

EC120 The World Economy in Historical Perspective

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Question 2: Discuss the effectiveness of the main Mercantilist commercial policies adopted in the Dutch republic and Britain in the 17th and 18th centuries. Hence, explain and assess Findlay and O'Rourke's claim that "Most of the rivalries of the age of mercantilism were about which national company could gain control of a given market or trading area ...".

Mercantilism

From the sixteenth to the eighteenth centuries, mercantilism dominated European politics and the economy. ("Mercantilism" comes from the Latin word "mercari," which means "to trade.") Mercantilists used particular economic strategies to increase the authority and wealth of their countries. The fundamental concept of mercantilist philosophy was that the quantity of precious metals, particularly gold and silver, a country possessed determined how prosperous it was, as they were perceived as stores of wealth. The main goal was to create a positive trade balance, therefore, selling more commodities than they imported, which would result in the accumulation of precious metals. The emphasis on building wealth via a favorable trade balance evolved into a fundamental component of mercantilist thought. As a result, countries felt the need to introduce certain policies and intervene in the economy in order to protect their domestic cooperations and achieve a favourable balance of trade (LaHaye, 2018).

Mercantilist Commercial Policies

Imposing high tariffs on foreign produced goods was one of the main policies implemented by European Governments from the 16th to 18th century. This measure was introduced in order to protect their local industry from foreign competition and, therefore, encourage consumers to buy from their local producers. In addition, governments heavily granted subsidies to their local industry, in the form of lower interest rates or direct financial contribution. These subsidies were granted especially to those industries which contributed to their national defence. This was of high importance, as war was a common theme during that time and, therefore, nations wanted to increase their independence in those sectors particularly. Lastly, exclusive trading rights for national companies in combination with colonialism was a recurrent policy used. As previously mentioned, the importance of certain precious metals was of the utmost importance, but most countries did not possess any gold or silver mines themselves. Therefore, in order to acquire precious metals, nations attempted to attain them from their colonies. Although this may have profited the mother country, it came at the cost of the colonies themselves, as they often suffered a great deal because of their occupants.

Mercantilism in Europe

Although this paper will focus on mercantilism in the Dutch republic and Britain in the 17th and 18th century, it is important to point out that they were not the only countries that made use of mercantilist policies during that time, as it was common that one nation's mercantilist actions incited comparable actions in another country. The commercial and industrial history of France provides the most noteworthy example of the resolute application of mercantilist principles, if we equally consider its essential features and its influence on the economic policy of other countries (Horrocks, 2017). One politician who had significant impact on the nation's mercantilist strategy was Jean-Baptiste Colbert, in the position of chief minister of France. His main goal was to transform France into a self-sufficient state and to create

independence from outside influences. He employed techniques and policies which had been introduced by policy makers before him, however, he applied them with extraordinary ruthlessness. Colbert sought to construct a comprehensive system of industrial and commercial supervision. On the one hand, he concentrated on encouraging fiscal unification, granting subsidies to manufactures and reducing tariffs within the kingdom. On the other hand, he proposed high tariffs specifically to imported manufactured goods. Although his policies seemed to have a positive affect on the French economy at first, the industry could not maintain that level for a significant amount of time and later decayed at the cost of the earlier success. (Horrocks, 2017).

Foundation and Operation of the EIC and VOC

As previously discussed, the creation of state-sponsored monopolies in the form of national companies was a frequently used tool for European governments during the time of mercantilism. However, why did governments choose to follow this path? Monopoly was popular because it increased tax income of the monarchy, which was seen as a source of emergency loans, and support for foreign and domestic governance. There is a claim that monopolies were also chosen because they were more efficient for directors and staff in light of the volatile Asian trading climate and the difficulties associated with corporate governance in a time of inadequate communication (Bogart, 2016).

The British government felt the need to found several national companies, such as the Hudson's Bay Company or Royal African Company, but perhaps one of the most influential example of this was the East India Company (EIC). It was founded on the 31st of December in 1600 during the rule of Queen Elizabeth I, with the main goal of establishing trade with East and Southeast Asia, as well as India. However, the British were not the only country with an important national company. In 1602, two years after the foundation of the EIC in 1600, the states general of the Netherlands founded the „Verenigde Oostindische Compagnie“ (VOC), as a consortium of rich merchants (Gelderblom, 2013). The VOC and EIC soon established themselves as the main competitors for land and resources, not shying away from the use of force between them and also towards the native inhabitants of the land. Trade was focused on several different items which possessed high value in comparison to their weight, such as tobacco and spices from India, as well as silver, sugar or tea from China. The voyage first started in 1601 when the EIC began their exploration to the East Indies. After setting up several trading posts in different cities, such as in the city of Surat, the Madras was used as a major trading center in 1639. The VOC also established permanent settlements in the East Indies, precisely speaking at Bantam on Java in 1605, as well as in current day Jakarta. After the capturing of this city, it was used as the main base of trade for the VOC in the East Indies (Gelderblom, 2013).

The long-distance voyages required an immense amount of financial capital and it is, therefore, important to analyze the financial structure of the EIC and VOC, as their implementations could be considered ground-breaking during that time. The VOC was founded in the form of a joint-stock ownership. This implied that investors, such as merchants or the public, were able to purchase shares of the VOC and, therefore, partake in the companies profits and losses. The EIC followed a similar structure, however, the VOC was more innovative in certain areas. For example, the Dutch national company possessed a permanent capital, limited liability for owners and managers, as well as transferable shares by the early 1620s, while the EIC only introduced comparable features in the 1650s (Gelderblom, 2013). It can, consequently

be said, that the VOC built the foundations in the aspect of financing the companies activities, which the EIC later adapted.

Mercantilist Policies

When assessing mercantilist policies, it is important to comprehend the situation prior to the applied policies. Looking at the merchant fleet capacity in 1570, the Netherlands had a capacity over 4 times as high as the British, with it being 232.000 metric tonnes compared to 51.000 (Vogel, 1915). When talking about mercantilist policies introduced by the British government, one can not exclude the so called „Navigation Acts“. First introduced in 1651 by the British politician Oliver Cromwell, these Navigation Acts only allowed goods to be imported into England or their territories from English ships or ships of the country of origin of the imported goods. Furthermore, certain products, such as sugar or tobacco, which were found in English colonies, first had to be imported into England before they could be exported into different countries. (Horrocks, 2017). The objective of the navigation acts was, therefore, clearly to exclude other European competitors, such as the Dutch, from these trades and gain advantages over their industries. To no surprise, the British monarchy, as well as the British citizens which partook in the sea-trade, were the ones who benefited massively from these measures at first. As a result of this mercantilistic policy, the English tax revenue increased steadily from the early sixteen-hundreds up to the early eighteen-hundreds (Findlay, R., & O'Rourke, 2007). The money generated was ultimately used to fund their navy, which increased the competition with other European countries, such as the Netherlands.

The Netherlands did not implement Navigation Acts themselves, however, they did apply common mercantilistic policies, which were discussed in the beginning of the essay, in order to protect their own shipping interests. Examples for this would be the ban of imports of French brandy and raising tariffs on silk and linen. This was their response to the French increasing tariffs on the majority of Dutch goods, such as fine woolen cloth, sugar or whale oil (Findlay, R., & O'Rourke, 2007). Same as for the British, the implemented tariffs & quotas resulted in an increased level of tax revenue, which was used for their navy, as well as the VOC. The introduced policies also proved effective for a major part of the population who worked in the industry, such as sailors or shipbuilders. It resulted in the Netherlands being a very dominant force in Europe during the early 17th century,

Inspecting the data 200 years later in 1780, Britain had increased to 1.000.000 million metric tonnes in their merchant fleets capacity, while the Netherlands only increased to 450.000 million metric tonnes (de Vries, 1997). This is only one indicator of the general trend, which was that the mercantilistic policies introduced by both countries were mostly effective in the short term. However, it caught up to them in the end, with Britain having success for a longer time-period than the Netherlands.

Explanation and Assessment of Findlay and O'Rourke's claim

Findlay and O'Rourke's claim that „Most of the rivalries of the age of mercantilism were about which national company could gain control of a given market or trading area ...“. Having complete control over a certain area meant the exclusion of other states, which was important for the acting governments due to a very certain belief. Countries perceived international trade to be a so called „Zero Sum Game“. This believe implies that the total wealth of the all nations combined would stay constant. Therefore, if one country is to receive any economic gains, this would come at the cost of another country's economic loss. Net change in

wealth would always be equal to zero. The now common economic idea that trade can also be a positive-sum game, which would benefit both countries who are participating in the trade, was not taken into consideration. This explains the actions taken by the European Governments in the East Indies and the wars that occurred in these the regions

Findlay and O'Rourke's can also be explained by the concept of rent seeking. Competition is a major influence for the prices of any given product. As current economic theory states, in a market with perfect competition, companies would continuously undercut each other in the seek of a larger market share. As a final result, a product could only be sold at the marginal price of the product and individual businesses are forced to accept the price that the market sets for their goods, making them price takers.. This results in the company not being able to create any profits. However, this principle does not apply to the founded national companies which were granted a monopoly right for certain products. This privilege allowed them to set prices to their liking, as the products could only be acquired from them. In every instance, the outcome is that businesses and persons in favor receive "rents," or payments in excess of what is often expected in free markets (Bogart, 2016). The results of the creation of monopolies are not favourable to the general population, as this results in a severe welfare loss, the so call „deadweight loss“. In addition, the national companies were in desperate need of the created „rents“, as they were necessary in order for them to even maintain their monopolistic position. The many wars fought over the different markets were financed by the created profits of the monopoly. However, this setup did not turn out to be sustainable in the long run. Many national companies, such as the VOC, suffered under cash constraints due to severe military and operational spending. Immense expenditures for war ultimately led to the downfall of the system, as they exceeded the profits of the national monopolies and trade (Horrocks, 2017). Looking back at the statement written by Findlay and O'Rourke, it becomes clear that it very much captures the main aspects of the mercantilistic era.

Conclusion

In conclusion, European politics and economies were significantly impacted by the mercantilist era, which lasted from the sixteenth to the eighteenth centuries. Driven by the belief that the accumulation of precious metals determined national prosperity, mercantilist policies shaped economic strategies such as imposing tariffs, subsidizing local industries, and establishing colonial monopolies exemplified by the East India Company (EIC) and Dutch East India Company (VOC). These policies were motivated by the belief that the accumulation of precious metals determined national prosperity. Although the applied policies did not always result in a positive outcome, the era created the pathway for today's economic system.

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