

Friedrich List's Critique of the Methuen Treaty

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Abstract. This article examines Friedrich List's critique of the Methuen Treaty. The Methuen Treaty removed all restrictions on English wool entering Portugal and reaffirmed England's commitment to import Portuguese wines at two-thirds the tariffs of French wines. Friedrich List argues that the agreement hurt Portugal's textile industry and slowed Portugal's economic growth. List's critique of the Methuen Treaty is a strong representation of his resistance to Adam Smith and Jean-Baptiste Say, but it is isolated from his robust theoretical framework. One possible explanation for the discontinuity is that the knowledge problem undermines List's theory. The lack of local data makes it difficult to conduct an accurate and straightforward policy analysis of the Methuen Treaty, making the analysis vulnerable to normative interpretations. Specifically, List's disagreement with Adam Smith's cosmopolitanism pushed him further away from a straightforward application of his theory.

Keywords: Adam Smith; Agriculture; England; Friedrich List; Industrialization; Portugal; Wine.

[es] La crítica de Friedrich List al Tratado de Methuen

Resumen. Este artículo examina la crítica de Friedrich List al Tratado de Methuen. El Tratado de Methuen eliminó todas las restricciones a la entrada de lana inglesa en Portugal y reafirmó el compromiso de Inglaterra de importar vinos portugueses a dos tercios de los aranceles de los vinos franceses. Friedrich List argumenta que el acuerdo dañó la industria textil de Portugal y desaceleró el crecimiento económico de Portugal. La crítica de List al Tratado de Methuen es una representación fuerte de su resistencia a Adam Smith y Jean-Baptiste Say, pero está aislada de su sólido marco teórico. Una explicación posible de la discontinuidad es que el problema del conocimiento socava la teoría de List. La falta de datos locales dificulta la realización de un análisis de políticas preciso y directo del Tratado de Methuen, lo que hace que el análisis sea vulnerable a interpretaciones normativas. Específicamente, el desacuerdo de List con el cosmopolitismo de Adam Smith lo alejó aún más de una aplicación directa de su teoría.

Términos clave: Adam Smith; agricultura; Inglaterra; Friedrich List; industrialización; Portugal; vino.

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Resumo. Este artigo examina a crítica de Friedrich List ao Tratado de Methuen. O Tratado de Methuen eliminou todas as restrições à entrada de lã inglesa em Portugal e reafirmou o compromisso da Inglaterra de importar vinhos portugueses a dois terços das tarifas dos vinhos franceses. Friedrich List argumenta que o acordo prejudicou a indústria têxtil portuguesa e desacelerou o crescimento econômico de Portugal. A crítica de List ao Tratado de Methuen é uma representação forte de sua redsistência a Adam Smith e Jean-Baptiste Say, mas está isolada de sua robusta contribuição teórico. Uma explicação possível para a descontinuidade é que o problema do conhecimento enfraquece a teoria de List. A falta de dados locais dificulta a realização de uma análise política precisa e direta do Tratado de Methuen, tornando a análise vulnerável a interpretações normativas. Especificamente, o desacordo de List com o cosmopolitismo de Adam Smith o afastou ainda mais de uma aplicação direta de sua teoria.

Palavras-chave: Adam Smith; agricultura; Inglaterra; Friedrich List; industrialização; Portugal; vinho.

JEL Codes: B12; B17, B41.

Sumario. 1. Introducción. 2. List's political economy. 3. The Friedrich List problem. 4. The origins of the inconsistency. 5. Conclusion

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1. Introduction

In December of 1703, Great Britain and Portugal ratified a commercial agreement known as the Methuen Treaty (Pellechia 2006) or the Port Wine Treaty. This commercial treaty removed all restrictions on the import of English woollens to Portugal, and it ratified the English commitment to importing Portuguese wine at a third less tariffs than French wines (Sodré 1965; Smith 1776). The objective of this article is to analyze Friedrich List's theory of economic development and his critique of the Methuen Treaty found in his book *The National System of Political Economy*, exploring the gap between his vast theoretical contribution and his analysis of the agreement.

The Methuen Treaty was established under controversy, as the Portuguese people questioned the deal's participants' honesty (Anderson 2014; Costa et al. 2016; Sodré 1965). The Marquis de Alegrete represented the Portuguese government during the Methuen Treaty negotiations. The citizens questioned his integrity when he bought a palace right after the trade agreement's ratification. Luís da Cunha, the Envoy Extraordinary of Portuguese Cortes to London (Silva 2003), heavily scrutinized the agreement and believed that it would negatively impact the local industry (Sodré 1965).

The tumultuous environment was fertile for different historical narratives and academic discourse. This included two important thinkers that polarized the debate on the true consequences of the Port Wine Treaty. Adam Smith was skeptical about the agreement's benefits to Britain, claiming that it was "evidently advantageous to Portugal, and disadvantageous to Great Britain" (Smith 1776, 421). On the other side of the argument was Friedrich List, a German economist and one of the early advocates for the protection of young industries (Schumpeter 1963; Viner 2016), who argued that the agreement led to the "sudden and complete ruin of the Portuguese manufactures" (List 1856, 132).

In his work *Das Nationale System der Politischen Oekonomie*, originally published in 1841 and translated into English in 1856 and 1885, List reacts to Adam Smith's position on the Methuen Treaty as well as Smith's stance on free trade. List's rebuke became a mainstream thought in the Lusophone literature. The famous Brazilian economist Celso Furtado agrees with this position, claiming that the Methuen Treaty created deep negative consequences to Portugal's manufacturing sector (Furtado 2020).

Although modern research suggests that the Methuen Treaty had no significant impact on Portugal's late industrialization (Cardoso 2017; Cardoso 2019), some history textbooks continue to follow List's perspective, claiming that "the terms of the Treaty of Methuen, signed in 1703 with the English and known as the Treaty of Cloth and Wine, made industrial development in Portuguese territory unfeasible by forcing Portugal to import manufactured products from England" (qtd. in Menezes and da Costa 2012, 200).

Although there is a robust literature analyzing the Methuen Treaty and a robust literature on List's political economy, no work has yet intensively studied List's critique of the Methuen Treaty. This paper aims to bridge these two literatures by analyzing List's position on the Methuen Treaty, extending his thoughts on the economic agreement to the theoretical framework presented in his *magnum opus*, *Das Nationale System der Politischen Oekonomie*. As Boianovsky (2013) points out, the 1885 English version of the *National System of Political Economy* does not include an introductory essay written by List. For this reason, this paper analyzes the 1856 English version of List's book which includes his introduction. When analyzing List's arguments against the Treaty of Methuen, it is found that he dismisses important theoretical factors inherent to his broad theory of national economic development.

Although List's critique of the Methuen Treaty is a short and powerful expression of his hostility to the ideas of classical economists like Adam Smith and Jean-Baptiste Say, it lacks critical theoretical components of his robust economic theory. Mainly, List's criticism of the Methuen Treaty does not refer to the three stages of economic development. List's theory suggests that only countries in the second stage of economic development should implement protectionist policies, claiming that agricultural countries should not adopt the prohibitive system. Even though he believes that Portugal is an agricultural nation in the first stage of economic development, he still supports a prohibitive system, contradicting his theoretical framework.

This article argues that List's theory of economic development is difficult to correctly apply to a real-world context since it faces the knowledge problem. The concept of the knowledge problem is associated with F.A. Hayek's argument that economic activity is founded on the coordination of choices and activities among cooperating individuals with dispersed private and local information (Hayek 1945; Horwitz 2004; Kiesling 2015). Knowledge is scattered and private, which makes it hard for any central authority to coordinate plans. From this perspective, the inconsistency of List's argument derives from the impossibility of acquiring knowledge about key variables concerning economic development. It is possible that the knowledge problem made List's analysis more susceptible to normative deviations because he was unable to rely on necessary variables. List's antagonism to a cosmopolitan perspective, particularly Adam Smith's theory, drove him away from a straightforward application of his theoretical framework.

2. List's political economy

Before analyzing List's position on the Treaty of Methuen, it is important to understand the assumptions and objectives of his political economy. Though contemporary to classical economists, List's economic thought is quite unique, differing from most economists of his time.

Between the Individual and the Whole Human Race

In 1825, Friedrich List emigrated to the United States to escape political persecution by the king of Württemberg. Prior to his arrival, List already exhibited views like the national school. Alexander Hamilton was one of the first members of such thought tradition. The American economist Daniel Raymond had a considerable influence on List's views (Szporluk 1988). The foundation of List's political economy is nationalism and the differentiation between a private economy and a national economy. List highlights the national identity as an essential factor when researching the nature of economic development and criticizes the "school's popular theory."

The popular theory refers the free trade ideas of Adam Smith and Jean-Baptiste Say. A common general theme of List's book *The National System of Political Economy* was to oppose the so called "popular theory" (Szporluk 1988, 116). List constantly criticizes the "cosmopolitan perspective of the school." He claims that Adam Smith's theories are built around the concept of an "everlasting state of peace," creating a parallel with the physiocrat François Quesnay's idea of the formation of a "merchant republic" (List 1856, 189). List's main criticism of the "popular theory" is that it conflates national and private economies.

According to List, the "popular theory" is not concerned with the welfare of a nation and seeks only the prosperity of individual's welfare (Boianovsky 2013). List states that one of a nation's requirements to be successful was to maintain a sense of national unity, pointing out that prosperity is achieved when private interests are subordinated to public interests and the pursuit of one common goal.

But between the individual and the whole human race there is the nation with its special language and literature, with its own origin and history, with its manners and habits, its laws and institutions; with its claims to existence, its independence, its progress, its duration, and with its distinct territory; an association having not only an entirely separate existence, but having an intelligence and interest peculiarly its own, a whole existing for itself, acknowledging within itself the authority of the law, but claiming and enjoying full exemption from the control of other similar associations, and consequently in the actual state of the world, able to maintain its independence only by its own strength and proper resources. (List 1856, 263)

List sees the nation as an independent entity with its own history, characteristics, and goals. The goal of a nation is to achieve productive power. The subordination of the individual's welfare to the national goals is the epicenter of the divergent ideas of the "school" and List. The "school" regarded individuals' self-interest motivation as the channel to create economic prosperity, whereas List saw the nation as the medium to achieve prosperity. Based on the importance of nationality, List defends the productive power as the collective goal of a nation.

List saw that government interventions played a crucial role in achieving the pathway to productive power. List's ideas are an early version of "the old development economics" which sees the government as the main engine behind economic development (Espinosa and Carreiro 2021). According to List, it is acceptable to override individual liberty if it is not consistent with the public good.

List (1856, 258-261) highlights that "individual liberty is generally desirable only so far as it is not inconsistent with the public good; so private industry can reasonably claim an unrestrained liberty of action, only to the extent that such action is consistent with the general prosperity of a nation." Therefore, if an individual's actions are not promoting the development the collective productive power of a nation, then the nation has the right to interfere for the sake of the national economy. The primary goal of List's political economy was to maximize national productive power (Boianovsky 2013).

Capital, Productive Power and Growth Stages

List's theoretical concept of productive power (Boianovsky 2013; Levi-Faur 1997) refers to the harmonious balance between three distinct types of capital: the capital of nature, the capital of matter, and the capital of intellect. Capital of nature alludes to every natural resource that is within a national border like water access and mining. Capital of matter refers to any output or input of production like machines, raw materials, and final products. Capital of intellect refers to institutions, entrepreneurial skills, and education. List has a hierarchical perspective on the importance of the three types of capital, seeing the latter as the most essential.

According to List, the productive power of a nation is not merely subjected to the ownership of natural and material capital, "it is dependent also upon institutions and laws, social, political, and civil, but, above all, on the securities of their duration, their independence, and their power as nations" (List 1856, 74). List's political economy is not a general guide for economic development (Boianovsky 2013). His theory was only applicable to some nations, and his analysis took into consideration rich historical and institutional variables. List argues that a country should possess inherent characteristics to be successful, including, but not limited to, possessing a considerable population, a preferable geographical location, and a vast territory with a variety of resources (List 1856).

List's first institutional differentiation is based on the climate, dividing nations between "temperate" and "tropical" countries. List's division is critical to the application of his developmental theory. Boianovsky (2013) points out that List sees countries located in a temperate zone as fit for manufacturing development, whereas countries in a torrid zone as fit for agriculture. In addition, List believes that tropical countries would be making a "fatal mistake" (List 1856, 75) if they attempt to become an industrial nation. According to List, the climate of a nation affects the availability of mental and

physical effort. Nevertheless, even a temperate country cannot achieve productive power without governmental initiative. This links to List's belief that the national interest differs from individual interest. His positive attitude to develop the industrial sector is based on the idea that "manufacturers and manufactories are the mothers and the daughters of civil liberty, of intelligence, of arts and sciences, of external and internal trade, of shipping and improved means of transport, of navigation and political power" (List 1856, 219).

According to List, the school's *laissez faire, laissez passer* principle would not allow a nation to achieve its potential productive power. Because of the self-interest motivation of individuals, they will continue engaging in trade as long as it is beneficial to them. However, if trade perpetuates a nation in the agricultural stage, consequently harming its growth potential, then the government is "not only authorized but bound by the interests of a nation to restrict or regulate employments harmless in themselves" (List 1856, 247-248).

Based on his historical analysis, List identifies three essential stages of growth in a temperate country. First, the country will develop its agriculture through the export of its surplus. After developing its agriculture, the nation will move to the second stage where early manufacturing will start to grow. In the third stage, a nation will have mastered agriculture, industry, and commerce. List is only referring to the transition from an agricultural nation to a nation that masters its productive power, but he also claims that there are stages prior to the agricultural stage such as the savage state and the pastoral state (List 1856, 265).

Boianovsky (2013) claims that List supports trade restrictions in the final two stages. However, it is likely that List only supports pure protectionism during the second stage of economic development. The issue is that List is not abundantly clear regarding when the prohibitive system should be implemented. The following quote shows that List supported trade restrictions solely during the second stage of a country's economic development.

At first, indeed, by free trade with nations of higher culture, they emerge from barbarism, and improve their agriculture; then, by means of restrictions, they give an impulse to manufactures, fisheries, navigation, and foreign commerce; then, finally, after having reached the highest degree of skill, wealth, and power, by a gradual return to the principle of free trade and free competition in their own and foreign markets, they keep their agriculturists from inaction, their manufacturers and their merchants from indolence, and stimulate them to wholesome activity, that they may maintain the supremacy which they have acquired. (List 1856, 188)

This quote also supports that List recommends a gradual implementation or alleviation of trade restrictions. List is truly clear regarding the need to progressively raise or decrease tariffs and he highlights the danger of immediate action. "No commercial policy is more dangerous and reprehensible than a sudden resort to absolute prohibition of foreign products" (List 1856, 78).

It is true that List does not support immediately lifting restrictions during the third stage, but he does support a gradual return to free trade.

List (1856, 78-79) argues that "duties thus fixed by anticipation must be strictly maintained by the government; it must be careful not to diminish them before the appointed time, and equally careful to raise them if they should prove insufficient." It is evident that the timing of the policy is key for the success of the prohibitive system. List's prohibitive system should not be seen as an immediate policy. If tariffs are indeed placed progressively, slowly, and carefully, in the short run a significant difference between the pre-intervention and post-intervention stage should not be observed. It is not an immediate policy with immediate results.

List also does not support trade prohibition after a nation reached its potential productive power in the third stage. Once in that stage, a nation would progressively diminish the duties and return to free trade. In the first stage of agricultural development, List also vehemently opposes trade restrictions, claiming that "to encourage agriculture by the aid of protective duties is vicious policy" (List 1856, 77). Only during the second stage, when manufacturing begins to grow, can policymakers begin to adopt protectionist policies.

The political economy of List reflects a nationalistic viewpoint in which the subordination of individual wellbeing to the welfare of the nation is critical for a civilization to reach the required degree of productive power. The balance of natural capital, material capital, and intellectual capital is referred to as productive power. This occurs in the final stage of development when the nation has progressed from the second stage, in which the government aids in the stimulation and protection of national manufacturing, to the third stage, where a country efficiently engages in agriculture, commerce, and industry.

List's theory is based on historical observations. In the first part of *The National System of Political Economy*, List only approaches the historical development of nations and summarizes its teachings. In the second part of the book, List builds his theoretical framework on the economic development of nations. List reserves a discussion of the Portuguese economic progress in chapter 5 of part 1 of his book, focusing on the Treaty of Methuen as an important historical milestone for the Portuguese late economic development.

3. The Friedrich List

In 1702, John Methuen, the English envoy to Portugal, visited Lisbon to persuade the Portuguese government to break relations with Louis XIV. The first Methuen Treaty is not of an economic nature but a political alliance. Methuen withdrew from Lisbon in 1703, leaving his son with the diplomatic capability to sign the treaty and break the alliance between Portugal and France (Sodré 1965; Francis 1960). In this first agreement, King Pedro II of Portugal formally joined the Second Grand Alliance, recognizing Archduke Charles as the legiti-

mate heir to the Spanish throne. The second Methuen Treaty signed in December of 1703 is an economic agreement between Great Britain and Portugal, and it is a direct result of the diplomatic success of the first political treaty signed in May of 1703 (Lodge 1933). The Port Wine Treaty was straightforward and composed of only three articles. It removed all regulatory restrictions on importing English woolens to Portugal. In addition, Great Britain was bound to import Portuguese wines at a third less tariff than French wines.²

In his *magnum opus*, *The National System of Political Economy*, List opposes Adam Smith's position that the Methuen Treaty was disadvantageous to Britain. Friedrich List claims that the agreement was deleterious to Portugal since it destroyed the Portuguese cloth industry and expanded Great Britain's influence in Portugal. List argues that "Portugal sank into complete political dependence upon England, while England acquired the means, through the gold and silver earned in her trade with Portugal, of extending her own commercial intercourse with China and the East Indie" (List 1856, 115). His reasoning follows a state-led industrialization approach to early industries (Gerschenkron 1962; Ince 2016; Szporluk 1988). The concepts advanced by List are an early version of "the old development economics," which views the government as the primary force driving economic growth (Espinosa and Carreiro 2021). As it was mentioned before, List argues that in the early industrial development stage, the state has a key role, through tariffs and protectionism, in assisting the national industry in achieving competitiveness.

However, to successfully implement the prohibitive system, a nation must meet two requirements. First, a nation must have a temperate climate. Second, the nation must be in the second stage of its economic development. Although Portugal was a temperate nation, List does not believe that Portugal was in the second stage of its economic development, claiming that "in the first of these stages we see Spain, Portugal, and Naples, in the second, Germany and North America; France appears to be on the limits of the latter; but England alone has not only reached, but maintains an industrial and com-

mercial supremacy" (List 1856, 188). Following List's theory, if Portugal were indeed in the first stage of development, it would benefit from trading with a more developed nation like Britain.

List's conclusion that Portugal was a first stage country is supported by historical data. Before the treaty, in the mid-1670s, Bordeaux wine was exported approximately 16,000 barrels/year to England, and Jerez wine was exported around 9,000 barrels/year to England. Shipments from Porto to England would not exceed 500 barrels/year (Martins 2003).³ From the end of the 1670s to the end of the 1680s, Portuguese wine exports to England rose from 1,200 barrels/year to almost 5,500 barrels/year (Martins 2003). Between the end of the 1680s and the end of the 1690s, the Portuguese wine exports to England reached 11,200 barrels/year. After the Methuen Treaty, between 1704 and 1720, the quantity of wine exported to England increased from 15,900 barrels/year to 22,700 barrels/year (Martins 2003). In the same period, the Portuguese overall exports to England increased from £240,000 to £349,000 (Fisher 1963). Hence, Portugal still had room to improve its agriculture through trade, and according to List's theory, the Portuguese Crown should not promote protectionist policies yet.

However, though List recognizes that Portugal was in the first stage of economic development, he still praises the minister Count of Ericeira for his initiatives to industrialize the country.

Portugal, however, under a skillful and an energetic minister made progress in manufactures and industry, the first results of which astonish us. That country, like Spain, was the immemorial possessor of large flocks of sheep. Strabo relates that a fine breed of sheep had been introduced there from Asia, and that a single sheep was sold as high as one talent. In 1681, when Count Ericeira came to the ministry, he conceived the project of establishing in the country manufactures of cloth, with the view of using their own wool and thus supplying Portugal and her colonies. (List 1856, 131)

Based on List's theory, if Portugal were indeed a first-stage agricultural country and possessed flocks of sheep but no cloth manufacturers, it would not be beneficial to artificially impulse the Portuguese manufacturing in the early stage. The question then becomes why there is a disconnection between List's theory and its application? If List's criticism of the Methuen Treaty were connected to his theoretical scope, he would not vehemently oppose trade between Portugal and Britain. Nevertheless, List praises the Portuguese prohibitive system even though such a system would only be acceptable during the second stage of economic development.

4. The origins of the inconsistency

² ART. I. His sacred royal majesty of Portugal promises, both in his own name, and that of his successors, to admit, forever hereafter, into Portugal, the woolen cloths, and the rest of the woolen manufactures of the British, as was accustomed, till they were prohibited by the law, nevertheless upon this condition:

ART. II. That is to say, that her sacred royal majesty of Great Britain shall, in her own the growth of Portugal into Britain: so that at no time, whether there shall be peace or war between the kingdoms of Britain and France, anything more shall be demanded for these wines by the name of custom or duty, or by whatsoever other title, directly or indirectly, whether they shall be imported into Great Britain in or hogsheads, or other casks, than what shall be demanded for the like quantity or measure of French wine, deducting or abating a third part of the custom or duty. But if at any time this deduction or abatement of customs, which is to be made as previously mentioned, shall in any manner be attempted and prejudiced, it shall be just and lawful for his sacred royal majesty of Portugal, again to prohibit the woolen cloths, and the rest of the British woolen manufactures.

ART. III. The most excellent lords the plenipotentiaries promise and take upon themselves, that their above-named masters shall ratify this treaty; and within the space of two months the ratifications shall be exchanged (Sodré 1965; Smith 1776).

³ Note that the Portuguese word "pipa" was translated to the English word "barrel."

This section explores explanations that can highlight the inconsistency between List's political economy and his critique of the Methuen Treaty. It is most likely that the discontinuity between List's historical observation of the Treaty of Methuen and his theory is a result of the knowledge problem. The knowledge problem is associated with the Austrian economist F.A. Hayek and refers to the inability of a central authority to gather dispersed and private information, making it hard, in the absence of a price system, to efficiently allocate resources (Hayek 1945).

Applied to the case of List's analysis of the Treaty of Methuen, it means that even though List subjects the individual's wellbeing to the productive power of the nation, to truly know what stage of development the country is in, it is still necessary to have access to local knowledge. The lack of data makes List's analysis less objective and more vulnerable to normative conclusions. For instance, List harshly criticizes Smith's stance on the Treaty of Methuen, and it is possible that given the time's political climate, List abandoned his theory of economic development to counter Smith's cosmopolitanism.

List's National System and the Knowledge Problem

As previously stated, List believes that the nation has the right to intervene in the national economy if an individual's actions do not promote the growth of the nation's collective productive power. Maximizing national productive power was List's main objective (Boianovsky 2013). In List's theory of economic development, the knowledge problem arises when he assumes that the king or the policy maker has the knowledge of specific information about a nation's population, like the level of intellectual capital and the spirits of art and enterprise.

According to List, first, a country will grow its agriculture by exporting excess. Following the development of its agriculture, the country will move to the second stage, when early manufacturing will begin to expand. A country will have mastered agriculture, industry, and commerce by the third stage. List only supports complete prohibition and protectionism in the second stage of economic development and is aware of the problems caused by the early implementation of trade restrictions and the late removal of the trade restrictions.

List (1856, 266) claims that "when manufacturing industry is still in the first stage of its development, protective duties should be very moderate; they should be raised by degrees in proportion as intellectual and material capital, skill in the arts, and the spirit of enterprise, increase in the country." Hence, the policy maker requires the precise knowledge of the state of industry in the country and the level of intellectual capital, material capital, spirit of enterprise and even art skills. According to List's theory, the Methuen Treaty's fast transition from free trade to prohibition and then from prohibition to free trade could be problematic.

It can be argued that neither the best Portuguese policy maker nor List would have the necessary tools to ac-

cess the level of intellectual capital, material capital, and entrepreneurial spirit that Portuguese citizens possessed. Although List can only truly apply his theory if he possesses knowledge about these important variables, the knowledge about these types of capital is only available within individuals. As a result, from a top-down perspective, correctly determining the level of duties and implementing the prohibitive system is extremely difficult.

Although List states Portugal already produced excellent cloth equal in quality to England's (Menezes and da Costa 2012), Costa et al. (2016) point out that Portuguese woolen enterprises were operating under a narrow margin of profits. They required not only monopoly rights but also protectionist measures. The Portuguese cloth industry output was not sufficient to supply both the domestic and Brazilian markets simultaneously (Costa et al. 2016). Hence, Count of Ericeira's protectionist policy had severe structural problems, hurt the British community in Portugal, and failed to create a competitive cloth industry.

List's claim that the Methuen Treaty destroyed the Portuguese cloth industry seems disconnected from the historical moment and his theoretical contribution. The Portuguese cloth industry was not prepared to compete with English enterprises. As Costa et al. (2016, 200) point out, the Methuen Treaty "just anticipated the interruption of the program to promote industrial output that had started twenty years earlier." Even with the legal advantage over the British competitor and state-backed monopoly, the Portuguese national industry failed to be efficient. Their failure to reduce their marginal cost caused their decline. They were highly inefficient as they were unable to be competitive even after over twenty years of protectionism enforced by the Portuguese Crown.

The Portuguese cloth industry was never meant to substitute the English textiles but complement its supply. As List (1856, 79) says "when, under the rule of suitable and progressive duties, the manufactures of a country do not thrive, it is evidence that the country does not yet possess the conditions requisite to a manufacturing people." Therefore, following List's point, if Portugal after a substantial time under the prohibitive system failed to develop its manufacturing, then Portugal was not suitable to be a manufacturing nation. When analyzing the Treaty of Methuen, List does not acknowledge that the early Portuguese state-led industrialization plan failed, and that Portugal was not ready to be a manufacturing nation.

When making his analysis of the Methuen Treaty, List dedicates no lines to the discussion of the spirit of enterprise in Portugal, the profit margins of the local cloth industries, the local prices of cloth, and the level of material and intellectual capital in the country. Though the implementation of his general policy prescription relies on a robust discussion of these variables, the data is only available within individuals and firms. Hence, the application of List's theory to the context of Portugal was limited by the knowledge problem, leading him to

provide an inconsistent and contradictory policy analysis of the Methuen Treaty.

List did not have the precise information to conclude if Portugal was indeed ready to be a manufacturing nation. He also did not have enough information to establish a precise level of duties. Hence, his analysis becomes not only inconsistent but also vague. List classification of Portugal as a first-stage country might have been completely arbitrary and not careful. It is also possible that, lacking the necessary knowledge to provide an accurate policy prescription based on his theoretical framework, he simply jumped into a shallow criticism of the Methuen Treaty to oppose Adam Smith's cosmopolitan political economy.

Opposition to Adam Smith

In *The Wealth of Nations*, Adam Smith criticizes the Treaty of Methuen. Given Smith's commitment to show the harms of mercantilism and the benefits of trade, it is surprising to see him criticizing a trade deal that became a symbol of specialization with Ricardo's example of comparative advantage (Ricardo 1891). In fact, Adam Smith sees the Treaty of Methuen as an old mercantilist policy and not as a free trade agreement. List divides Adam Smith's arguments in three points.

First, Smith claims that the Treaty of Methuen granted Portugal a specific privilege over France, but the British cloth paid the same duty as other nations. Smith's second argument is that Portugal was engaging in a round-about trade. Smith believes that trade with Portugal was performed to acquire gold to trade with other countries. The Brazilian gold gained during the trade with Portugal was employed to purchase other consumable goods. Smith calls this feature a round-about trade and believes that "a direct foreign trade of consumption is always more advantageous than a round-about one" (Smith 1776, 422). According to List, Smith's third and last point was that England "not receiving the precious metals from Portugal, would have procured them elsewhere" (List 1856, 136).

List sequentially responds to Smith's three arguments. First, after a series of rhetorical questions,⁴ List recognizes that "the treaty gave Portugal a privilege, but one merely nominal; it conferred upon the English a privilege *de facto*" (List 1856, 135). According to List, England needed the Portuguese wine since they ceased the importation of French wine, also claiming that the Brazilian gold and silver helped Britain acquire goods

from the Indies. List also points out that the manufacturers of cloth in Portugal were ruined due to the deal.

List then responds to Smith's second point regarding the round-about foreign trade of consumption where England was trading cloth for Brazilian gold and then using that gold to purchase foreign goods from other countries instead of directly trading with other countries. List scrutinizes Smith's free-market mindset and even questions his intellectual honesty and intelligence, claiming that "Adam Smith could not escape whilst uttering these strange and almost ridiculous arguments, blinded as he was by the idea, not ungenerous, of justifying absolute free trade" (List 1856, 135).

List then proceeds to provide a practical example claiming that Smith's round-about argument is the same as saying that "a baker who sells bread to his customers for money, and with that money buys flour from the miller, is not doing an advantageous business, because he is not directly exchanging his bread for flour business by two exchanges instead of one" (List 1856, 135-136). List also points out that Portugal was Britain's final consumer and that the goods that Britain purchased from the Indies and other countries were necessary to produce the final good. He adds that Portugal did not demand British goods to engage in direct trade.

List rejects Smith's third claim that Britain could buy gold from other nations without bearing a cost for not buying gold from Portugal. List asserts that Britain would not benefit from the surplus of Portuguese gold whereas its rivals would. If Portugal ratified a deal with Holland or France, the English manufacturing industry and navigation would not have accomplished any success. Regarding Portugal, List claims that the Methuen Treaty was harmful since "the agriculture and manufactures, the commerce and navigation of Portugal far from being invigorated by this arrangement with England, declined thenceforward without intermission" (List 1856, 137).

It is important to highlight that Smith's opposition to the Treaty of Methuen is linked to his theoretical framework. Dimand (2018) points out that in Smith's *Lectures on jurisprudence*, a lecture series initially delivered at the University of Glasgow in 1762-1763, Smith prefers a free trade agreement with France over a free trade agreement with Portugal.

A free trade to France would tend infinitely more to enrich Great Britain than a free trade to Portugal, because France, on account of its superior opulence having more to give, would take more of us, and exchanging to a much greater value and in a much greater variety of ways, would encourage more industry in Great Britain and give occasion to more subdivisions of labor. (Smith 1978, 629)

France was a more populous country than Portugal. According to Smith's theory, since the extent of the market limits the division of labor, closing the doors to France would diminish the capacity of the division of labor. Smith's argument against the Methuen Treaty is strong in the context of normalization with France. Adam Smith was already advocating for changes in

⁴ Did not the English from that time enjoy a monopoly of the Portuguese market for products manufactured by them, and of which they also possessed the raw material? Did they not find in this trade full compensation for the heavy duties? Did not the course of exchange favor the consumption of Portuguese wines in England by the difference of about fifteen per cent? Did not the exportation of French and German wines to England nearly altogether cease? Did not the gold and silver of Portugal furnish England the means of buying in India large stocks of goods, with which the continent of Europe was inundated? Were not the manufactures of cloth in Portugal entirely ruined for the benefit of the English manufactures? Did not all the colonies of Portugal, and especially rich Brazil, thus become virtually English colonies? (List 1856, 135).

trade practices between France and Britain, which were soon accomplished with the ratification of the Eden Agreement in 1786.

The Anglo-French Commercial Treaty of 1786 shortly ended the rivalry between France and Britain (Henderson 1957). This is extremely important given that, like the Methuen Treaty, List also opposed the Eden Agreement. List considers the Eden Agreement a second edition of the treaty of Methuen with “effects quite as disastrous as the Portuguese original” (List 1856, 143). List also praises protectionist policies promoted by the French government.

Free trade with England occasioned such dreadful disasters to an industry which had grown up under the continental system, that it became necessary to seek a speedy refuge in the prohibitive system, under the shield of which, according to the testimony of M. Dupin, the manufacturing industry of France doubled between 1815 and 1827. (List 1856, 146-147)

List’s criticism of the Eden Agreement is consistent with his growth stages theory. Since France was deep in the second stage of economic development, it is appropriate, according to List’s theoretical framework, to implement a prohibitive system to support the national industry. However, the parallel between the Methuen Treaty and the Eden Agreement as both producing the same effect is inconsistent with List’s growth stages theory. If Portugal and France were in different growth stages, free trade would have different outcomes in each country.

Yet, List’s critique of the Treaty of Methuen is indeed well aligned with his opposition to the “school.” John Austin (1842, 520) critically reviews List’s *National System of Political Economy* and highlights that List is eager to distinguish his political economy from the “school’s cosmopolitical economy.” Watson (2012, 460) mentions that List “attempts to signal the reasonableness of his position by caricaturing Smith’s.” It is also worth mentioning that, when reviewing List’s economic thought, Jacob Viner (1929) claims that List’s criticism of Adam Smith is unfair, not meeting the standards of objective scientific analysis. The impossibility of applying List’s theory due to the knowledge problem supports Viner’s point.

Because of the knowledge problem, when criticizing Smith’s position on the Methuen Treaty, List did not have enough information to be objective and scientific. As a result, List abandoned his theory and engaged in a series of theoretically unfounded attacks on Smith. Given that List dedicates a considerable part of his analysis of the Treaty of Methuen to refute Adam Smith’s perspective on the treaty, such a point raised by Austin (1842) seems an avenue of explanation to the inconsistency between List’s framework and his analysis of the treaty.

5. Conclusion

List’s perspective on the Methuen Treaty is present in the modern historical literature. Historical text-

books and even relevant economists derived their understanding of the Methuen Treaty from List’s work, overlooking the discontinuity between List’s framework and his analysis. Boianovsky (2013) highlights that some economists who were influenced by List’s ideas ignored the distinction between “temperate” and “tropical” zones, often using List’s framework to support policies in developing countries. What is curious about the Treaty of Methuen is that when analyzing the effects of the treaty on the Portuguese industrial sector, List himself ignored another central idea of his own theoretical framework. There is a clear disconnection between his criticism of the Methuen Treaty and his theory of growth stages. This inconsistency led some scholars to replicate List’s negative understanding of the treaty without placing the treaty into the general theoretical framework of the *National System*.

According to List, in the first stage of economic development, a country will develop its agriculture by exporting its surplus, then move to the second stage where the early industry will grow. In the third stage, a nation will have a harmonious dominance of agriculture, industry, and commerce. This paper shows that List only defends the prohibitive system during the second stage. In addition, he believes that Portugal was in the first stage of economic development. Hence, Portugal should not adopt the prohibitive system. Nevertheless, even if the growth stages are ignored, List’s analysis of the Treaty of Methuen continues to be contradictory, claiming that if a country under the prohibitive system fails to develop its manufacturing, then that country is not suitable to be a manufacturing nation. This happened with Portugal after almost two decades of prohibition, but List ignores such a feature.

John Austin (1842) critically reviews List’s *National System of Political Economy* and points out inconsistencies in List’s framework.

No country (says he) has a true call to manufactures, unless she is gifted with the following capacities for manufacturing to advantage, A large and well-rounded territory; a large and manifold provision of the natural means of manufacturing; an agriculture pretty far advanced; a general diffusion of mental cultivation amongst the individuals composing the community; political and legal institutions, which afford security for person and property, and allow a free use of bodily and mental faculties. (Austin 1842, 535-536)

Austin (1842) claims that, by such a standard, countries like Spain and Russia would not possess the necessary qualities to be a manufacturing nation. Nevertheless, List still calls for a prohibitive system in such nations.

This article argues that List’s inconsistency when characterizing the development stage of countries rises in results of the impossibility of knowing if a country possesses the necessary attributes to be a manufacturing nation. The knowledge problem significantly weakens List’s theory, and the discrepancy derives from a lack of

knowledge about variables that lie within individuals, such as intellectual capital, material capital, the spirit of enterprise and art skills. Since List did not have this knowledge, when analyzing the Methuen Treaty, he does not provide a discussion about these variables.

The proper application of List's theory requires local data that he did not possess. As a result, List's analysis of the Methuen Treaty lacked sufficient data capable of truly identifying the development stage of the Portuguese industry. The result was an analysis that was disconnected to his overall theory of economic development and vulnerable to normative conclusions. Since Adam Smith

believed that the treaty benefited Portugal over England, List dedicated his analysis to prove the contrary.

List devotes a considerable part of his analysis of the Treaty of Methuen to refute Adam Smith's perspective on the treaty. Austin (1842) points out that List had a solid opposition to the school's political economy and that he tried to differentiate his analysis and theory from the school's perspective. This feature is an avenue for explaining the inconsistencies between List's theoretical framework and his analytical work. List's critique of the Methuen Treaty is a fitting example of his hostility to Adam Smith's ideas, and it also exemplifies the chal-

lenges that the knowledge problem imposes on economists when attempting to apply economic development theories to a complex social environment.

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