

Mercantilism

- 16th – 18th C
- Economics as applied statecraft
- Promotion of National wealth and power
- Wealth as gold or “treasure”
- Importance of trade surpluses
- Trade surplus leads to a net gold inflow, and thereby to greater national wealth and power
- Analogy between nations and households
- Encourage domestic production and exports, discourage imports
- Trade as a zero sum game

Some Mercantilist Programs—Von Hornick

- Von Hornick: *Austria Over All, If Only She Will* (1684)
 - Full use of all land and natural resources for domestic industry
 - Large working population
 - Finish raw materials at home, as finished goods have a higher value
 - Discouragement of imports, and no imports where domestic supply is available
 - Imports be confined to raw materials to be finished at home

Von Hornick

- Prohibition of all bullion exports (bullionist position)
- Necessary imports be obtained in exchange for domestic goods, not gold or silver
- Sell surplus manufactures to foreigners, if possible for gold and silver
- Hornick very influential in Austria

Mercantilist Programs— Thomas Mun

- Thomas Mun: *England's Treasure by Foreign Trade* (1664)
 - Importance of trade and the social position of the merchant
 - Bring all unused land into production
 - Fully utilize natural resources including fisheries
 - Reduce consumption of imports, particularly luxuries
 - Export goods with inelastic demand—can charge higher prices

Thomas Mun

- Customs duties on imports to be consumed domestically
- Export in own ships
- Encourage distant trade
- make England a trans-shipment point
- Export of bullion permitted, if for purposes of trade (non-bullionist position)
- “Make the most we can of our own”

Mercantilist Policies

- France
 - Colbert (1619-1683), economic advisor to Louis XIV
 - Encouragement of French manufacturing industry, particularly luxury goods
 - Subsidies to industry and provision of infrastructure
 - Detailed control of production methods and standards
 - Encouragement of population and restrictions on emigration
 - Colonies

Mercantilist Policies

- England
 - Navigation acts (1651-1673)
 - Protective tariffs and import prohibitions
 - Restrictions on the export of raw materials
 - Reservation of the Colonial market
 - Monopoly trading companies

Mercantilism and Monetary Theory

- Early realization of a link between gold inflows and increased price levels (Jean Bodin)
- Anticipation of what would now be called the quantity theory of money:
 $MV=PT$
- Link between M and P well understood
- Sometimes suggested that increases in M could “quicken trade”
- Keynesian interpretation of mercantilism

Mercantilist Monetary Theory

- Balance of trade surplus leads to a gold inflow that increases money supply and domestic prices
- Locke—process is reinforcing
- Hume—Specie-flow mechanism: balance of trade surplus leads to a specie inflow and increase of domestic prices. This will lead to lower exports and higher imports until a balance of trade equilibrium is reached (assumes full employment)
- Mercantilist policy is self defeating

Critics of Mercantilism

- David Hume: specie-flow mechanism and emphasis on trade restrictions as restricting innovation
- Physiocrats
 - importance of agriculture
 - Laissez-faire policy
- Adam Smith
 - Artificial stimulation of manufacturing and trade (misallocation of resources)
 - International specialization and *mutual gains from trade*

Main Points of Mercantilism

- Economics as statecraft not analysis
- Tendency to see gold and “treasure” as constituting national wealth
- Emphasis on balance of trade surpluses
- Emphasis on maximizing productivity and output
- Bullionist and non-bullionist positions
- Trade as a zero sum game
- Role of government in encouraging domestic manufacturing and exports while minimizing imports
- Link between money supply and prices