly, disputes rarely crystallized neatly along party lines so that Latin American liberals could be found on occasions arguing for policies that would have puzzled economic liberals in Europe.

(B). FREEDOM TO TRADE

The system against which 'freedom to trade' struggled was mercantilism. In addition to its well-known features of maximizing the trade surplus of the country concerned in order to accumulate *specie* (gold and silver), mercantilism when exercised by imperial countries such as Portugal and Spain limited the number of ports that could be used, imposed numerous restrictions on intra-colonial trade and prohibited the use of foreign ships. In those rare instances when trade with foreign countries was permitted, discriminatory tariffs were applied to prevent it reaching significant proportions.

The mercantilist system applied by Portugal and Spain to its colonies in the Americas faced numerous challenges even before the publication in 1776 of Adam Smith's Wealth of Nations. One was the impact of imperial wars, which meant that the colonies could face extreme shortages at times of conflict; another was natural disasters, which could necessitate a more urgent response to essential needs than that permitted under the colonial trading system; a third was the contraband trade, which became ever more profitable as additional restrictions were added to the mercantilist system.

The occupation of Havana by the British in 1762 had emphasized the contradictions of the mercantilist system, while creating a constituency in Cuba that had tasted the fruits of enlarged trading possibilities. The following year the Dutch had thrown open some of their ports in the Caribbean to the ships of all nations (provided, of course, they were not at war with the Netherlands) and this raised the prospect for the Spanish of an increase in the contraband trade. When this Free Port system was adopted by the British for the islands of Jamaica and Dominica, a Spanish response became a matter of urgency.

This duly happened in 1778, although the rules for the Spanish Caribbean islands had been relaxed even earlier. In that momentous year, the Bourbon Spanish Emperor Charles III passed the *Reglamento para el comercio libre* allowing a greater number of ports on both sides of the Atlantic to participate in the imperial trade that had previously been channeled almost exclusively through Cádiz on the Iberian side and three ports on the American side. These Bourbon reforms did not at first extend to Venezuela or New Spain, but these restrictions were lifted in 1788 and 1789 respectively.

Of course, Charles III did not mean to apply 'free trade' or even 'freedom to trade'. Indeed, his main concerns were to reduce contraband, increase tax revenue and ensure that a greater proportion of intra-imperial trade should consist of Spanish goods. In this he was largely successful, as we shall see, but in a good example of the law of unintended consequences the *Reglamento* unleashed a series of changes that would eventually lead to 'freedom to trade' for the countries of Spanish America.

The Portuguese response was at first less supportive of 'free trade' . Indeed, the reforms enacted by the Marquis of Pombal in the 1750s created new trading monopoly companies. However, by the 1760s policy in Portugal was taking a similar turn to that in Spain. The last state-organised fleets sailed from Portugal to Brazil in 1766 and thereafter properly licensed ships were free to sail whenever they pleased to Salvador and Rio de Janeiro. When the Pombaline monopoly companies were disbanded after the minister's fall from power, ships from Portugal were free to enter any Brazilian port. This change made it possible for merchant navy ships to make two trips a year to Brazil with a big impact on imperial trade.

What the Pombaline and subsequent reforms could NOT do was stop the contraband trade along Brazil's vast coastline. British ships in particular were particularly brazen about visiting Brazil without permission with about a dozen arriving each year in the 1780s. Furthermore, British captains were quick to take advantage of the loophole under which a distressed vessel (*arribada*) could put into port. In Rio de Janeiro, for example, the number of *arribadas* increased from eight in 1791 to 30 in 1800 and it is unlikely that weather conditions alone accounted for the increase.

Both sets of reforms – Bourbon and Pombaline – had the intended effect of increasing not only trade itself, but also the proportion of exports to the Americas from peninsular sources. In the case of Spain, for example, this went from 38 per cent in 1778 to 57 per cent in 1796. This, of course, was anathema to anyone who **really** believed in free trade, since the increase was due to the opening of new ports rather than the application of the Ricardian law of comparative advantage. However, 1796 would mark the end of this particular phase of Spanish imperial trade, as it was also the year in which Britain and Spain went to war with disastrous consequences for Spain. Its fleet was largely destroyed off Cape St. Vincent the following year and Spain was in no position to supply the colonies with their essential needs – yet alone the luxury goods for which they had begun to acquire a taste.

The situation was now so desperate that colonial administrators were forced to take matters into their own hands. The *intendente* in Cuba, for example, gave permission to slave trading ships entering Havana to depart with whatever Cuban exports they could buy. The Spanish crown therefore bowed to the inevitable and permitted the colonies in the Americas to trade with ships of neutral countries provided that the ships sailed to Spain with their cargoes before returning to their home ports. Britain, being at war with Spain and therefore not neutral, could not take advantage of this. However, US ships could although they had no intention of sailing to Spain before returning to US ports and Spain had no means of enforcing it.

The extension of trade to neutral ships was an important step in the march towards 'freedom to trade'. Indeed, that is one reason why it was revoked two years later by the Spanish crown. Efforts to enforce the prohibition were hugely unpopular and, after Spain was invaded by Napoleonic forces and Charles IV abdicated in 1808, utterly ineffective. Once again local officials took matters into their own hands, the most famous being the Viceroy of Buenos Aires in 1809 who gave permission for foreign ships, including British, to enter the Río de la Plata.

The Napoleonic invasion forced the Portuguese court to take refuge in Brazil. This had the support of the British, who extracted in return the right of freedom to trade for all allied and neutral countries. Within a matter of months the foreign trade of Brazil was largely in the hands of British merchants, who used Brazil as a platform from which to penetrate other South American markets – especially the ports of Buenos Aires and Montevideo.

When the Napoleonic forces were ousted from the Iberian peninsula, it made no difference to the 'freedom to trade' of Brazil which was now largely in British hands. However, when Ferdinand VII ascended the Spanish throne, it was inevitable that an attempt would be made by the imperial power to reverse the advance of 'freedom to trade' by restricting the access of neutral ships to its ports in the Americas.

Once again, however, there was little the Spanish government could do to enforce it and this time the colonists had either declared independence or were in no mood to obey. The

Captain-General of Cuba, for example, refused to implement the order banning foreign ships and by 1818 the Crown was obliged to open Cuban ports to unrestricted trade. Local officials in Central America and other parts of the Americas then did the same. Finally, in March 1824, Ferdinand VII promised genuine 'freedom to trade', but by this time Spanish authority in the Americas had been reduced to a small part of Peru together with the islands of Cuba and Puerto Rico.

When the fighting ended, therefore, all independent countries - Brazil as well as the former Spanish colonies – started with 'freedom to trade'. So, however, did the remaining Spanish colonies – Cuba and Puerto Rico. And the ports of Santo Domingo, occupied by Haiti in 1822, also enjoyed the same 'freedom to trade' as the ports in the western half of Hispaniola. All countries could now import from the cheapest source and export to wherever they wanted. This was not, however, 'free trade' as both imports, and even more exports, were subject to all sorts of discrimination by partner countries in addition to the high tariffs and export duties applied by Latin American countries.

Freedom to trade brought all sorts of new trade partners into the Latin American sphere. And after recognition of the independent states, it brought back the old partners as well – Spain for most, Portugal for Brazil and France for Haiti. However, with only a few exceptions the new partners would prove to be more important in the long-run. The old partners, with the partial exception of France in Haiti, could not provide the imports now required nor the market for the new or indeed traditional exports.

Of the new partners, by far the most important was the United Kingdom. Although British merchants had oversupplied the South American markets in particular after 1808, trade soon settled down to more sustainable levels. Britain would face a challenge in foodstuffs and lumber from the United States, in porcelain and other fine good from France and in a range of quality manufactured goods from the German states. However, British dominance lasted for some years. In 1842, for example, the UK was still responsible for half of all Brazilian imports with France and the US a distant second and third respectively. And the UK was still taking nearly 30 per cent of Brazilian exports in that year despite its low demand for coffee and preference for colonial sugar. Britain was equally dominant in the rest of South America. In Central America, Cuba, Haiti, Mexico and Puerto Rico, however, the UK faced a serious challenge from the United States even before 1850.

(C). Free Trade

Before 'freedom to trade' could become 'free trade' for Latin America, a series of obstacles had to be overcome. Some of these had been put in place by Latin America's trade partners and would not be fully removed even by the time of the First World War. Others had been inherited by the newly independent states from Portugal and Spain and in a few cases were made worse by post-colonial governments. The march to 'free trade' was a long one with many a bump along the road.

The first set of obstacles was the desire of the partners to have special trade privileges that did not apply to others. Since recognition of independence was eagerly sought, the temptation for some of the partners to demand such privileges in return was irresistible. And, as always in trade policy, a bilateral trade deficit with a Latin American country would be seen as an opportunity by the partner to extract trade concessions. Although in a formal sense Latin American states agreed to these measures, it could not be denied that they drove a wedge through the principles of free trade since the cheapest source of imports was often excluded from the market by discriminatory tariffs.

Unsurprisingly, given its dominant position, it was the UK that was the first to exploit the opportunities for trade discrimination. Following the transfer of the Portuguese Court to Brazil, a Treaty of Navigation and Commerce was signed with Great Britain in 1810 that fixed a maximum tariff on British goods of 15 per cent but without reciprocity; this was the same rate as that paid by Portuguese goods entering the Brazilian market, but much lower than those of other friendly nations. This unequal treaty should have lapsed on Brazilian independence in 1822, but Britain succeeded in replacing it in 1827 with an Anglo-Brazilian commercial treaty confirming the maximum tariff for British goods of 15 per cent – again without reciprocity. Brazil did what it could to limit the trade distorting impact by lowering tariffs on all imports in 1828 to a maximum of 15 per cent, but this had the undesirable side-effect of undermining protection for Brazilian industry. The treaty with Britain was finally ended in 1844.

Great Britain did the same in Haiti in 1814, but this time without even recognizing Haitian independence. At the time Haiti was divided in two – a Kingdom in the north ruled by Henri Christophe and a Republic in the south ruled by Pétion. The latter had imposed a tariff of 10 per cent and Britain was able to obtain a 50 per cent reduction, but – as in the case of Brazil – without reciprocity. When Boyer united Haiti in 1820, he pressed again for British recognition. The UK, however, still refused to accept an independent Haiti on the specious grounds that it could not do so ahead of France, ignoring the fact that it had recognized the independence of the Latin American republics without waiting for Spain – the former colonial power - to do so. This so enraged President Boyer that he cancelled the trade privileges granted to the UK in 1826.

France and Portugal, as former colonial powers, also wanted trade privileges. Portugal was too weak to extract them from Brazil, but France was able to obtain them in Haiti in 1825 following recognition of Haitian independence. She did not, however, provide reciprocity. French privileges extended to the export duties, not just import tariffs, applied by Haiti to its main exports. As a growing number of ships starting calling at Haitian ports flying the French flag, the revenue fell. Boyer wisely cancelled the French trade privileges in 1828. There would be no reciprocal Franco-Haitian trade treaty until 1904 despite the fact that most Haitian exports went to France.

Spain, having little to offer by way of manufactured goods, could do nothing to extract trade privileges in its former colonies. In the Caribbean, however, it was a different matter and a four-fold tariff system imposed on Cuba and Puerto Rico ensured the lowest tariff on Spanish goods in Spanish ships and the highest on foreign goods in foreign ships. This trade discrimination meant that the two remaining colonies were obliged to import many essential goods, especially flour, from Spain despite the fact that other countries, especially the United States, could have supplied them much more cheaply.

Spanish trade privileges in its Caribbean colonies came to an end in 1892, but this had nothing to do with a Spanish commitment to free trade. Instead, it was due to the growing diplomatic power of the United States. The US had signed Treaties of Commerce and Navigation with most Latin American republics following independence (the main exception was Haiti where recognition was delayed until 1862), but the US had not sought or obtained trade privileges. Instead, she had sought Most Favoured Nation (MFN) status, a position with which the UK was also comfortable after the ending of trade privileges in Brazil.

This position lasted until the US Civil War. However, subsequent administrations were much more aggressive in trade policy, raising tariffs sharply on imports and seeking to use the growing economic power of the US to extract trade privileges. This came to a head in 1889 when Secretary of State James Blaine used the meeting in Washington DC that would launch the Pan-American Union to call for a Customs Union in the Americas. This initiative was rebuffed by the Latin American republics present, but the McKinley tariff the following year gave the US a new weapon. The president was now entitled to impose additional tariffs on imports from those countries not agreeing to reciprocal trade concessions.

Within two years, the Dominican Republic, Spain on behalf of Cuba and Puerto Rico and the UK on behalf of many of its Caribbean colonies had agreed to slash the tariff on US imports. In the Caribbean only Haiti resisted and was punished with additional taxes. And the United States insisted that Cuba after independence in 1902 should sign a reciprocal trade treaty giving the US reductions on all imports in return for concessions on Cuban sugar and tobacco exports.

Another obstacle in the path of free trade was the commercial policy of the European imperial powers. For Latin America the most important of these were the UK and France. At the time of independence both countries had in place systems of imperial preference that gave preference to colonies over foreign countries. This was an obstacle for Latin American exporters of raw sugar, wool, coffee and spices. Only cotton imports into Britain were exempt as the duty was zero. In addition, all European countries – not just the imperial ones – operated cascading tariffs designed to protect their own industries by applying higher tariffs on processed imports such as refined sugar.

The UK struggled with tariff reform for many years, briefly – in 1844 – imposing an additional tariff on slave-grown sugar from countries such as Brazil and Cuba. However, in 1846 the Corn Laws were abolished and an eight-year period began in which imperial preference was phased out and many tariffs, such as that on raw sugar, were reduced to zero. This was good news for those Latin American countries exporting those commodities most affected, although the duty on refined sugar would remain until 1874. At that point, the UK came close to duty-free trade, although import tariffs and excise duties were still collected on a small number of goods – especially wines and spirits. This 'golden-age' of British free trade would last until the First World War when imperial preference was again introduced with negative consequences for many Latin American exporters.

France followed a different path, combining imperial preference with outright prohibition on many goods that competed with French production. The system was significantly relaxed in 1860 in the Anglo-French commercial treaty of that year, but imperial preference remained. This meant, of course, that Latin American exporters of products that competed with colonial exports faced discrimination in the French market. This discrimination never ended and, indeed, became worse as the 19th century advanced for two reasons. First, the French empire expanded rapidly in Africa and Asia, bringing new sources of supply against which Latin America had to compete on unequal terms, and secondly tariff reform in 1891 reversed the tendency towards liberalization that had taken place after 1860.

A customs union (*zollverein*) among the German states had begun shortly after most Latin American states became independent. However, the common external tariff was modest so that the implied discrimination against Latin American exports was small. The low tariffs were in part designed to discourage protectionist Austria-Hungary from joining, but her defeat by Prussia in 1865 removed the need to keep import duties at moderate levels. Thus, following German unification in 1871 the tariffs moved up sharply with a damaging effect on certain commodities exported from Latin America such as leaf tobacco and cigars.

Under these circumstances, it is not surprising that Latin American governments were under no pressure to abolish or reduce import tariffs themselves. Their main trade partners – France, Germany, UK and US – all made extensive use of tariffs before 1850. Even after the end of imperial preference in Britain, cascading tariffs were still widely used to protect parts of British industry such as refined sugar. And less important trade partners, such as Austria-Hungary, Italy, the Ottoman Empire and Russia never had any doubts about the wisdom of protective tariffs.

There was an additional reason why Latin American states remained committed to taxes on trade. Independence had disrupted colonial fiscal systems and led to the end of various income streams. Taxes on trade – imports and exports – were an obvious target with tariffs designed to generate revenue. If such tariffs could also provide a protective function, so much the better. If some tariff rates never reached the astronomical levels in Russia or the United States, this had less to do with the arguments against high tariffs by the handful of Latin American intellectuals in favour of trade liberalization and had much more to do with the need to keep tariffs at a level that maximized revenue. High tariffs designed for protection, of course, often generate zero revenue as all imports are excluded.

Tariffs inherited from colonial Portugal and Spain were relatively low. These were then raised quickly. By mid-19th century, after the end of the commercial treaty with Great Britain, the average tariff rate in Brazil – measured by the ratio of import duties to imports – was nearly 30 per cent. It was the same in Colombia. In Buenos Aires Province in the United Provinces of Río de la Plata, virtually an independent country at the time, the average tariff rate was 31 per cent in 1836. In Mexico in the 1840s it had already risen to 45 per cent. By contrast, in supposedly protectionist France, the average tariff rate fell from 17.2 per cent in 1846-50 to 13.2 per cent in 1851-5. In Latin America only Peru, bolstered by revenue from guano exports after 1852, was able to lower tariffs significantly.

These high tariff rates could be explained by the exigencies of the post-colonial fiscal crisis and in some cases the demands of war and civil strife. Yet, as Coatsworth and Williamson have shown, they did not come down as more normal conditions prevailed. Tariff rates crept up after 1865 and, by the 1890s, were even higher than those in the United States if unweighted averages are used.

Tariff rates averaged 30 per cent in the last decade of the 19th century. There was even a protectionist element in these tariffs, as governments became more sensitive to the need to promote local industry against competition from imports. Yet this was in fact as close as Latin America would come to 'free trade', although some federal countries such as Brazil still applied inter-state tariffs at this time. By the end of the First World War, tariff rates would rise again and in the 1930s would be joined by a formidable arsenal of non-tariff barriers to keep out imports.

(D). Laissez-faire

International trade policy was not, of course, the only issue with which economic liberalism had to grapple. There were many others. The most difficult ones can be conveniently be grouped around the three factor markets: labour, land and capital. Other policy issues, such as the dismantling of state monopolies inherited from the colonial period, were less controversial.

Latin America in the 19th century suffered from a scarcity of labour, meaning that the demand for labour exceeded the supply at the prevailing wage rate. Resolving this disequilibrium through an increase in wage rates was regarded by all members of the elite as anathema since it was thought it would lead to a major loss of competitiveness. Thus, policy placed an emphasis on increasing supply.

In all countries, but especially Brazil and Cuba, slaves formed part of the labour supply at the end of the Napoleonic Wars. Among the slave populations death rates almost invariably exceeded birth rates, so that the slave population could only be maintained through the slave trade. This had been abolished first by Denmark from 1803, then by the United States from 1808 and by Britain a few weeks later. British pressure was then applied to Holland and Sweden, two other imperial powers in the Americas, to end the trade from 1814.

British pressure was also applied to France, Portugal and Spain, but their resistance was great. It was not until the 1830s that France made any serious effort to stop the trade and Spain only started to do so in the 1840s. Portugal did the same, but by now Brazil was independent and resisted fiercely all British efforts to curtail the slave trade until the 1850s. At that point the trade was outlawed throughout the Americas, although an illegal trade to Cuba continued until 1873.

The independent Spanish American countries had no means of continuing the slave trade even if they had wanted to. Furthermore, many states passed laws freeing the children of slaves. Thus, it was inevitable that slavery itself would eventually come to an end. However, emancipation in Latin America was a long-drawn out affair as Liberals as well as Conservatives agonized over the implications for labour supply. The United Provinces of Central America in 1824 were the first, closely followed by Mexico in 1829. Other countries followed suit, the last being Puerto Rico in 1873, Cuba in 1880 and Brazil in 1888. Generally, slavery lasted longer the greater the proportion of slaves in the working population, suggesting that humanitarian considerations were not the crucial factor in emancipation.

With slavery ending, the scarcity of labour became more acute. Coercion therefore continued to be used by the state, although this time without slavery. The policy options included debt peonage, indentured labour and anti-vagrancy laws. All these policies, while deeply illiberal, were implemented by supposedly Liberal governments as well as their Conservative opponents. No contradiction was seen between Liberalism as a political philosophy and labour market coercion as a policy tool. It was only towards the end of the century when free inward migration on a large-scale became realistic that Liberalism and economic policy could be more closely aligned. And even then Liberals saw no contradiction between their belief in the free market and the use of state subsidies to promote immigration.

The market for land was also problematic for economic liberalism. With an abundance of land, Latin American governments were concerned with two things: first, turning existing landholdings to more productive uses and, secondly, ensuring that the mass of the population could not withdraw from the labor force by retreating into subsistence farming.

Liberals had no problem with the alienation of Church land, as it could be argued that it was now not only more productive but had increased the power of the state against the ecclesiastical authorities. Communal land, important in those countries with a large indigenous population, was another matter altogether. The transfer of such lands to private ownership was pursued vigorously by Liberals despite the apparent contradiction with personal freedoms. However, for Liberals the need to secure a labour force for the expanding export sectors became an issue that overrode all other considerations. The alienation of communal land served Liberal aims well, as it expanded private landholdings in productive areas, ensured an increase in labour supply and generated tax revenues through the increase in international trade.

The remaining factor market, capital, was less contentious. Almost all members of the elite shared a conviction that foreign capital – both direct and portfolio – was a necessary condition for the growth and development of the region. Only in Haiti did the elite reject this assumption. Frequent debt crises, starting in the 1820s, made it difficult to attract foreign capital, but the conviction that it was needed remained. When Liberals came to power, they were among the most assiduous in courting foreign investment even if this meant providing a guaranteed rate of return on capital.

The extreme version of this Liberal faith in foreign capital was provided by Porfirio Díaz in Mexico. In the decades before the *Porfiriato*, Mexico had experienced a series of disastrous investments by local capitalists in key infrastructure projects that never came to fruition. Only foreign capitalists, such as Weetman Pearson, were now seen as capable of delivering successful outcomes. The científicos around Díaz, especially José Limantour, were quite capable of driving a shrewd bargain with foreign capitalists, but they never wavered in their belief that only foreign investment could rescue Mexico from decades of under-performance. Much the same was true of Central America, the Dominican Republic and many South American states.

By the end of the 19th century, economic liberalism had succeeded in many of its aims. The export sector was expanding rapidly, producing commodities needed by the industrialized countries of Europe and North America. Tax revenues were booming, aided by the rise in imports made possible by export expansion. Public spending on issues close to Liberal hearts, such as education, was also on the rise. Yet it had taken a long time for this virtuous circle to come into place. And within a few years of the new century starting, it would be broken first by the Great War and then by the Great Depression.