The debate on the role of the state versus that of the free market in the socioeconomic process is as old as the history of political economy. Adam Smith is the best-known early thinker whose writings became the focus of the early debate. Alexander Hamilton and Friedrich List were among contributors to the issues raised by Smith. Major shifts in the debate occurred amidst the devastating impact of the Great Depression and World War II, giving rise to what one writer characterized as “The Clash that Defined Modern Economics” — the clash between John Maynard Keynes and Friedrich von Hayek. More recently, the role of the state has become a major political issue among politicians across the globe. This junior seminar attempts to introduce students to this debate. The goal is not to resolve the issues involved in the debate, but rather to build up the conceptual and empirical knowledge needed to be informed participants in this all-important debate.

Selected quotes from the major texts on the subject may give us a general idea of the complex issues debated. Writing in 1776, Adam Smith stated in *The Wealth of Nations* that

> every individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry, he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand [the invisible hand of the free market] to promote an end which was no part of his intention. . . . By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it. I have never known much good done by those affected to trade for the public good.\(^1\)

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In the 1920s, as Nicholas Wapshott narrates,

*Keynes believed it was a government’s duty to do what it could to make life easier, particularly for the unemployed. Hayek believed it was futile for governments to interfere with forces that were, in their own way, as immutable as natural forces. Keynes rejected adherence to the free market as an inappropriate application of Darwinism* [the survival of the fittest principle] *to economic activities and argued that a better understanding of the workings of an economy would allow responsible governments to make decisions that could iron out the worst effects of the bottom of the business cycle. Hayek eventually came to the conclusion that knowledge about how exactly an economy worked was difficult if not impossible to discover and that attempts to form economic policy based on such evidence were, like a barber practicing primitive surgery, likely to do more harm than good.*

The idea of the “Washington consensus” was added to the debate in the 1990s. Thus, Narcis Serra, Shari Spiegel, and Joseph E. Stiglitz declared in their 2008 edited volume:*

*The point of departure in this book is the Washington Consensus — the set of views about effective development strategies that have come to be associated with the Washington-based institutions: the IMF [International Monetary Fund], the World Bank, and the US Treasury. . . . According to Williamson [John Williamson], ‘The Washington Consensus was a . . . response to a leading role for the state in initiating industrialization and import substitution. The Washington Consensus said that this era was over. . . . In the countries that followed Washington Consensus policies, economic growth was limited at best, and disproportionately benefited those at the top. In Latin America, for example, . . . growth under the Washington Consensus was half of what it had been from the 1950s through the 1970s when the region followed other economic policies, such as import substitution. Even in countries where Washington Consensus policies appear to promote growth, such growth was often not accompanied by significant reductions in poverty. Meanwhile, the countries of East Asia followed a quite different set of policies, and had enormous successes. For instance, governments played an important role in promoting particular industries. In some cases, government enterprises (such as Korea’s national steel company) became global leaders in efficiency. To be sure, governments in the region did maintain macro stability, but they were slow to liberalize trade, and some countries, such as China, still have not fully liberalized capital markets. In short, both theory and evidence weigh heavily against what has come to be called Washington Consensus policies.*

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In his carefully considered response in defense of the Washington Consensus, John Williamson says,

*I think one must concede that some of the East Asian countries, notably Korea and Taiwan, were far from pursuing laissez-faire during their years of catch-up growth, but this does not prove that their rapid growth was attributable to their departure from liberal policies, as critics of the Washington Consensus seem to assume axiomatically. There were, after all, two other East Asian economies that grew with comparable rapidity, in which the state played a much smaller role. Indeed, one of those — namely, Hong Kong — was the closest to a model of laissez-faire that the world has ever seen.*


“explodes the myth that a market economy leads inevitably to democratic government” [p. ix]. “... ‘the invisible hand’ of free markets around the globe is being balanced by the notably more visible hand of central governance” [p. 8]. “Of immediate concern is that China’s governing model is more appealing to the developing world and some of the middle-sized powers than America’s market democratic model. Given a choice between a market democracy and its freedoms and market authoritarianism and its high growth, stability, improved living standards, and limits on expression — a majority in the developing world and in many middle-sized, non-Western powers prefer the authoritarian model” [p. x].

The Chinese-American comparison is carried further by Thomas L. Friedman and Michael Mandelbaum. In their book, *That Used to be Us: How America Fell Behind in the World It Invented and How We Can Come Back*, they offer the reader their experiences in China and in the United States:

> “In September 2010, Tom [Thomas Friedman] attended the World Economic Forum’s summer conference in Tianjin, China. Five years earlier, getting to Tianjin had involved a three-and-a-half-hour car ride from Beijing to a polluted, crowded Chinese version of Detroit, but things had changed. Now, to get to Tianjin, you head to the Beijing South Railway Station — an ultramodern flying saucer of a building with glass walls and an oval roof covered with 3,246 solar panels — buy a ticket from an electronic kiosk offering choices in Chinese and English, and board a world-class high speed train that goes right to another roomy, modern train station in downtown Tianjin. Said to be the fastest in the world when it began operating in

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2008, the Chinese bullet train covers 115 kilometers, or 72 miles, in a mere twenty-nine minutes.

The conference itself took place at the Tianjin Meijiang Convention and Exhibition Center — a massive, beautifully appointed structure, the like of which exists in few American cities. As if the convention wasn’t impressive enough, the conference’s co-sponsors in Tianjin gave some facts and figures about it (www.tj-summerdavos.cn). They noted that it contained a total floor area of 230,000 square meters (almost 2.5 million square feet), and that ‘construction of the Meijiang Convention Center started on September 15, 2009, and was completed in May, 2010.’ Reading that line, Tom started counting on his fingers: Let’s see — September, October, November, December, January . . . Eight months.

Returning home to Maryland from that trip, Tom was describing the Tianjin complex and how quickly it was built to Michael [Michael Mandelbaum] and his wife Anne. At one point Anne asked: ‘Excuse me, Tom. Have you been to our subway lately?’ We all leave in Bethesda and often use Washington Metrorail subway to get to work in downtown Washington, DC. Tom had just been at the Bethesda station and knew exactly what Anne was talking about. The two short escalators had been under repair for nearly six months. While the one being fixed was closed, the other had to be shut off and converted into a two-way staircase. At rush hour, this was creating a huge mess. Everyone trying to get on or off the platform had to squeeze single file up and down one frozen escalator. It sometimes took ten minutes just to get out of the station. A sign on the closed escalator said that its repairs were part of a massive escalator ‘modernization’ project.

What was taking this ‘modernization’ project so long? We investigated. Cathy Asato, a spokeswoman for the Washington Metropolitan Transit Authority, had told the Maryland Community News (October 20, 2010) that ‘the repairs were scheduled to take about six months and are on schedule. Mechanics need 10 to 12 weeks to fix each escalator.’

A simple comparison made a startling point: It took China’s Teda Construction Group thirty-two weeks to build a world-class convention center from the ground-up — including giant escalators in every corner — and it was taking the Washington Metro crew twenty-four weeks to repair two tiny escalators of twenty-one steps each. We searched a little further and found that WTOP, a local news radio station, had interviewed the Metro interim general manager, Richard Sarles, on June 20, 2010. Sure, these escalators are old, he said, but ‘they have not been kept in a state of good repair. We’re behind the curve on that, so we have to catch up . . . Just last week, smoke began pouring out of the escalators at the Dupont Circle station during rush hour.’

. . .

The quote [quotes from letters to newspapers] we found most disturbing, though, came from a Maryland Community News story about the long lines at rush hour caused by the seemingly endless Metro repairs: ‘My impression, standing on line there, is people have sort of gotten used to it,’ said Benjamin Ross, who lives in Bethesda and commutes every day from the downtown station.

. . . People have sort of gotten used to it. Indeed, that sense of resignation, that sense that, well, this is just how things are in America today, that sense that
America’s best days are behind it and China’s best days are ahead of it, have become the subject of watercooler, dinner-party, grocery-line, and classroom conversations across America today” [pp. 3-5].

These quotes hit the nail on the head — they hit the central issue in the debate: Given that the existence of the market is a necessary condition for national economies to perform at a high level, how large should the role of the state be for the economy to grow and serve the needs of all citizens? What weight do we attach to the role of the state in explaining the performance of national economies over time? How do we explain the differences in the role of the state between one country and another over time? How does the inter-play between economics and politics (political economy) feature in the explanation? How important are the differing historical experiences that created the differing economic and political conditions that influence the size and role of the state over time? Why have major economic and political thinkers differed on the issue of the role of the state versus that of the market in the socioeconomic process? Why has the role of the state versus that of the market become a burning issue among politicians across the globe (particularly in the United States) since the 1980s? These and related questions constitute the central focus of the course.

For purposes of clarity at the onset, some elements of the foregoing questions need a brief elaboration. One such element pertains to notable economic and political thinkers. Historians of ideas generally agree that to understand why particular thinkers thought and wrote the way they did we must examine their life experiences, the prevailing socio-political conditions under which they thought and wrote, and the dominant intellectual traditions that shaped their intellectual development. The other element concerns policy debate and choices among politicians. On this, the role of vested interests and their relative bargaining power is crucial. In a democracy (government of the people, by the people, and for the people), this creates a potential conflict between what should be done (the theoretically ideal policy) and what can be done, something that Adam Smith recognized. The historical process, which created over time different interest groups with differing relative bargaining power at a given moment in different countries, is, therefore, pertinent to our understanding of the issues debated.

Because the course focuses on major issues of our time, students are encouraged to think freely and debate the issues among themselves in and outside the classroom. There are no right and wrong arguments. Emphasis is on the amount of relevant information gathered from a variety of sources and the logical organization and interpretation of the information. Students must see this course as their own, even though designed by the professor, who, as a more advanced student, will guide the classroom debate and share his intellectual experience with the students.

The course appears to be very extensive, covering several countries over long time periods. But, because it focuses primarily on the role of the state, within the context of

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7 The authors’ formula for the US to regain its leadership of the global economy “consists of five pillars that together constitute the country’s own version of a partnership between the public and private sectors to foster economic growth” (pp. 34-36).
the ongoing state-market debate, it is not as extensive as it appears. Only those aspects of
the development process relevant to the role of the state in the selected countries or
regions will be of concern to us in the readings. Where necessary, the professor will
provide the basic facts. The interpretation of those facts and their employment to develop
arguments in the state-market debate will be left largely to the students, with some
guidance by the professor.

II Course Requirements

The weekly meetings in the course outline are centered on specific aspects of the course,
each of which has a set of questions to guide the reading and the discussion. Students are
advised to pay close attention to these questions in their readings and preparation for each
meeting. There are three sets of four-page essay questions (two questions each). As stated
in the course outline, students have to choose one of the two questions in each of the
three sets. Readings for the essays are listed in each case. The question chosen will
determine which readings to select. Students are expected to be resourceful and discover
relevant texts or sources of information, beyond those listed, in their preparation for the
weekly meetings and for the production of the four-page essays. As shown in the course
outline, the essays will be formally presented and discussed in class. Students are
expected to revise their essays following the class discussion and submit them the
following week to the professor for grading. Each essay carries 30 marks. The dates for
the presentations are shown in the course outline.

The course is on a subject that is being hotly debated by scholars, politicians, and the
general public. We expect students to come to each class fully prepared to participate
actively in a lively debate. It is particularly important that students attend every class, and
do so punctually, so that we can all start each class together. Attendance carries a total of
10 marks.

III REQUIRED TEXTBOOKS

(A) Textbooks to be purchased by students


2 Narcis Serra and Joseph E. Stiglitz (eds.), *The Washington Consensus Reconsidered: Towards a New Global Governance*


4 Nicholas Wapshott, *Keynes, Hayek: The clash that defined modern economics*

(B) **Required textbooks to be placed on print reserve**


**Electronic Reserve for Required Readings**


I


IV Course Outline

1 **February 2, 2021:**
Discussion of course focus, scope, and requirements, including specifics on students’ preparation for and participation in class discussion. The main material for this introductory class is the course outline containing some details about the course. These details should be studied closely before the class.

2 **February 9, 2021:**
The Washington Consensus, the Beijing Consensus, and the political debate on the role of the state versus that of the free market. Among other things, the discussion focuses on what is meant by the Washington Consensus and the Beijing Consensus, and a brief history of the debate, including the role played by President Ronald Reagan of the United States and Prime Minister Margaret Thatcher of the United Kingdom.

**Main questions for the discussion:** i) What are the essential differences between the Washington consensus and the Beijing consensus? ii) What would you consider the long-lasting contributions of President Reagan and Prime Minister Thatcher to the state-market political debate? iii) From what we know, where did the Trump presidency stand in terms of the state-market debate?


3 **February 16, 2021:**
Notable economic thinkers, their times and their ideas: Adam Smith; Alexander Hamilton; Friedrich List.

**Main questions for the discussion:** i) Under what historical circumstances did they formulate their ideas? ii) What are the main differences between their ideas? iii) What impact did their ideas have on state policy in their respective countries?


4 **February 23, 2021:**
Notable economic thinkers, their times and their ideas: John Maynard Keynes, Friedrich von Hayek.
Main questions for the discussion: i) Under what historical circumstances did they formulate their ideas? ii) What are the main differences between their ideas? iii) What impact did their ideas have on state policy worldwide?

Required Reading: Wapshott, Keynes, Hayek: The clash that defined modern economics.

5 March 2, 2021:
The British Industrial Revolution and the State-Market Debate

Main questions for the discussion: i) How important was the role of the state in the British Industrial Revolution? ii) Would you agree that the British Industrial Revolution confirms the importance of the market in long-run economic development? iii) Would you agree that the British Industrial Revolution was the first successful case of cooperation between the state and the market?


6 March 9, 2021:
Presentation and Discussion of 4-page Essays: Students should write their 4-page (typed and double-spaced) essays on any one of the following questions (half of the essays will be presented and discussed on March 9, 2021 and the other half on March 16, 2021):

i) In what ways does the historical evidence on the British Industrial Revolution support the argument of the proponents of free markets and minimal government?

ii) To what extent does the role of the state explain why it was England, and not the Netherlands, that launched the Industrial Revolution?

7 March 16, 2021:
Presentation and Discussion of 4-page Essays Continue

Readings for the Essays:
i) Inikori, Africans and the Industrial Revolution in England, pp. 89-155;


iv) Other readings found by students.
8  **March 23, 2021:**

**Main questions for the discussion:** i) How important was the role of the state in the economic development of the United States from the late eighteenth century to 1900? ii) What difference did the changing role of the state make to economic development in Latin America between 1850 and 2000? iii) To what extent does the differing role of the state explain the differing levels of development of the economies of Latin America and the United States between 1800 and 1900?

**Required Reading:**
ii) “The State, the Market, and Economic Development in Latin America” (Text Prepared for the Class by Joseph E. Inikori).

9  **March 30, 2021:**
Presentation and Discussion of 4-page Essays: Students should write their 4-page (typed and double-spaced) essays on **any one** of the following questions (half of the essays will be presented and discussed on March 30, 2021, and the other half on April 6, 2021):

i) *In what ways does the path of socioeconomic development in the United States from the late eighteenth century to the present contribute to our understanding of the issues in the state-market debate?*

ii) *In what ways does the path of socioeconomic development in Latin America from 1850 to 2000 contribute to our understanding of the issues in the state-market debate?*

10 **April 6, 2021:**
Presentation and Discussion of 4-page Essays Continue

**Readings for the Essays:**


ii) “The State, the Market, and Economic Development in Latin America” (Text Prepared for the Class by Joseph E. Inikori).


iv) Other readings found by students.
April 13, 2021:
Socioeconomic development in Asia (China, India, Japan), 1850-2000 and the state-market debate.

Main questions for the discussion: i) What can we learn about the role of the state from the effect of quasi colonial rule on economic development in China in the nineteenth century? ii) What can we learn about the role of the state from the effect of British colonial rule on economic development in India? iii) What does the role of the state in Japan’s economic development from the mid-nineteenth century to World War I contribute to our understanding of the issues in the state-market debate?

Required Reading:

April 20, 2021:
Presentation and Discussion of 4-page Essays: Students should write their 4-page (typed and double-spaced) essays on any one of the following questions (half of the essays will be presented and discussed on April 20, 2021, and the other half on April 27, 2021):

i) Using China, India, and Japan as case studies, show how the consequences of colonization and semi-colonization help us understand the issues in the state-market debate.

ii) In what ways does a comparative study of economic growth in China and the United States since the 1970s help us understand the issues in the state-market debate?

April 27, 2021:
Presentation and Discussion of 4-page Essays Continue

Readings for the Essays:


iv) Other readings found by students.

May 4, 2021:
Concluding discussion of the state-market debate:

1. Summary statement of the positions of our selected notable thinkers on the state-market debate:
Adam Smith – the pursuit of self-interest and the invisible hand of the free market.

Alexander Hamilton and his opponents – comparative advantage in manufacturing is historically created with the help of the state in the early stages;

response of his opponents: agriculture is the most productive sector of the economy; the state should not artificially force the movement of resources from agriculture to manufacturing; at the appropriate moment the free market will move resources to manufacturing.

Friedrich List: Late industrializers need state intervention to catch up with the leading nations, after which universal free trade can be established under a universal republic (a world federal government constituted by all nations of the world, making laws that govern all nations).

John Maynard Keynes and Economic Downturn: The state must act responsibly to minimize the adverse effects and get the economy back on its feet.

Friedrich von Hayek: The free market should be allowed to run its course without state interference during an economic downturn.

2. The empirical evidence from our historical investigation:

The State and the Market in the Industrial Revolution in Great Britain: Taxes, public capital formation, national debt, and the size of government in industrializing Britain; the state and import substitution; the state and the growth of overseas markets for British entrepreneurs through imperialism of protection (1650-1850) and imperialism of free trade (1850-1950).


The State and the Market in China’s Industrialization: 1800-1900; 1949-1970; 1970 to the present.

The State and the Market in India’s Industrialization: 1857-1947; 1950-1980; 1990 to the present.


4. As stated in the course outline, this course is an introduction to the all-important debate on the role of the state and that of the unfettered free market in socioeconomic development. I hope the issues discussed and the way they were discussed have been worth your time and effort. I thank you all for your effort and perseverance.
Recommended Further Readings Placed on Print Reserve


