3

Mercantilism

Institutional changes underway in Westem Europe by the beginning of the sixteenth century led to the decline of feudalism and the rise of an alternate set of socioeconomic institutions. The new era was distinguished by the emergence of stronger, more centralized nation-states and was encouraged and supported by a new doctrine. The term *mercantilism* is applied to the doctrine or policy that the economic interests of the nation as a whole are more important than those of individuals or parts of the nation; that a preponderance of exports over imports, with a corresponding accumulation of bullion, is desirable; and that agriculture, industry, and commerce should be directed toward this end. It was a policy that, not surprisingly, allowed the emergent nation-states to flex their newfound economic muscles.

By the nineteenth century, however, the intellectual and institutional environment had changed again to allow much more individual freedom and much less concentration of economic and political power. The term *capitalism* (coined by its chief antagonist, Karl Marx) carne into use to describe the more decentralized economic organization of this new era. Thus, mercantilism refers to an intervening period between feudalism and economic liberalism. It describes an economic creed that prevailed at the dawn of capitalism, before the Industrial Revolution took hold.

There are two basic ways to analyze the economics of the system of thought called mercantilism. One way considers mercantilism to be a fairly cohesive, "static" set of ideas-that is, a body of thought summarized in the events of the day. We call this the *doctrinal* approach. Another approach sees mercantilism as an important historical process. It concentrates on the dynamics of competing interests and their role in defining economic and political institutions. We call this the *process* approach. Both approaches view mercantilism as a system of power, but the former features a set of distinctly mercantilist propositions, or "central tendencies," that characterize the thought of the age. In this approach, the propositions of mercantilism presumably withered away as mercantilism eventually was replaced by a competing set of ideas. The doctrinal approach suggests that humans and their ideas may be arranged on a continuum with "mercantile" at one extreme and "liberal" at the other. By contrast, the policy view spotlights those self-interested forces in the economic system that generate changes in power and wealth. It concentrates on the specific regulations of the mercantilist period and how each affected the competing groups of interests held by the monarch, parliament, courts, and producers. Compared to the doctrinal, or ideational, approach it emphasizes permanence because it assumes that the driving force of individual behavior in the mercantilist period is the sarne as the driving force of contemporary capitalism, namely, the self-interested pursuit of gain.

Despite a tendency to view these two approaches as rival theories, there is no reason why they cannot be treated as complementary. It is likely that our most complete understanding of mercantilism will come through the application of both approaches. For pedagogic reasons, however, we treat them separately in this chapter.

MERCANTILISM AS DOCTRINE: THE ECONOMICS OF NATIONALISM

The term *mercantilism* was coined by Mirabeau in 1763 to describe that loose system of economic ideas that dominated economic discourse from the beginning of the sixteenth century to almost the end of the eighteenth century. Mercantilist writers were a disparate group. Many of them were merchants who simply espoused their own interests. Despite its international scope-mercantilism was a creed shared by England, Holland, Spain, France, Germany, Flanders, and Scandinavia-there was less consistency and continuity among mercantilists than among the Scholastics of the previous age. This lack of cohesion among mercantilist writers may be due to the absence of common analytical tools that could be shared and passed on to a generation of successors. Moreover, communication among mercantilists was poor or nonexistent, in contrast to the strong network of interrelations among modem economists. Nevertheless, mercantilism was based on several unifying ideas-doctrines and policy pronouncements that appear and reappear throughout the period.

An early, condensed summary of mercantilist principies was provided by Philipp Wilhelm von Hornick, an Austrian lawyer who published a nine-point mercantilist manifesto in 1684. Von Hornick's blueprint for national eminence emphasizes independence and treasure. Not all mercantilists accepted every point in von Hornick's program, but his nine points are sufficiently representative of the loose system of ideas that has come to be known as mercantilism.

Von Hornick's nine principal rules of national economy are:

1. That every inch of a country's soil be utilized for agriculture, mining, or manufacturing
2. That all raw materials found in a country be used in domestic manufacture, since finished goods have a higher value than raw materials
3. That a large, working population be encouraged
4. That all export of gold and silver be prohibited and all domestic money be kept in circulation
5. That all imports of foreign goods be discouraged as much as possible
6. That where certain imports are indispensable they be obtained at firsthand, in exchange for other domestic goods instead of gold and silver
7. That as much as possible, imports be confined to raw materials that can be finished at home
8. That opportunities be constantly sought for selling a country's surplus manufactures to foreigners, so far as necessary, for gold and silver
9. That no importation be allowed if such goods are sufficiently and suitably supplied at home

ln the discussion that follows, we shall be concerned primarily with the general nature of these premises rather than with their elaboration by specific individuals. Readers should be mindful of the fact that the resulting characterization is a *simpli-*

fication and an idealization that may not apply specifically to any single mercantile nation. British, French, Dutch, and Spanish mercantilism differed in many essential respects, for instance. This disclaimer applies even more to individuals, a fact that may be easily verified by reading and comparing the writings of at least two mercanWists. (Some of the references provided at the end of this chapter may be consulted to that end.) No single individual held ali the ideas that are expressed below as representing mercantilist thought, and what follows is only one of a number of possible characterizations of mercanWist ideas. The mercantilist period was one during which the threads of many ideas were being spun; as a consequence mercantilism as a set of ideas remains something of a patchwork quilt.

We will focus attention on severa! areas of interest: "real-world" ideas, views on international trade and finance, and examples of "dualism" in domestic policy. After an assessment of mercanWist ideas, we consider the historical process of mercanW-ism and its eventual role in the emergence of liberalism.

The Mercantilists and Real-World Ideas

Unlike writers from the feudal period, mercantilist writers showed less concern for moral issues (e.g., justice and salvation) and more concern for secular matters (e.g., wealth and power). On some issues a few writers of the mercantilist period looked backward, whereas others looked forward to laissez-faire, but en masse they were concerned with material, objective economic means and ends. And although their overall social goal of "state power" was subjective, their opinions on the workings of the economic system were a clear reflection of real-world habits of thought.

We have seen that the Scholastics built on the precept of divine law. As a rule, mercantilists rejected divine law in favor of natural law. Sir William Petty (see chapter 4), a trained physician, illustrated how conclusions about economic behavior could be drawn from analogies with natural sciences. ln his best-known economic treatise, *Political Arithmetick,* Petty noted that:

> We must consider in general, that as wiser Physicians tamper not excessively with their Patients, rather observing and complying with the motions of nature, than contradicting it with vehement Administrations of their own: so in Politicks and Oeconomicks the sarne must be used. *(Economic Writings,* I, p. 60)

Though Petty wrote late in the mercantilist period, theories of social causation grounded in natural law appeared as early as the mid-sixteenth century. The idea of natural law grew into a fundamental tenet of the economic liberalism of the eighteenth century, providing, in one important respect, an almost seamless transition away from earlier preoccupation with the divine. As Eli Heckscher, a recognized authority on the period, emphasized: "There was little mysticism in the arguments of the mercantilists ... they did not appeal to sentiment, but were obviously anxious to find reasonable grounds for every position they adopted" *(Mercantilism,* II, p. 308).

International Trade

These real-world concerns of the mercantilists were reflected in their intense focus on the material gain of the state. They saw society's material resources as a means to achieve the goals of national enrichment and well-being. They insisted that the nation's resources be used in such a way as to make the state as powerful as possible both politically and economically. Following the Age of Exploration, the sixteenth and seventeenth centuries witnessed the rise of great trading nations, as nation-states used exploration, discovety, and colonization to build power and influence. The major topic considered by mercantilist writers was, understandably, international trade and finance. Gold, and means to acquire it, was never far from the center of their concerns.

The Role of Money and Trade in Mercantilism. Money and its accumulation were prime concerns of the growing nation-states of the mercantilist era, because treasure was seen as a necessaty element of national power. As already noted, a flourishing international trade followed the age of discovety and colonization, and gold bullion was the unit of intemational account. The acquisition of gold through trade and trade restrictions of many types were essential mercantilist ideas, and money, not real goods, was commonly equated to wealth.

Production and trade are vital steps to increased prosperity. To mercantilists, however, prosperity in the sense of increased per-capita income was secondaty to the concentration of economic power in the hands of the state. National prosperity was to be accomplished through an export-import policy that led to a stockpiling of bullion. This stratagem, often referred to as "favorable balance-of-trade" policy, encouraged importation of (low-value) raw materials and exportation of (high-value) finished goods, thus assuring a net flow of money to the mercantilist countty.

All this might sound quite reasonable if the mercantilists had been rationalizing preexisting comparative advantages within trading nations, but the disappointing truth is that many of them looked on trade and bullion accumulation as a zero-sum game, where more for countcy A meant less for countries B, C, and so forth. They did not appear to understand that increased total output and appropriate (dual) gains from trade might accrue simultaneously to trading partners. Given this zero-sum mentality, protectionism and "beggar-thy-neighbor" policies were justified as a means to increase national wealth, which would, in tum, increase national power and prestige.

Intemational Trade and Specie Flow. Some writers, such as Gerard de Malynes (1586-1623), were confirmed bullionists, opposed to any export of specie (i.e., gold/silver coins) whatsoever. He condemned the practice of specie export by the East India Company, which was the leading avenue of Britain's trade with the East in the early seventeenth centuty. Although he had previously taken Malynes's position, Edward Misselden (1608-1654) attacked the extreme bullionist view, which amounted to an absolute prohibition of specie export even on individual transactions. Instead, Misselden advanced the notion that govemmental policies should be directed to maximizing specie eamings on the basis of an overall balance of trade.

However contradictoty and misdirected their orientation toward money seems to have been, the mercantilists produced the first real awareness of the monetary and political importance of international trade and, in the process, supplied a framework for international settlements that included both visible (products) and invisible (shipping expenses, insurance, etc.) items. ln the course of attacking the bullionists, for example, Misselden developed the fairly sophisticated concept of a trade balance couched in terms of debits and credits. ln *The Circle of Commerce* (1623), he actually calculated a balance of trade for England (from Christmas 1621 to Christmas 1622). He concluded, with disappointment, that it was a bad year.

> We see it to our griefe, that wee are fallen into a great Underballance of Trade with other Nations. Wee felt it before in sense; but now we know it by science: wee found it before in operation; but now we see it in speculation: Trade alas, faile's and faint's, and we in it. (Circle *of Commerce,* p. 46)

Misselden wished to emphasize the "scientific" nature of his calculations, and it is this fact, rather than the accuracy of his data, that sets his accounting apart from the mere collection of numbers, a practice that was widespread in early Egypt and Mesopotamia. Misselden arranged data for the purpose of understanding economic effects and promoting social ends, a more productive enterprise in a scientific sense.

One of the anomalies in mercantilist literature is the pervasive belief that wealth would be maximized through specie accumulation resulting from a trade surplus. Many mercantilists misunderstood the effects of an increase in the domestic money supply (monetization) that usually followed a trade surplus. One common error was the persistent belief that a favorable balance of trade--and thus specie accumulation-could continue over long and indefinite periods without adverse consequences. This error was fully exposed by David Hume **(1711-1776),** the philosopher-economist contemporary of Adam Smith. He identified a price-specie flow mechanism that linked the quantity of money in an economy to its prices, and alterations in prices to balance-of-trade surpluses and deficits.

Hume's idea, like most good ideas, appears simple in retrospect. Imagine a surplus in England's balance of trade. As a result, gold flows into England, but if ali of the new gold is monetized (i.e., coined)-a distinct likelihood under a strict monetary gold standard-England's money stock increases in the sarne proportion. More money in circulation drives up domestic prices, including the prices of goods in the export sector of the economy, so that England's trading partners tend to buy fewer English goods in the face of higher prices. Faced with less money from the sale of exports, English consumers tend to buy fewer imports, so that in England the price of foreign goods falls relative to English goods. Foreign countries now buy fewer English goods and English consumers now buy more foreign goods. The result is to reverse the trade balance so that gold subsequently flows out of England and into the treasuries of its trading partners. ln this manner, any initial trade *imbalance* tends to correct itself; and the misguided attempt to accumulate gold indefinitely becomes self-defeating. Hume's analysis deprived mercantilism of a key tenet of its logical foundation.

Hume expressed a more enlightened, and underappreciated, view of money: "'Tis none of the wheels of trade: 'Tis the oi!," he wrote. Nevertheless Hume foresaw short-term salutary effects in the acquisition of specie. He wrote:

> ln my opinion, 'tis only in this interval or intermediate situation, betwixt the acquisition of money and rise of prices, that the increasing quantity of gold and silver is favorable to industry. When any quantity of money is imported into a nation, it is not at first disperst into many hands; but is confin'd to the coffers of a few persons, who imrnediately seek to employ it to the best advantage. ("Of Money," in *Writings on Economics,* p. 38)

Hume believed that money is a "veil" that obscures the real workings of the economic system, and whether a nation's stock of money is large or small is of no great consequence after its stock of money adjusts to changes in the levei of domestic prices.

The underlying principle behind Hume's specie-flow mechanism is the quantity theory of money, an idea anticipated by the political philosopher John Locke (1632-**1704).** The quantity theory of money poses a direct, predictable, and positive connection between the quantity of money in circulation and the domestic price level, such that increases in the money supply lead to increases in the price level. Most mercantilist writers, however, failed to understand the quantity theory of money. ln most early expressions, the "theory" is no more than a tautology affirming that a given increase in money (say, a doubling) produces a given increase (doubling) of the price level. A more sophisticated variant equates the money stock multiplied by velocity (the number of times money turns over per year) to the price level multiplied by the number of income-generative transactions per year. ln formulaic fashion, it is written as $MV = Py$. As a theory of the price level that identifies dependent variables (prices) and independent variables (money, velocity, and transactions), it is alternately expressed as $P = MV/y$ or, more generally, $P = f(M, V, y)$. When V and y are assumed to be constant, an increase in M leads to proportionate increases in P. Although this more sophisticated version did not appear until long after Locke and Hume (but see the discussion of Richard Cantillon in chapter 4), the mercantilists, to the detriment of their analysis, did not see even the simplest connection.

The Nation-State: Mercantilism as Domestic Policy

Many mercantilists feared the consequences of too much freedom, so they relied on the state to plan and control economic life. The list of policies specially designed to promote the interests of the nation-state was long and varied, consisting of many different regulations of the domestic and international economy. The domestic economy carne under less scrutiny than the international economy and was subject to varying degrees of control; some sectors were heavily regulated, some only lightly so. Similarly, taxation and subsidization of particular industries, and measures restricting entry, varied widely across markets.

It was common practice during the mercantilist era for the state to establish legal monopolies in the form of franchises and patents. A franchise granted exclusive trading rights to a particular merchant or league of merchants, such as the East lndia Company. Some franchises also received massive subsidies from the king. The effect of all of this was a "mixed" economy, but with the mix far less on the side of individual freedom than was the case during the first half of the nineteenth century in England or in the United States. Some historians have treated the mercantilists as mere individual merchants pleading their own narrow interests. ln a governing system in which the monarch controls virtually ali property rights, perhaps the only way for a merchant class to develop is by an alliance of power between the monarch and the merchant-capitalist. The monarch depended on the merchant's economic activity to build up his or her treasury while the merchant depended on the authority of the monarch to protect his or her economic interests. Use of the political process to secure monopoly gains was by no means confined to that era, however. The practice is what economists now call *rent seeking,* where "rent" refers to the profits that are attributable to the existence of monopoly rather than to competitive advantage. ln a later section, we shall probe more deeply into this particular idea as it relates to mercantilism.

' biguity" in Mercantile Policies. From the very beginning we find mercantilist writings that on the one hand extolled international economic controls for society's enrichment but on the other hand presented eloquent pleas for domestic noninterference. ln the doctrinal approach this dualism is somewhat of an embarrassment. At times, individual mercantilists could sound like impassioned economic liberals (in the nineteenth-century sense). An anonymous tract (attributed to John Hales) entitled *A Discourse on the Common Weal of This Realm of England* (1549) exhibited an early and prophetic distrust of the effe ctiveness of legislative controls in promoting society's welfare. Investigating the economic consequences of subdividing common land for individual ownership (i.e., the enclosure movement), the author argued that market forces are more efficient allocators of resources than government decree because profit provides the proper incentive to act. Underscoring the stupidity and futility of governmental regulation of grazing land, the author pointed out the difficulty of enacting such legislation (vested interests will inevitably arise to challenge it) and, if passed, the clifficulty of enforcing the legislation (those who seek profits will finda way to subvert the law by one means or another). Moreover, economic regulations are often defeated by "natural" responses. For example, government-imposed price controls invariably give rise to black markets, regardless of when enacted. If Hales was indeed the writer in question, he made it clear by the following statement that self-interest is both natural and powerful: "everie man naturally will follow that wherein he seeth most profit." According to A. F. Chalk, "This is surely a very dose approximation to Adam Smith's views concerning the self-interest motive in economic activity" ("Natural Law," p. 335).

The anonymous writer of 1549 was only one of many who advanced views during the mercantilist era advocating more liberal economic activity. Pleas for free interna! trade became increasingly vigorous as the mercantile system devolved, especially in the writings of John Locke, Sir Dudley North, Charles Davenant, and Bernard de Mandeville. The emerging "liberal" beliefs relating to domestic policy not only stand in strong contrast to adamant mercantilist views on externa! trade restrictions, they represent a harbinger of persuasive challenges to state-controlled economies that reached an apex in Adam Smith's *Wealth of Nations.* A sympathetic assessment of mercantilism maintains that "what had begun as opportunistic and sporaclic protests against commercial controls thus emerged, almost two centuries later, in the form of a systematized philosophy of economic individualism which proclaimed the beneficence of the laws of nature" (Chalk, "Natural Law," p. 347).

Labor and the "Utility of Poverty"

The interests of the moneyed merchant class and the landed aristocracy converged on the question of domestic policies toward labor and wages. Mercantilists considered the maintenance of low wages and a growing population as a means of national aggrandizement. The argument that labor should be kept at the margin of subsistence runs throughout the mercantilist age. ln his classic work, *The Position of the Laborer in a System of Nationalism,* Edgar Fumiss called it the "utility of poverty" argument. ln the extreme it is premised on a belief that "suffering is therapeutic" and that, given the opportunity, menial workers would be lazy and improvident. It was believed that the generally low moral conclition of the lower classes inclined them toward drunkenness and debauchery if wages were too high. ln other words, if wages were beyond subsistence, the quest for physical gratification would lead workers to excess, vice, and moral ruin. On the other hand, workers facing poverty because of the high price of subsistence and/or low wages would be encouraged toward industry, which meant that they "lived better." Reflecting the common attitude of the era, Arthur Young noted in bis *The Farmer's Tour Through the East of England* (1771): "Everyone but an idiot knows that the lower classes must be kept poor or they will never be industrious." The conventional wisdom of the day held that unemployment was simply the result of indolence.

Bernard de Mandeville (paradoxically, a "liberal" in other contexts) represents one extreme. He argued that children of the poor and orphans should not be given an education at public expense but should be put to work at an early age. Education ruins the "deserving poor," he argued, so that

> Reading, Writing and Arithmetick are very necessary to those whose Business requires such qualifications, but where People's livelihood has no dependence on these Arts, they are very pernicious to the Poor.... Going to School in comparison to Working is Idleness, and the longer Boys continue in this easy sort of Life, the more unfit they'll be ... for downright Labour, both as to Strength and Inclination. *(Fable of the Bees,* p. 311)

Various proposals were put forward to limit debauchery and to make the poor industrious. In 1701, John Law proposed a tax on consumption in order to encourage frugality among the rich and industriousness among the poor. David Hume, who contributed to the liberal movement in other respects, supported "moderate" taxes to encourage industry, but he thought that excessive taxes destroyed incentives and provoked despair. These writers seemed to be aiming at a real wage that would support an "optimal levei of frustration," one high enough to provide incentives for "luxuries" but low enough so that they could never be attained. As Furniss observed, it was of the utmost importance to mercantilist writers that

> the lowest ranks of the laboring classes be kept as full as possible, for upon the members of this group England relied for that economic power which was to bring her forth victorious from the struggle of nations after world supremacy. Thus, the nation's destiny was conditioned upon a numerous population of unskilled laborers, driven by the very competition of numbers to a life of constant industry at minimum wages: "submission" and "contentment" were useful characteristics for such a population and these characteristics could be fostered by a destruction of social ambition amongst its members. *(Position of the Laborer,* p. 150)

A Summary of Mercantilism as a System of Ideas. The major theoretical defects in mercantilist doctrine (always granting exceptions) were an inability to grasp the cyclical nature of intemational accounts and the linkage between domestic money supply and prices. In short, the mercantilists failed to integrate the Locke-Hume price-specie flow mechanism (or the quantity theory of money) into their analysis, which is ironic in view of their careful collation of trade statistics and systematic record keeping. Indeed, this penchant for assembling and keeping statistics on real-world quantities may well be the mercantilists' most important legacy to modem economics. Analytical insights in the mercantilist period, such as they were, sprang from careful empiricism. Mercantilists were among the first economic writers to be more concerned with actual experience than with metaphysical speculation. They brought economic questions to prominence, and in so doing, set the stage for advances made in the next period of economic thought.

In the meantime, economic processes within the mercantile economy (especially of England) were introducing institutional changes that taken together provide a cogent explanation for the historical rise and decline of mercantilism. This explanation pays little attention to what mercantilists said. It concentrates instead on what they did and why they did it.

■ MERCANTILISM AS AN ECONOMIC PROCESS

The doctrinal approach to mercantilism gives us insight into how certain writers reacted to their environment in formulating a national creed, but it implies that only nationalistic ends were appropriate to mercantilist policies. What we call the process approach seeks to explain why and how mercantilism arose when it did and why it eventually gave way to a distinctly different economic system. This latter approach examines the economic motivations of individuais or coalitions within a national economy. It focuses on the gains to economic agents of using the state in order to acquire profits. Such profits, in the vernacular of modem economics, are called rents (i.e., monopoly returns). Thus, mercantilism is presented here as a form of rent seeking. Rather than rationalize a body of thought, this process view focuses on the factors that motivated historicaI change.

Some Basic Concepts in the Modern Theory of Regulation

ln understanding the rise and fall of mercantilism, it is helpful to look forward for a mechanism to understand events of the past. Hence, a brief look at some contemporary ideas in the theory of economic regulation and politics is in arder (a fuller explanation is contained in chapter 24). The term "rent seeking," conveys self-interested behavior of any or ali parties to incarne distribution. When applied to the contemporary analysis of economic reguiation, the idea is that, in *their own interests,* politicians (members of Parliament, Congress, state legislators, city councilors, etc.) wilI *supply* government monopoly privileges and regulations to individual businesspeople or merchants or to any group whose self-interest leads it to *demand* regulation. This self-interested activity does not (necessariiy) mean that politicians wilI accept direct cash payments, although we shall see that such payments were far more common in the mercantilist era than they are today. The modem world involves more subtlety. Lobbyists can bestow favors on lawmakers outside of a strict cash nexus. Since most politicians are members of law firms, patronage via company retainer fees is a less obvious manner of accepting side payments. Contributions to electoral campaigns may be made at arm's-length from the candidate herself. Modem analysis seeks to explain the existence or absence of monopoiy privileges in some realms of economic activity by examining the costs and benefits to the *individuais* engaged.

The formal specification of costs and benefits need not concem us here, but a couple of examples might help to understand how the process view works as an explanation. Consider "industry representatives," or lobbyists, as potential demanders of regulation. Their demand for monopoly privileges from government (e.g., entry control and/or subsidies) would obviously be reiated to how much profit they, or their clients, could expect from the privileges. For example, anything increasing the uncertainty of the duration of a monopoly privilege would reduce the value of the monopoiy franchise to the industry. So would any costs imposed on the regulated firm (e.g., taxes and/or periodic inspections) as a quid pro quo for the franchise.

Now consider reguiation from the supplier's side. Contemporary economics tells us that self-interested politicians will maximize their benefits (e.g., reelection and/or side payments) by supplying regulation in retum for votes and/or money. People adversely affected by legislation face a major problem: the cost of organizing opposition. Large, diverse groups, such as retailers, may find it difficult to overcome the high costs of combining in order to establish an effective lobby. Small, narrow groups, such as undertakers, may find it easier to organize lobbying activities but may be unable to afford the expense of a successfuI lobby effort. The amount of reguiation politicians will offer depends on the costs and benefits of doing so, as well as the coalition and organization costs necessary to actually supply the regulation. Ordinarily the larger the group required to pass special-interest legislation, the higher the coalition costs.

From an analyticaI standpoint, regulation may be treated as a "good" that is supplied and demanded like other goods in more conventional markets. A decrease in the net benefit to those who stand to gain from reguiation would, other things being equal, lead to a reduction in the amount of regulation demanded. Likewise, an increase in the costs of supplying regulation-such as when the ability to supply regulation is transferred from a single indii dual (a monarch or dictator) to a group of individuals (a parliament or city council)-would, other things being equal, lead to a reduction in the supply of regulation.

In the mercantilist era, the prospect of obtaining a monopoly gave merchants a powerful incentive to seek regulation from the monarch. In this respect, the economic logic of mercantilism is the sarne as that driving much present-day politico-economic activity. Some groups (e.g., artisans then, telecommunications firms now) possess inherent organizational advantages in lobbying for state regulatory protection from competition (e.g., lobbying local justices of the peace responsible for enforcing the Statute of Artificers then, the Federal Communications Commission now) relative to other groups, such as consumers in general. Usually, then, the gains of successful interest groups consist of transfers of wealth from the consumers of regulated products to those who benefit from the regulations.

A particular kind of monopolistic actii ty takes place when firms combine to form a cartel, which is a formal combination of firms acting as a single monopolist under some form of central control. (OPEC, for example, is an international cartel run by the ministers of various oil-producing countries). Prices and/or output shares are ordinarily assigned to the members of the cartel, and their behavior is monitored or policed by an administrative board. Cartels may be privately or publicly organized, but in either case, strict entry controls are maintained. Private cartels are inherently unstable because there is a strong incentive to cheat on cartel price or output agreements if the cartel cannot be effectively policed. Most privately organized cartels are therefore unstable because enforcement is difficult. Cartels organized and/or sustained by governments, however, are more stable because govemments have inherent advantages in enforcement. One of the advantages is that the cost of enforcement can be shifted to taxpayers. In instances where enforcement costs are a major consideration, therefore, certain firms may willingly submit to specific regulations as an inexpensive way to organize themselves into a virtual cartel. By putting themselves under the protection of government these firms relinquish direct control over entry, prices, or profits, but the other side of the bargain is that they gain protection from competitors, enjoy lower costs of enforcement, and are often able to influence the nature and substance of the regulations imposed.

Whether analyzing the old mercantilism of monarchical Europe or its more sinister twin in contemporary democracies, economic regulation can be seen as the outcome of a competitive process whereby interest groups seek the state's protection against rival interests. In the mercantilist setting, the relevant interest groups were most often local administrators, merchants, and laborers in the domestic economy, and import/export firms the international economy.

Entrepreneurship: Productive and Unproductive

Putting the concept of entrepreneurship in historical perspective underscores the fragile nature of entrepreneurism within the pantheon of economic ideas because culture and institutions determine whether entrepreneurial efforts result in the *creation* of wealth or its mere *distribution* (what economists today call rent seeking). What we call the "competitive process" may be focused on gaining special privileges from a central authority, or organizing the production and sale of goods to gain consumers' favor. In either case it is driven by a human actor motivated by profit. We call this actor an enterpriser, or *entrepreneur.*

Most likely entrepreneurial activity is as old as human history. But entrepreneurship takes on different guises depending on institutional and cultural context. ln premarket societies property rights were concentrated in the hands of a tribal leader, and in Iater societies they were in the hands of the monarch. The nature of entrepreneurial activity conforms to the institutional makeup of society. Centralized authority and concentrated property rights give one form to entrepreneurship; highly dispersed property rights and highly developed markets give it another. Normatively speaking, enterprising behavior can be productive or unproductive. Unproductive entrepreneurship redistributes wealth but does not add to it; productive entrepreneurship adds to society's wealth.

William Baumol and Robert Strom remind us that unproductive entrepreneurship in bygone eras was a response to different institutional and cultural incentives:

> For much of buman history there was no guarantee tbat tbe individual whose efforts enhanced the magnitude of the pie would reap rewards. Indeed, history is replete with examples of tbe opposite, as monarchs readily expropriated the property of others. ln many cultures, the monarch theoretically owned everything, and in some societies, the king chose to transform this theory into reality quite often. Likelihood of expropriation is surely the ideal disincentive to productive effort. ("'Useful Knowledge' of Entrepreneurship," pp. 531-532)

ln an age that takes its name, mercantilism, from the growing pool of merchants who engaged in buying and selling activities throughout the Western world, it would be surprising to find a low levei of entrepreneurship. But what kind? The following hypothetical elaborates the issue within a mercantilist context.

Suppose a king or queen *gives* a grant to a favored courtier for the exclusive right to import and sell wine. The recipient will restrict output to what can be produced at the monopoly price, receiving monopoly profits (or rents) at the expense of consumers. One of the consequences of this action is that wealth is redistributed from consumers to suppliers. But suppose instead that the monarch puts the right to import and sell wine out for competitive bid. The winning bidder will be able to earn monopoly profits, but he will have to expend resources (lobbying the queen, engaging in legal pleadings, and so on) to obtain the right. ln this case consumers lose as before, but there is an additional loss of resources expended by the winning bidder (as well as the losers, too). This kind of entrepreneurial activity, namely competition to secure exclusive privilege rather than to produce and sell what consumers want at an attractive price, is called *rent seeking.* It constitutes unproductive entrepreneurial activity. It may include bribery, larceny, and other forms by which rents and special privileges are sought.

During antiquity, cultural attitudes and practices placed a low value on productive entrepreneurial activity. The Age of Exploration opened up vast new markets and allowed commerce to expand at an accelerating pace, which gave entrepreneurs, a conspicuous part of the practical makeup of mercantilist society, expanded opportunities to engage in productive entrepreneurship. The explorers and their backers took unprecedented risks in the search for and development of new markets and resources. If successful, they increased the wealth of society at the sarne time they secured profits for themselves. Naturally the rent-seeking mode of wealth production was still operative. Monarchs, for example, were lobbied for the exclusive rights to import particular goods (for example, tobacco or spices). But productive entrepreneurship was, slowly but surely, gaining a foothold. Productive entrepreneurship, practiced by individuals engaged in enterprising activities that require independence of thought and action geared toward the acquisition of wealth, power, and prestige, *adds* net value to society. The key point that cannot be stressed enough is that the direction of entrepreneurial activity, at any particular time and in any particular place, depends heavily on the prevailing institutional arrangements and relative payoffs to activities that promote or retard economic growth.

ln many societies today strong centralized governments have supplanted the monarchs of old. Not surprisingly, rent seeking is still commonplace. However, the cultural and institutional context is different than that associated with mercantilism. ln contemporary society unproductive entrepreneurship may be exercised by persons who employ novel approaches to opportunistic, criminal, or socially damaging activities-opportunists who, rather than expand the economic pie by creating more wealth, seek to grab a larger slice of the pie for themselves by redistributing existing wealth. Individuals who worm their way into the bribe-taking bureaucracy, or attorneys who foment novel, potentially lucrative lawsuits, provide ready examples. Lobbying of politicians for privileges by industry (energy, agricultural, pharmaceutical) is an example of so-called "corporate capitalism" or unproductive entrepreneurship.[1]

The mercantilist era marked a kind of passage from medievalism to modernism. During this transition old attitudes and institutions weakened and the venues for productive entrepreneurship expanded. However, until about the time of the British Industrial Revolution the prevailing institutions in most countries encouraged redistributive activity by enterprising individuais, chiefly through rent seeking. During and after capitalism took root the structure of payoffs began to change again, as we shall soon see, putting entrepreneurship in a more positive light.

Internai Regulation in English Mercantilism

Unproductive entrepreneurship and rent seeking permeated both internai and external commerce in England over the fifteenth and sixteenth centuries, continuing to a degree in later centuries. Economic regulation at all levels of government took basically the sarne form in English mercantilism as it does in contemporary societies. Governments granted licenses, thereby offering the favored few protection from competitors. Important differences existed, however, between the conduct of institutions involving *local* as opposed to *national* regulation and monopoly. Local regulation of trades, prices, and wages in mercantilist times was vested in the medieval guild system. Enforcement of guild regulations in the Tudor period prior to Elizabeth I (1485-1558) was the responsibility of the guild bureaucracy, in combination with the town or shire administrative machinery. Elizabeth attempted to codify and strengthen these detailed regulations in the Statute of Artificers, a law that outlined the specific enforcement duties of local justices of the peace (JPs), aldermen, and local administrators. JPs and other administrative enforcers of local regulations were paid either very little or not at all for these services, a fact that led to local alignments of economic interests. These interests ultimately rendered the local provision of monopoly rights ineffective.

At the national levei industrial regulation was created in three ways: (1) by statutes of Parliament, (2) by royal mandates, and (3) by decrees of the Privy Council of

[1] It must be noted tbat no type of entrepreneurship can take place without property rights establishment and enforcement-a central role of government in ali but the most primitive societies. This role extended into the establishment of military installations to protect the great trading companies, partly established by the Crown in England (for example, the Africa Company, East lndia Company, and so on).

the king's court. It should be noted that merchants and monarchs alike stood to gain from rent seeking. The meshing of private interests of monarch and monopolist was firmly enshrined in English comrnerce as early as the fourteenth century, perhaps even earlier. The nature of this alliance was underscored in debate on the issue of monopoly in the House of Commons in 1601:

> First, Let us consider the word monopoly, what it is; Mo *nos* is *Unus*, and *Polis, Civitas*: So then the Meaning of the Word is; a Restraint of any thing Publick, in a City or Common-Wealth, to a Private Use. And the User called a Monopolitan; *quasi, cujus privatum lucrum esturbis et orbis Commune Malun.* And we may well term this Man, The Whirlpool of the Prince's Profits. (Tawney and Power, Tudor *Economic Documents,* II, p. 270)

These revealing definitions of monopoly and the monopolist remind us that the motives of economic actors are usually recognizable and have not changed over the centuries. But it would be a mistake to carry the analogy too far. Although the basic nature of mercantilism then and now is the sarne, there are important differences in the two rent-seeking environments. The most important difference for the purposes of the discussion here concerns the supply side of the market for regulatory legislation.

Mercantilist regulations at the national levei were supplied by a single ruler, or monarch. Monarchy represents a uniquely low-cost opportunity for rent seeking, especially when compared with modem, democratic societies where the power to supply regulatory legislation is dispersed among various (sometimes conflicting) governmental powers. The consolidation of national power under the mercantile monarchies provides a logical explanation for the widespread rent seeking and economic regulation during this period of English history. We shall soon see how the growth and ultimate takeover of the power to supply regulatory legislation by Parliament dramatically altered the costs and benefits to buyers and sellers of monopoly rights in such a way as to lead to the decline of mercantilist regulation. But first we must consider the pattem and fate of local regulation.

The Enforcement of Local Economic Regulation

The legal framework for the enforcement of mercantilist economic regulation at the local level was set forth by the Elizabethan Statute of Artificers. This statute attempted to codify older rules for the regulation of industry, labor, and welfare, the important difference being that such regulations were to be national rather than local in scope. Some writers have pointed to the enormous increase in wages after the Black Death as the impetus to national regulation. The imrnediate economic reason was much more likely the inability of the towns to restrict cheating on local cartel arrangements. Towns petitioned the king to establish a nationally uniform system of regulation with the intent to protect local monopoly rights against encroachment, especially by outsiders. There were many attempts by self-interested merchants and town administrators to regulate economic activity and to prevent interlopers on local franchises. The city of London, especially, wished to restrict aliens and foreign technology that inhibited town profits. The solution most often proffered was to banish to the countryside aliens or those workers who did not meet "legal" qualifications for various trades. These sentiments are expressed in numerous Tudor documents.

The nationally uniform system of local monopolies was to be enforced by the JPs. In Eli Heckscher's words, "The Justices of the Peace were the agents of unified industrial legislation" *(Mercantilism,* I, p. 246). A primary feature of the system was that the JPs were not paid; and Heckscher argues that the absence of pay for the JPs led to lax enforcement through ineptitude and laziness. But it is more likely that low or no pay created a situation ripe for malfeasance by encouraging a self-interested pattern of enforcement--one suggesting both *sub rosa* activities and selective cartel enforcement of industries in which the JPs themselves had vested interests. Evidence suggests that the JPs' holdings in regulated enterprises increased as a consequence of the way the regulations were enforced. This could generally be accomplished either through preferential treatment-the firm in which a JP had an interest could be allowed to cheat on the cartel, while other firms could not-or through bribes made to minor enforcement personnel. The Queen's Council dictated that the JPs themselves be policed by high constables, who, having less civil authority than the JPs, were often on the receiving end of bribes. By the time of James I it was openly acknowledged that the JPs could be easily "bought." ln 1620, the following testimony was given before Parliament by a Committee of Grievances:

> There are some patents that in themselves are good and lawful, but abused by the patentees in the execution of them, who perform not the trust reposed in them from his maj [esty]; and of such a kind is the Patent for lnns, but those that have the execution abuse it by setting up lnns in forests and bye villages, only to harbour rogues and thieves; and such as the justices of peace of the shire, who best know where lnns are fittest to be, and who best deserve to have licenses for them, have suppressed from keeping of alehouses; *for nane is now refused, that will make a good composition* (Corbbett, *Parliamentary History,* pp. 1192-1193).

The reference to "a good composition" implied side payments by innkeepers in order to be granted licenses.

ln every age it is difficult to find accurate records of illegal transactions because there is no incentive to report them. ln the case of mercantilism, however, the testimony of contemporary observers seems to corroborate the view that the enforcers of internal mercantile regulations were self-interested parties. Thus, the claim that enforcers were indifferent and careless because they were not paid seems naive in retrospect. Modem economic theory leads us to *expect* malfeasance as the predictable response to low pay in occupations where an element of trust is dominant.[2] That is because the opportunity cost to the wrongdoer of being caught (and fired) is low. From this self-interested standpoint, the behavior of tbe JPs during the mercantilist era was quite efficient and predictable, given the constraints imposed by the Statute of Artificers.

Local Regulation and Resource Mobility. Another difficulty in enforcement of the Elizabethan system of local regulation is that those regulated could escape the jurisdiction of the law by moving outside the towns. Evidence exists that the rules were blatantly disregarded, despite attempts to limit mobility. Movement of artificers to the countryside was in fact blamed for the decay, impoverishment, and ruin of the cities (Tawney and Power, Tudor Economic Documents, I, pp. 353-365). As long as buyers and sellers could migrate to an unregulated sector in the suburbs and the countryside, the local cartel arrangements in the towns could be subverted. France, however, differed from England in this regard. According to Heckscher, "The most vital difference was that many important districts were set free from the application of the statutes in England, while in France notbing remained unregu-

[2] For example, see Gaiy Becker and G J. Stigler, "Law Enforcement, Malfeasance, and Compensation of Enforcers."

lated in principle, apart from purely accidental exceptions or subordinate points" (Mercantilism, I, p. 266). lt does not appear that the English countryside was "set free" in any conscious, deliberate act of policy. Instead economic resources merely responded to the incentives produced by a local pattern of enforcement pursued by the JPs. Movement out of the towns was simply a way for some artisans and merchants to lower their costs of operation.

Migration to escape local cartel regulations did not have to involve much distance. The suburbs of towns were filled with handicraftsmen who either could not get into the town guilds or wanted to escape their control. Because the nature of the trade involved was akin to that of a widely dispersed flea market, various efforts to bring these "cheaters" under control proved futile. Adam Smith illustrated this point nicely: "If you would have your work tolerably executed, it must be done in the suburbs where the workmen, having no exclusive privilege, have nothing but their character to depend upon, and you must then smuggle it into town as well as you can" (*The Wealth of Nations*, p. 313). Cheating on the local cartels thus became the economic order of the day, and the state's lack of success in dealing with enforcement problems is ample testimony to the inefficient nature of the Elizabethan cartel machinery.

Occasionally the crown struck back by creating institutional arrangements that made enforcement more efficient. For example, Elizabeth made a practice of granting to her favorite courtiers the right to collect fines for violations of the regulatory code. Eventually these rights carne to be sold to tbe highest bidder, the successful bidder keeping for himself whatever he could collect. Enforcement remained uneven, and a sizable unregulated sector of the economy persisted, however, because some infringements (e.g., patents) were more lucrative to collect on than others. ln the end the Statute of Artificers contained the seeds of its own destruction. The behavior of the unpaid or low-paid JPs and the ability of firms to escape regulation were the two major factors that helped undo *local* mercantilist regulation in the long run. We now tum to a consideration of the important part played by the mercantilist judiciary in the gradual demise of *national* economic regulation.

Toe Mercantilist Judiciary and the Breakdown of National Monopolies

ln a system of national regulations, the only way to escape legal jurisdiction is to leave the country, which is more difficult and more costly than moving from city to suburb. Thus, the absence of a viable, unregulated alternative brought about more stable cartel arrangements in national markets than in local ones. The undoing of the national monopolies must therefore be explained by other factors, namely the changing constraints on economic activity in mercantilist England.

English Common Law and the Courts. The English judiciary system developed slowly and intricately. Basically, three common law courts evolved in the period between the Norman invasion and the mercantile era: the Court of King's Bench, the Court of Common Pleas, and the Court of Exchequer. These courts presided over civil matters, and ali were initially under the crown's direct control, with the king often rendering decisions in the early period. During the thirteenth tbrough the fifteenth centuries the courts grew increasingly independent of the crown, although the king retained the power to appoint and remove judges.

Up to the time of the Tudors, jurisdiction between the three courts was undefined and payment of judges depended in part on the collection of court fees. This led to a great deal of jurisdictional competition between the courts. Moreover, the functional separation of the branches of government toward the end of the fourteenth century intensified the division of interests between the King's Council, the Court of King's Bench, and Parliament: The Council identified and allied with the executive branch of government (monarch), the King's Bench united with the judicial branch, and Parliament became a legislative body, but with some vestiges of a judiciary (the House of Lords remains the highest appellate court in England). The separation of governmental functions brought with it a self-interested alignment between the common law courts and Parliament. The common law courts recognized Parliament as the source of laws that the courts were charged to enforce. ln tum the many common lawyers in Parliament carne to believe that errors in the judiciary should be corrected by Parliament, not by the King's Council.

This alliance between the common law courts and Parliament began centuries before the mercantilist period, by which time the courts had cartelized and established firm bureaucracies and jurisdictions. By 1550 the coincidence of interests between the courts and Parliament had intensified, owing principally to the rise of a competing legal system in the form of the *royal* courts that were established by the time of Elizabeth I.

The competing judicial system emerged from a tradition in Roman law *(curia regis)* that regarded the powers of the crown as outside normal legal jurisdictions, therefore, outside the common law courts. These other courts became entrenched in branches ofthe Royal Council, its subordinate court (the Court of Star Chamber), and in other parts of the executive branch of government, such as, the Court of Chancery. *As* the Court of Chancery and the Court of Star Chamber extended their jurisdictions into that of the common law courts, they met with fierce resistance from the judicial "cartel." Persistent attacks by the common lawyers successfully destroyed one of the courts of Chancery (Maitland, *Selected Historical Essays,* p. 115), and the confrontation served to cement the alliance between the common law courts and Parliament. ln order for Parliament to enhance its power relative to the crown, it needed support for its legal actions, a support the common law courts were eager to provide. Besides its composition of individuais of similar training and interest, the common law courts were further drawn into Parliament's orbit because, inasmuch as the House of Commons could overturn any decision by a common law court, Parliament itself was regarded as simply another common law court. lnterdependence was further motivated by the fact that whereas Parliament could control jurisdictional boundaries and other matters before the courts, it was dependent on the courts for the permanence and security of its legislation. This intertwined, complex judicial system formed the backdrop against which national mercantilist regulations were enacted and applied.

Effects of Judicial Competition on the Durability of Monopoly Rights

Competition between the king's courts and the common law courts created uncertainty over the durability of a monopoly right granted by a single governmental authority because a monopoly right valid in one court would not necessarily be considered valid in another. Hence, the security of monopoly privilege depended on the shifting fortunes of each court system, because monopoly rights become less valuable as they become less certain, and durable attempts by the crown to establish monopoly privileges met with less and less success over time.

Example 1. On grounds of national defense, Queen Elizabeth claimed regalian rights to the production of saltpeter and gunpowder in the 1580s. She granted a monopoly right to manufacture these products to George and John Evlyn. The Evlyn farnily subsequently enjoyed lucrative benefits from rent splitting with the crown for almost fifty years, but persistent counteraction by other merchants and the common law courts finally brought down the monopoly privilege, after which the manufacture of both saltpeter and gunpowder became the object of open competition.

Example 2. Elizabeth tried to imitate the French king's successful and lucrative salt tax but did not meet with the sarne success. Five years after a patent monopoly in salt was established, the patentees abandoned their investment, leaving huge salt pans rusting on the English coast. Private capitalists without any exclusive privileges thereafter entered the industry and profitably produced and sold salt over the next three decades, despite repeated attempts by the crown to reestablish monopoly rights.

Example 3. ln 1588, a paper monopoly was granted to John Spilman, who claimed to have a new process for producing white paper. Ordinarily, patents issued to protect a new invention or process were unopposed by Parliament and the common law courts, but sometimes the patent was extended to enable its holders to "engulf" closely related products. Spilman gained this comprehensive benefit in 1597 when he was granted a monopoly over all kinds of paper manufactory. The monopoly proved impossible to enforce, however, and according to John Nef *(Industry and Government,* p. 106), within six years Spilman had to content himself with "such a share of the expanding market for papers as the efficiency of his machinery, the skill of bis workmen, and the situation of his mills enabled him to command." Elizabeth's luckless experiences with franchising and rent-seeking activities ended in 1603, when, beseeched to grant a monopoly of playing cards, she personally declared that such patents were contrary to common law. Nevertheless, her successors often made new attempts to supply various regulations.

Example 4. During the monarchy of James I (1603-1625), successor to Queen Elizabeth I, the House of Commons and the cornmon law courts consolidated their power and succeeded in blocking the establishment of enforceable, national monopolies that interfered with their interests or the profits of merchants aligned with them. This opposition to the crown's supposed right to supply regulation reached its zenith in 1624, when the celebrated Act Concerning Monopolies legally stripped the king of all means to monopolize industry.

Example 5. Upon the death of James I in 1625, his son, Charles I, ascended to the British throne and promptly tried to reassert regalian rights to grant monopoly by letters patent or by order of the Privy Council. With the aid of his powerful and persuasive minister, Sir Francis Bacon, he found a loophole in the 1624 statute and tried to make deals with large producers in many industries, particularly in alum and soap. Between 1629 and 1640 the alum patent brought in f:126,000 and the soap patent an additional f:122,000. King Charles's brazen move ultimately led to a head-to-head confrontation with Parliament and the constitutionalists, a battle that he ultimately lost, along with bis head, in 1649.

These examples demonstrate that the returns from seeking national monopolies through the state fell drastically in the sixteenth and early seventeenth centuries as the conflict between Parliament and the crown intensified. History is unclear whether the conflict itself was motivated by monopoly policy, but regardless of origin, the conflict generated important side effects in the rent-seeking economy of England during the mercantilist era. Whereas the crown's concem for "public interest" may have played a role in the transition of power from the king to Parliament, the institutional facts of the centuries-old alliance between common law courts and Parliament plus Parliament's control over jurisdictional disputes between the two court systems suggest a very powerful, self-interested economic motivation. One important question remains, however: Why was Parliament unable to reinstitute and sustain mercantilist policies when it became the sole supplier of regulatory legislation?

The Decline of Mercantilism and the Rise of Parliament

The focal point of the conflict between Parliament and the crown in the struggle to supply monopoly rights concemed patents. Parliament wanted to restrain the unlimited power of the crown to grant monopoly privileges. The struggle was not over free trade versus government control but rather over who would have the power to supply economic regulations.

This became abundantly clear in 1624 when the House of Commons petitioned King James I to cease and desist from granting monopoly privileges in the form of letters patent. The petition was provoked by public controversy regarding a lighthouse on the English coast known as the Wintertonness Lights. Parliament had originally issued a patent to the master of Trinity House to erect and maintain the lighthouse. Under the provisions of this patent ships carrying coal past the lighthouse were to be charged sixpence for every 640 bushels of coal transported. In the meantime, Sir John Meldrum successfully petitioned King James I for a patent to the lighthouse, upon receipt of which he began to charge a rate for coal that was nearly seven times the rate allowed the master of Trinity House under the initial patent. Parliament was incensed, and invoked "public welfare" as the rationale for wresting economic control from the crown. Such displays of public virtue are, however, most often transparent attempts to gain control over a powerful means of patronage.

Although Parliament ultimately beat the crown at its own game and became the sole supplier of legislation in England, it was unable to consistently exploit its new power because of the high costs of multiparty decision making. It is invariably more costly to each individual for decisions to be made by many parties rather than by a single party, such as the monarch. Unable to delegate authority to an effective bureaucracy (which did not exist in this period), Parliament found it costly to legislate and even more costly to enforce economic regulations. It is a wry twist of history that after struggling long and hard with the crown for the right to operate a national system of economic regulation, Parliament discovered that the costs of sustaining the system were much larger than the pro rata benefits. On this fact, mercantilism ultimately floundered, and significant deregulation of the British economy subsequently ensued. Historically, mercantilism waned in the eighteenth century, only to resurface with more contemporary visages in the future. During antiquity, cultural attitudes and practices placed a low value on entrepreneurial activity.

The Force of Ideas: Mercantilism, American Style

Colonization was both an expression of mercantilism and an extension of it. All of the great nations of the sixteenth through the eighteenth centuries-Spain, Portugal, Holland, France, and England-engaged in colonizing activities around the globe. In the process of creating profits for Europeans, of course, great discoveries were made, including the modern discovery ofthe Americas. The desire to accumulate wealth and power (often through conquest) was a

(continued)

driving force in what we call mercantilism. The dominance of nation-states and the process of state building over the mercantilist period was, in large part, an expression of economic interests within those states. Supply and demand provides a ready explanation: Colonies provided a source of cheap raw materiais and a ready market for the finished goods and services produced by the mother countries.

Mercantilist ideas, policies, and practices had an enormous impact on the history of the United States. The new overseas markets were relatively free and competitive, so that English and other European immigrants in the North American colonies were free to sell their wares to ali demanders and to buy needed products (mostly finished goods) from any willing sellers. But as a legal extension of the English state, American colonists had to toe the line established by the mother country.

Practically from the beginning, the North American colonists were shackled with regulations that created profits (rents) for English economic interests. The Stuart kings claimed "regalian rights" over the economic development of the colonies and cut deals with, for example, the Virginia tobacco growers and merchants for a "take" in the form of taxes. Later, after England's constitutional revolution (1650-1660) and the restoration of the monarchy, Parliament gained new powers, so that both the monarchs and the Parliament regulated economic activities in the New World.

Although such rules were extensive, a small sample of them is illustrative of their impact.* Under a series of Navigation Acts (such as those passed in 1660, 1663, 1673, and 1696), American colonists were required to ship their exports in English-built ships. Particular exports of the colonists were "enumerated," that is, required by Parliament to be exported *only* to England or to English colonies. Tobacco, sugar, and indigo were on the list in 1660. The Navigation Act of 1663 benefited English merchants even more. It required that *ai* European goods (with a few self-serving exceptions) transported to the colonies be shipped from England and on English-built ships. This had the effect of protecting British manufacturing and ship-building interests from foreign competition as well as allowing the crown to tax those goods that were excepted from the regulation.

Later, Parliament assigned customs officials in the colonies extraordinary powers of search and seizure and voided ali colonial laws contrary to parliamentary decrees. English rulers, merchants, and politicians, as well as colonial governors, took advantage of the situation, and rent seeking became rife. One example makes clear the motives: The Hat Act passed Parliament in 1732 under pressure from London felt makers. Already facing French competition, London hat makers were fearful of the establishment of a hat industry in the North American colonies. The act prohibited the exportation of hats from one colony to another, required colonists wishing to enter the trade to undergo a seven-year apprenticeship, limited apprentices to two per shop, and barred the employment of Negroes in hat making altogether. A Molasses Act, passed the following year, had the sarne intent and purpose.

Naturally, these kinds of mercantilist policies had to be enforced, and the distance between colony and mother country made enforcement costly. Despite rampant piracy, smuggling, and privateering (capture of "enemy" ships during wartime), England's economic regulations were surprisingly effective, in part because independent colonial trade was hampered by a *legally* prescribed lack of money and credit institutions. Mercantilist laws and regulations forced a high degree of "self-sufficiency" on the American colonists, even though the colonists generally carried trade deficits with England. Rent-seeking activity in England finally created a huge reduction in the welfare of the average colonist, and rebellion was the inevitable outcome. Thus, the collision course with England, which ended in the Declaration of lndependence and the birth of a new nation, was set much earlier in a course of action that taxed and regulated colonial trade and reduced the well-being of the average colonial citizen. This type of protectionism was (and remains today) associated with mercantilism and "neomercantilism."

*These examples are drawn from Richard B. Morris (ed.), *Encyclopedia of American History,* pp. S10-514.

Some historians emphasize the "dual" nature of mercantilist thought, which became increasingly manifest near the end of the mercantilist era. Many !ater mercantilists rejected domestic controls while they simultaneously defended protectionist measures in foreign trade. This apparent contradiction is less paradoxical if mercantilism is viewed as a form of rent-seeking activity. One particular incident, though small in itself, reveals that self-interested rent seeking was never far from the surface when mercantilist policies were shaped. King Charles I battled Parliament over his "ancient right" to customs duties, but lost his fight in 1641. Refusing to yield, the king reasserted his claim of absolute authority to levy taxes while Parliament was dissolved. Leaning on the support of Parliament, import merchants refused to pay customs to the king, who retaliated by seizing the merchants' goods. Some of the merchants resisted and were brought before the Privy Council. Merchant Richard Chambers brazenly declared that "merchants are in no part of the world so screwed as in England. ln Turkey they have more encouragement" (Taylor, *Origin and Growth of the English Constitution,* p. 274).

TRANSITION TO LIBERALISM

Major historical turning points in the distant past are always difficult to pinpoint. Such is the case with the transition from a heavily regulated national economy to one of relatively free trade. ln practice, no pure laissez-faire economy has ever existed, but significant structural changes in the British economy were detectable between the seventeenth and nineteenth centuries. To some extent, doctrinal and policy views of mercantilism offer different reasons for this transition.

The Doctrinal Transition: Mandeville

The doctrinal view maintains that mercantilism broke down because it lost intellectual respectability. ln the century prior to 1776, liberal criticism of mercantilism reached a high pitch. One of the most effective proponents of the new liberalism during this period was Bernard de Mandeville.

Mandeville, who was mentioned previously as a sponsor of the mercantile doetrine of the utility of poverty, published an allegorical poem in 1705 entitled *The Grumbling Hive;* or *Knaves Turn'd Honest.* ln this satirical work he argued that individual vices (self-interest) produce public virtues (maximize society's welfare), one of the central themes of Smith's *Wealth of Nations.* Later the poem was reprinted and enlarged in *The Fable of the Bees,* published in two parts (part I in 1714 and part II in 1729). The book was a sensation.

Rejecting a rationalist, metaphysical view of knowledge, Mandeville emphasized a theory of human nature based on the empírica! proposition that sense impressions are ali we can know of the world. Reasoning must come from facts, not from any rationalist or a priori considerations. ln this important sense, he foreshadowed the liberal revolution, whose most effective voice was Adam Smith. Since sensations are the source of knowledge and since each individual receives different externa! stimuli, early empiricists argued that the optimal social organization would be one allowing a maximum degree of individual freedom.[3]

[3] Although he does not do so consistently, Mandeville suggests at severa! places in *The Fable* that man's central motivating force is pleasure. Thus, some may regard him as an anticipator of utilitarian thought (see chap. 6 of this text).

Mandeville thus rejected absolute criteria as the foundation for social systems or for individual behavior. He insisted that right and wrong are relative, and he wrote: "Things are Good and Evil in reference to something else, and according to the Light and Position they are placed in" (Fable, p. 367). This passage is reminiscent of Xenophon's earlier subjectivism (see chapter 2). Although Mandeville's empiricism and moral relativism were roundly attacked during his lifetime, his position gradually gained acceptance, popularizing the view (still current) that normative problems cannot be handled effectively by science.

Further, Mandeville's belief that despite being "full of vice" (or self-interest) individuals nevertheless promote public benefits was a clear anticipation of liberal thought. Humans are at base selfish creatures since they "give no Pleasure to others that is not repaid to their Self-Love, and does not at last center in themselves, let them wind it and tum it as they will" (*Fable,* p. 342). But as he pointed out, "Pride and Vanity have built more Hospitals than all the Virtues together" (Fable, p. 261).

Although Mandeville cannot be regarded as a consistent exponent of liberalism, he nevertheless presented a clear discussion of the philosophical underpinnings of nineteenth-century liberal thought. Even though he did not apply his system of self-interest to actual problems of commerce, as writers such as Richard Cantillon (see chapter 4) did, he nevertheless remains an important harbinger of economic liberalism.

The Institutional Transition

Regardless of which interpretation one applies to mercantilism, the system retarded economic growth as an unintended consequence of its principies and practices. Toe conventional, doctrinal interpretation emphasizes the misguided effort to accumulate gold and specie, whereas the process view underscores how societal wealth was dissipated through monopoly creation and rent seeking at different leveis of govemment. According to the doctrinal view, mercantilism declined as its "errors" were slowly but surely exposed. The process view emphasizes the unintentional consequences of rent-seeking activity, which spawned institutional changes that gradually made rent seeking and interna! regulation by the central government less feasible. Under either interpretation liberalism and free trade emerged as viable altematives.

Pure laissez-faire never existed in England (or anywhere else) even after Parliament wrested the ability to supply regulation from the crown. The landed class retained control of Parliament and continued to pass legislation favorable to that class. But historians acknowledge that the deregulation of the British economy at this time was significant, even if their characterization of the dissolution of the old order has been willy-nilly. Whether deregulation eventually occurred because better ideas won out or because there was an increase in the cost to Parliament of supplying regulation, it should also be noted that the seventeenth and eighteenth centuries were periods of rapid technological advancement and that such quick-paced innovation in a reasonably competitive environment will tend to reduce the demand for legal cartels. This feature, too, may have played an important role in the decline of regulation in seventeenth-century England.

■ CONCLUSION

The analysis of mercantilism presented in this chapter has focused on the British economy. Intellectual and institutional forces interacted in the eighteenth century to nudge England and eventually other countries toward liberalism. Even at the height of its regulatory activity, however, the British economy was a pale reflection of its European counterpart-the Frencb economy administered by Colbert, Louis XIV's finance minister. French mercantilism is often called "Colbertism," thus bearing tbe personal stamp of the man wbo sbaped its policy. Wbat made French mercantilism different was its very high degree of centralization and very efficient system of policing, factors that were never so great in England. Tbe liberal reaction to French mercantilism reached its height in the writings of the Physiocrats, a group of French economists discussed in the following chapter.

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NOTES FOR F'uRTHER READING

The dominant the custom in economic literature has been to treat mercantilism as a set of ideas rather than as a set of individual and group interests spawned and shaped by prevailing institutions. Within this ideational/doctrinal view there have been two separate traditions, one "absolutist" in approach, the other "relativist." The absolutists tend to view the history of economics as a more or less steady progression from error to truth, whereas the relativists view past doctrines as justified within the context of their times. The former emphasize the presence of grave errors in mercantilist logic, errors exposed by David Hume and the classical economists. The primary instance of such faulty reasoning was the failure of mercantilist writers to recognize the self-regulating effects that the "specie-flow mechanism" imposed on attempts to realize a perennial trade surplus. The relativists, beginning with the German historical school and their English disciples, generally defend mercantilism as historically acceptable, given its aim of national power and wealth. Gustave Schmoller, *The Mercantile System and Its Historical Significance* (New York: Smith, 1931), represents the German historicist view. English disciples of the German Historicists include W J. Ashley, *An Introduction to English Economic History and Theory,* vol. 1 (New York: Putnam, 1892); and W Cunningham, *The Growth of English Industry and* Commerce, 2 vols. (New York: A. M. Kelley, 1968).

Jacob Viner is the clearest exponent of the absolutist view. His two classic papers on mercantilism were originally published in 1930 as "English Theories of Foreign Trade before Adam Smith," parts 1 and 2, *Journal of Polítical Economy,* vol. 38 (1930), pp. 249-301, 404-457, reprinted as the first two chapters of Viner's *Studies in the Theory of International Trade* (London: G. Allen, 1937). Viner viewed the mercantilists' trade theory as "objectionable from the point of view of modem doctrine," arguing that the "simplicity and brevity of the early analysis at least resulted in fallacies of comparable simplicity, but the !ater writers were able to assemble a greater variety of fallacies into an elaborate system of confused and self-contradictory argument" *(Studies,* p. 109). ln a trenchant criticism of the relativist position, Viner wrote:

> The economic historians ... seem to derive from their valid doctrine, that if sufficient information were available the prevalence in any period of particular theories could be *explained* in the light of the circumstances then prevailing, the curious corollary that they can also be *justified* by appeal to these special circumstances. There are some obvious obstacles to acceptance of this point of view. It would lead to the conclusion that no age, except apparently the present one, is capable of serious doctrinal error. It overlooks the fact that one of the historical circumstances that has been undergoing an evolution has been the capacity for economic analysis. More specifically, to be invoked successfully in defense of mercantilist doctrine it needs to be supported by demonstration that the typical behavior of merchants, the nature of the gains or losses from trade, the nature of the monetary processes, and the economic significance of territorial division of labor have changed sufficiently since 1550, or 1650, or 1750 to make what was sound reasoning for these earlier periods unsound for the present-day world. *(Studies,* pp. 110-111)

An interesting exploration of Viner's point is presented by W R. Allen, "Modem Defenders of Mercantilist Theory," *History of Political Economy,* vol. 2 (Fall 1970), pp. 381-397.

Eli Heckscher's magisterial two-volume work, *Mercantilism,* published in Swedish in 1931 and translated into English (see references) and revised by the author in 1935, spans both the absolutist and relativist positions. Heckscher treats mercantilism as a coherent and interrelated system of power and economic controls in which attempts were made to maximize the well-being of the state. He argues that: "The state must have one outstanding interest, an interest which is the basis for ali its other activities. What distinguishes the state from aU other social institutions is the fact tbat, by its very nature, it is a compulsory corporation or, at least in the last instance, has the final word on the exercise of force in society" *(Mercantilism,* II, p. 15). Though Heckscher's interpretations are open to dispute on specific points, his book remains the essential work on the subject. On a more elementary levei, Max Beer's *Early British Economists* (London: G. Allen, 1938) presents a less intricate discussion of mercantilism than Heckscher or Viner.

The original works of many of the major mercantilist writers, e.g., Gerard de Malynes, Thomas Mun, and Daniel Defoe, have been reprinted and published by A. M. KeUey. A rich lode of secondary materials exists focusing on mercantile doctrine and on individual mercantilists. R. C. Wlies discusses the shifting aims and analysis of mercantilist writers in "The Development of Mercantilist Thought," in S. Todd Lowry (ed.), *Pre-Classical Economic Thought* (Boston: *Kluwer,* 1987). The dualistic or "mixed" nature of mercantilist thought is emphasized in exceUent papers by A. F. Chalk (see references) and W D. Grampp, "The Liberal Elements in English Mercantilism," *Quarterly Journal of* Eco*nomics,* vol. 66 (November 1952), pp. 465-501.

George D. Chosky focuses on the economic thought of a farnous pair of mercantilists in "Previously Undocumented Macroeconomics from the 1680s: The Analytical Arguments and Policy Recommendations of Sir Dudley North and Roger North," *History of Political Economy,* vol. 24 (Summer 1991), pp. 515-532; and sarne author, "The Bifurcated Economics of Sir Dudley North and Roger North: One Holistic Analytic Engine," *History of Political Economy,* vol. 27 (Fali 1990), pp. 477-492. Marina Bianchi, "How to Learn Sociality: True and False Solutions to Mandeville's Problem," *History of Political Economy,* vol. 25 (Summer 1993), pp. 209-240, explores the thought of one of the most provocative writers of the era.

Three papers by E. A. J. Johnson probe mercantilist doctrine on the question of labor, unemployment, and the relation between labor intensity and international trade. As such, they form a useful accompaniment to the volume by Furniss cited in the references at the end of this chapter. See Johnson, "The Mercantilist Concept of 'Art' and 'Ingenious Labour,"' *Economic History,* vol. 2 (January 1931), pp. 234-253; "Unemployment and Consumption: The Mercantilist View," *Quarterly Journal of Economics,* vol. 46 (August 1932), pp. 698-719; and "British Mercantilist Doctrine Concerning the Exportation of Work and 'Foreign Paid Incarnes,"' *Journal of Political Economy,* vol. 40 (December 1932), pp. 750-770. Also see D. Woodward, "The Background to the Statute of Artificers: The Genesis of Labor Policy, 1558-63," *Economic History Review,* vol. 33 (February 1980), pp. 32-44.

Some inteUectual detective work into authorship and doctrinal influences is reflected in M. Dewar, "The Memorandum 'For the Understanding of Exchange': Its Authorship and Dating," *Economic History Review,* vol. 18 (April 1965), pp. 476-487; and G. H. Evans, "The Law of Demand: The Roles of Gregory King and Charles Davenant," *Quarterly Journal of Economics,* vol. 81 (August 1967), pp. 483-492. On the sarne subject, with an extension to classical economics, see A M. Endres, "The King-Davenant 'Law' in Classical Economics," *History of Political Economy,* vol. 19 (Winter 1987), pp. 621-638.

Philosophy conditioned political, social, and economic thought in the mercantilist era and during the transition to liberalism. A reading of Thomas Hobbes's *Leviathan* (London: Dent, 1914) or Niccolo Machiavelli's *The Prince* (New York: Modem Library, 1950) exposes power as the central theme of the period. The amoral character of mercantilist thought is perhaps nowhere better expressed than in Machiavelli's advice to the prince: "Thus it is well to seem merciful, faithful, humane, sincere, religious, and also to be so; but you must have the mind so disposed that when it is needful to be otherwise you may be able to change to the opposite qualities" *(The Prince,* p. 65). The dualism in economic thought is explained partly by the philosophic dualism of the time. For an explanation of the impact of the "new" philosophies of Hume and Locke on liberalism and classical economics see Werner Stark, *The Ideal Foundations of Economic Thought* (New York: Oxford University Press, 1944), and Carl Becker, *The Heavenly City of Eighteenth-Century Philosophers* (New Haven, CT: Yale University Press, 1932).

Philosophers who developed certain theoretical tools of economic analysis also spurred the intellectual evolution of laissez-faire. In this regard, see Karen I. Vaughn, *John Locke: Economist and Social Scientist* (Chicago: University of Chicago Press, 1980); M. L. Myers, "Philosophical Anticipations of Laissez-Faire," *History of Political Economy*, vol. 4 (Spring 1972), pp. 163-175; and same author, *The Soul of Modern Economic Man* (Chicago: University of Chicago Press, 1983).

What we have called the process, or policy, view of mercantilism derives from the historical conception of Heckscher and the contemporary application of self-interested behavior and property-rights theory to understanding institutions and institutional change. Specifically, the policy view features economic and political "actors" maximizing individual self-interest. This view of mercantilism was suggested early on in Adam Smith's *Wealth of Nations* (see references), but it was more forcefully stated in reviews of Heckscher's *Mercantilism*. A highly regarded scholar, Heckscher nevertheless irritated economic historians by his generalized treatment of economic policy and his excessive emphasis on the cohesiveness of mercantilism as doctrine and policy unaffected by actual economic events. On this point, see C. H. Heaton, "Heckscher on Mercantilism," *Journal of Political Economy*, vol. 45 (June 1937), pp. 370-393.

Some historians charged that Heckscher's treatment, embedded as it was in ideas, practically ignored all reference to the political process through which the so-called unifying mercantilist policies were made. For example, D. C. Coleman, "Eli Heckscher and the Idea of Mercantilism," *Scandinavian Economic History Review*, vol. 5 (1957), pp. 3-25, concluded that the term mercantilism, as a label for economic policy, "is not simply misleading but actively confusing, a red herring of historiography. It seems to give a false unity to disparate events, to conceal the close-up reality of particular times and circumstances, to blot out the vital intermixture of ideas and preconceptions, of interests and influences, political and economic, and of the personalities of men" (pp. 24-25). Coleman argues that policy cannot be treated in a vacuum, nor can the role and interests of parties to the political process be ignored. Thus, the application of contemporary positive economic theory dealing with economic regulation and public choice goes far in filling this important gap in Heckscher's treatment.

This policy view as described in the present chapter is expanded by R. B. Ekelund, Jr., and R. D. Tollison, "Economic Regulation in Mercantile England: Heckscher Revisited," *Economic Inquiry*, vol. 18 (October 1980), pp. 567-599; and, same authors, "Mercantile Origins of the Corporation," *Bell Journal of Economics*, vol. 11 (Autumn 1980), pp. 715-720; elaborated further by B. Baysinger, R. B. Ekelund, Jr., and R. D. Tollison, "Mercantilism as a Rent-Seeking Society," in J. M. Buchanan et al. (eds.), *Towards a Theory of the Rent-Seeking Society* (College Station: Texas A & M University Press, 1980), which also includes other papers of interest on the subject. Ekelund and Tollison's views on mercantilism culminate in *Mercantilism as a Rent-Seeking Society* (College Station: Texas A&M University Press, 1981) and its extension, *Politicized Economies: Monarchy, Monopoly and Mercantilism* (College Station: Texas A&M University Press, 1997), where applications of property rights, rent-seeking theory, emergence of the modem corporation, and the neoinstitutional economic framework of the mercantilist economies of France, England, and Spain come under review. A similar approach along with extensions is found in D. C. North and B. R. Weingast, "Constitutions and Commitment: The Evolution of Institutions Governing Public Choice in Seventeenth-Century England," *Journal of Economic History*, vol. 49 (December 1989), pp. 803-832; and in H. L. Root, *The Fountain of Privilege: Political Foundations of Markets in Old Regime France and*

England (Berkeley: University of California Press, 1994), chapters 6 and 7. Some critics argue, albeit without supporting theory or evidence, that the neoinstitutional approach is inapplicable to mercantilism or that it neglects or downplays the importance of ideas. See, for example, Lars Magnusson (ed.), *Mercantilist Economics* (Boston: Kluwer Academic Publishers, 1993), which contains the following papers: Salim Rashid, "Mercantilism: A Rent-Seeking Society?" Cosimo Perrotta, "Early Spanish Mercantilism: The First Analysis of Underdevelopment," and A. W Coats, "Concluding Reflections." Disparate, largely historiographic and ununified, views of mercantilism that focus on particular individuals or "theories" have emerged: see, for example, Lars Magnusson, *Mercantilism, The Shaping of Economic Language* (London: Routledge, 1993); and Cosimo Perrotta, "Is Mercantilist Theory of the Favorable Balance of Trade Really Erroneous?" *History of Political Economy*, vol. 23 (Summer 1991), pp. 301-336. However, as of yet, no positive theories of ideology or idea formation bave emerged to set against an economic approach. The historiographic (chiefly scholastic) methodology employed in most attempts to capture the essence of something called "mercantilism" has not as yet produced much fundamental understanding of the main developments of the period. lndeed, one recent account of a single mercantilist (John Cary) and his translation into a number of languages argues (unconvincingly) that the empire- and power-building paradigm that mercantilism represents should be the starting point of a canon of economic theory. That canon would replace the trade-oriented market theory developed by Adam Smith that has served economics to the present day: see Sophus A Reinert, *Translating Empire: Emulation and the Origins of Political Economy* (Cambridge: Harvard University Press, 2011). This argument will not bear scrutiny either with evidence or historical accuracy. Compare, for example, the evidence and conclusions concerning economic growth and ideational change over the English mercantile period in two works by Joel Mokyr: "Mercantilism, the Enlightenment, and the Industrial Revolution," in Ronald Findlay et al. (eds), *Eli Heckscher, International* Trade, *and Economic History* (Cambridge: Massachusetts Institute of Technology Press, 2006), pp. 269-303; and *The Enlightenment Economy: An Economic History of Britain, 1700-1850* (New Haven, CT: Yale University Press, 2010).

Details of the legal and political system that constituted mercantilism are given in a number of references in the present chapter. Maitland and Holdsworth provide the classic sources on the mercantilist judiciary. D. O. Wagner, "Coke and the Rise of Economic Liberalism," *Economic History Review*, vol. 6 (March 1935), pp. 30-44, presents a very interesting illustration of the duplicity with which common law jurists approached the subject of free trade. The fields of public choice and regulation, from which much of the process view of mercantilism takes its foundation, are the subject of chapter 24. However, there are severa! specific articles that are vital to understanding mercantilism as a process, especially Gary Becker and G. J. Stigler, "Law Enforcement, Malfeasance and Compensation of Enforcers," *Journal of Legal Studies*, vol. 3 (January 1974), pp. 1-18; Isaac Ehrlich and R. A. Posner, "An EconomicAnalysis of Legal Rule Making," *Journal of Legal Studies*, vol. 3 (January 1974), pp. 257-286; W M. Landes and R. A. Posner, "The Independent Judiciary in an lnterest-Group Perspective," *Journal of Law & Economics*, vol. 18 (December 1975), pp. 875-901; and G. J. Stigler, "The Theory of Economic Regulation," *Bell Journal of Economics and Management Science*, vol. 2 (Spring 1971), pp. 3-21.