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
- Customs duties on imports to be consumed domestically
- Export in own ships
- Encourage distant trade
- Make England a transshipment 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