

BOOK REVIEWS

Chi-Yuen Wu's Review of Gottfried von Haberler's *The Theory of International Trade*

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Translator's Note

This review of Gottfried von Haberler's *The Theory of International Trade* was originally published in 1937 in *Shehui kexue (Social Sciences)*, a leading academic journal in early twentieth-century China (Wu 1937). Founded by Tsinghua University in 1935, the journal published fifteen issues in six volumes between 1935 and 1950, featuring research by some of China's most distinguished social scientists. In 2019, the School of Social Sciences at Tsinghua University relaunched the publication under the new title *Qinghua shehui kexue (Tsinghua Journal of Social Sciences)*.

Before beginning his studies at the London School of Economics, Chi-Yuen Wu had studied economics at Tsinghua University. At the time this review was published in 1937, Wu had just finished his doctoral dissertation, published two years later as *An Outline of International Price Theory* (Wu 1939), under the supervision of Lionel Robbins. The dissertation would later earn praise from notable economists such as Gottfried Haberler and Murray Rothbard.

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The Theory of International Trade with Its Applications to Commercial Policy

Gottfried von Haberler

Translated by Alfred Stonier and Frederic Benham

William Hodge, 1936; xvi + 408 pp.

Bertil Ohlin and Haberler are the two leading authorities on the contemporary marginalist school's theory of international trade. Fortunately for those unable to read German or Swedish, their theories have subsequently been published in English. Ohlin's theory can be found in his representative work, *Interregional and International Trade*. Haberler's views are presented in this book, *The Theory of International Trade*. The book was originally published in German in 1933 and quickly became a very popular textbook

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on international trade theory in continental Europe. It was only recently translated into English by Stonier and Benham of the London School of Economics. The translators are very learned, their English is fluent, and there are very few errors. Furthermore, the English edition has been revised and expanded by the author based on the original, resulting in an improvement over the German version in some respects. Consequently, both the original and the translation are worth introducing here.

The scope of this book can be divided into three parts: (1) various theoretical issues of international money and finance; (2) the pure theory of international trade; and (3) international commercial policy. Regarding (1), the author focuses on the two major issues of foreign exchange and the balance of international payments. Regarding the issue of foreign exchange, he believes that both the balance of payments theory and the purchasing power parity theory have their respective advantages and disadvantages. He first points out that when the balance of payments is in equilibrium, the foreign exchange rate must be at its equilibrium point (14). However, when using the balance of payments situation to explain the exchange rate, we must not view these items as fixed amounts, but rather as variables that are functions of the exchange rate. In other words, we should interpret the international receipt items as the supply curve of foreign exchange, not the “quantity supplied.” Similarly, international payment items should be interpreted as the demand curve for foreign exchange. Then, the exchange rate is determined at the point of intersection between the supply and demand curves (19ff.). This reviewer completely agrees with the author’s revision of the balance of payments theory in this regard. However, the author goes a step further and offers a comment on this revised balance of payments theory which the reviewer considers to be erroneous: “The balance of payments is partially dependent on the exchanges; it cannot, therefore, be used to explain them” (31).

This means that the balance of payments is partly determined by the exchange rate, and therefore cannot be used to explain the exchange rate. This statement is equivalent to saying “‘Supply and demand’ depend on price; therefore they cannot be used to explain price.” Clearly, this is incorrect. Haberler’s mistaken view stems from a failure to distinguish clearly between the two different meanings of supply or demand—that is, a failure to understand the difference between supply or demand curves and the quantity supplied or demanded. The quantity supplied or demanded is indeed a function of price and cannot be used to explain price. But supply and demand curves are different. The supply and demand curves themselves represent the functional relationship between the exchange rate and the quantity supplied or demanded; we cannot say that they are determined by price. Therefore, we cannot say that supply and demand curves cannot be used to explain price. Since the author was able to view the balance of payments as the supply and demand curves for foreign exchange, and

the exchange rate as a type of price, he should not have passed the aforementioned judgment on the exchange rate theory of the balance of payments theory. Because the author fell into this error, this book has a major shortcoming—namely that he failed to truly reconcile the balance of payments theory with the purchasing power parity theory, nor did he clarify the relationship between the exchange rate problem and the problem of equilibrium in the balance of payments.

His discussion of the purchasing power parity theory of exchange rates is quite correct. Like other contemporary authorities, he believes that the purchasing power parity theory can only be used to explain changes in the exchange rate, but cannot be used to explain the determination of the absolute level of exchange.

Regarding the issue of equilibrium of international payments, Haberler focuses on the transfer problem. The so-called transfer problem refers to the problem of how to transfer an international debt from the debtor country to the creditor country. This problem actually has two aspects: (1) the monetary transfer; and (2) the commodity transfer. The author almost completely ignores the former aspect. Regarding the latter aspect, his stance is synthetic. He acknowledges that both the orthodox theory of transfer and Ohlin's theory of transfer contain a portion of the truth; therefore, he advocates reconciling these two theories to form a more complete doctrine.

His most important contribution lies in the pure theory of international trade: he revises the comparative cost doctrine into an opportunity cost doctrine. Suppose there are two countries, A and B. In country A, one unit of labor produces twenty units of commodity X or fifteen units of commodity Y . In country B, one unit of labor produces sixteen X or eight Y . According to the comparative cost doctrine, country A should produce Y and country B should produce X . But we can also explain this using the opportunity cost doctrine: In country A, the opportunity cost of X is $0.75Y$; in country B, it is $0.5Y$. Therefore, the opportunity cost of commodity X is lower in country B than in country A, so country B produces X . Generally speaking, each trading country should produce those commodities for which its opportunity cost is lower than that of other countries (582). Transforming the comparative cost doctrine into the opportunity cost doctrine in this way can reduce or eliminate the connection between the comparative cost doctrine and the labor theory of value. In other words, the validity of the comparative cost doctrine is not shaken by whether the labor theory of value is correct or erroneous.

Finally, in the section on international commercial policy, Haberler provides a theoretical basis for liberalism. From this perspective, we can say that this book is the most important work on liberal international trade theory since Taussig.



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