

# Principles of Macroeconomics

## Chapter 14

### Mercantilism and Neo-mercantilism

In the remainder of this textbook, we will be looking at four different macroeconomic *paradigms*, emphasizing their *world views*. A *paradigm* or *world view* is a unifying perspective or central theoretical approach that serves as the core of a political-economic policy. These four paradigms differ markedly. Consequently, if it seems that everyone agrees here, you have missed the point.

The four world views or paradigms that will concern us are:

1. Mercantilism and Neo-Mercantilism
2. Classical Macroeconomics
3. Keynesian Macroeconomics
4. Monetarism

Each will be discussed in turn. Instead of trying to integrate or reconcile these conflicting world views, we will instead emphasize their differences. The emphasis will be on presenting, in simple English, the primary issues that define and distinguish these world views.

#### Mercantilism and Neo-mercantilism

Mercantilism was the dominant economic theory and policy in Europe before the development of Classical theory. It dominated European theory and policy from about 1550 to 1800. Mercantilism was still practiced in Great Britain as late as 1850. Mercantilism, in one form or another, was common in many European countries through the nineteenth century. In addition, mercantilist theories and policies have been common in other countries around the world. Neo-mercantilism literally means "new mercantilism." Neo-mercantilism is quite common in the world today, although

there are very few practitioners who call themselves mercantilist or neo-mercantilist. Neo-mercantilism today is more of an ad hoc approach to economic policy questions that enjoys strong grass-roots appeal among many people and politicians. If you understand mercantilism and its modern cousin, neo-mercantilism, you should have no problem finding this kind of thinking and policies in the world today.

Mercantilists generally viewed the world from the following perspectives:

- Mercantilists argued that wealth was money. Money in their day was gold and silver, so this view is often called "bullionism." The acquisition of gold and silver bullion (money) was the goal of mercantilist economic policies.
- Wealthy countries had a lot of bullion; poor countries had little. Developing countries had bullion coming in while countries that were getting poorer had bullion flowing out of the country.
- More important, good economic policies were policies that brought bullion into the country; bad policies caused a drain of bullion. Mercantilists tended to judge all policies by these criteria.
- The world's wealth (bullion) was fixed.
- Since wealth was fixed, if we get a bigger slice of the world's wealth, then someone else must get less. It is a dog-eat-dog world!
- Bullion can flow into a country if the country: 1) can find gold or silver at home or abroad; or 2) can steal it from others; or 3) can trade for it. These policies are listed in order of mercantilist preference. It is not surprising why Spain in the 16<sup>th</sup> and 17<sup>th</sup> centuries was the mercantilist's favorite example of a successful country.
- If finding or stealing bullion was not possible, then trading for it would have to do. To bring bullion in, a trade surplus (that is, positive net exports) was necessary.
- Mercantilists were very concerned about trade balances. They were also constantly worried about "them" --- the other countries competing with "us" for the fixed wealth.

- Mercantilists did not like monopolies, but they disliked and distrusted open, competitive markets even more.
- The government was expected to pursue policies that made sure we were winners, not losers. This was a brutal world with little need for political correctness. For example, if you had to exclude foreign competitors to gain a trade surplus, then so be it. Likewise, a navy might be very beneficial in eliminating trade competitors, literally!

Mercantilism favored protectionism and policies designed to create and maintain trade advantages. These policies were explicitly and unabashedly interventionist. For mercantilists, a "good" government was a big and powerful government.

Neo-mercantilism is an updated version of mercantilism that is very much alive in the world today. In neo-mercantilism, bullionism has been dropped, but the fixed-wealth view and the preoccupation with trade balances remain. In neo-mercantilism, the government is expected to pursue policies that make us winners. Neo-mercantilists still see things in terms of "Us vs. Them."

## **A Case Study in Neo-Mercantilism: MITI**

MITI stands for the "Ministry of International Trade and Industry." It is a ministry in the Japanese government. MITI and Japan's Ministry of Finance oversee Japan's *industrial policy*. Industrial policy is a term that entails government promotion of its domestic industries. It has been a staple of European government policy as well as a mainstay of Japanese economic policy for decades. In the 1980s, the U.S. was roundly criticized for not having a formal industrial policy. The U.S. does pursue similar policies in different agencies, but it does not have a formal industrial policy. Industrial policies have been developed more extensively in Japan and Europe before the creation of the European Union.

### **MITI's Targets**

MITI is charged with promoting Japanese industries that it identifies as being able to best benefit the Japanese economy. The focus is on promoting and protecting

Japanese interests in the world economy. Since WWII, MITI has targeted the following sectors:

#### **1950s**

- Coal, electric power
- Steel, and shipbuilding

#### **1960s**

- Chemical and light industries
- Consumer electronics

#### **1970s**

- Anti-pollution technologies
- Energy-saving technologies such as low-emission incinerators, lighter cars with reduced emissions, solar and fuel cell applications, downsizing steel and aluminum production
- Automobiles

#### **1980s**

- Computer memory (primarily DRAM)
- fifth-generation computer and video technology (primarily analog)
- Aircraft
- Space Program

#### **1990s**

- Robotics
- multimedia (especially based on fiber optics)
- HDTV (primarily analog)

### **MITI's Track Record**

MITI was credited with remarkable success in its early planning. Until the 1980's MITI seemed to enjoy one success after another. This was especially true when MITI was primarily involved in planning how Japanese firms could innovate and apply Western technologies and by playing the catch-up game. However, MITI has had less success as the Japanese economy matured and economic success began to depend more on creating new technologies rather than innovating Western technologies. Except for

robotics (an American invention, but a Japanese innovation), MITI's plans for the 1980s and 1990s either failed or had only limited success.

Critics today argue that Japan's success is best viewed as a success despite MITI, rather than success because of MITI. However, though its reputation has been tarnished by recent misses, proponents of "industrial policies" still view MITI as the world's most successful industrial policy.

### **Additional Policy Goals**

In addition to the primary goals described above, MITI has pursued the following:

- Create an Asian-Pacific "Co-Prosperity Sphere" with Japanese firms in the vanguard
- Create Japanese infrastructure to promote exports
- Promote foreign infrastructure (primarily in Asia) to promote co-prosperity production
- Assist Japanese firms in making strategic foreign acquisitions in U.S. and Europe (Columbia Pictures, CBS Records, MCA/Universal Studios, International Computers [U.K.])
- In general, MITI has pursued a "protectionist policy that has differed markedly from European protectionism. European protectionism has generally focused on protecting depressed and declining sectors. In contrast, MITI has tried to refrain from protecting depressed sectors with no future, preferring instead to seek out and promote sectors that were deemed to have a bright future.

### **MITI's Policy Tools**

MITI pursues its policy objectives through a formidable set of tools at its disposal. At its discretion, MITI can:

- Grant patent rights to firms best able to promote Japanese industry
- Suspend Japanese Antitrust Laws
- Encourage/Require participation in cartels
- Determine utility rates
- Grant permission to expand retail facilities. Traditional restriction cap retail outlets at 5,382 square feet. MITI considers all requests for larger facilities. The average MITI appeals time is over eight years.

- Establish trade practices, often with protectionist objectives
- Provide credit at subsidized interest rates
- Tax incentives
- Government procurement preference
- Use its influence and connections to pressure Japanese companies to "Buy Japanese"
- Grants and subsidies to Japanese firms
- Provide preferential access to credit
- Protect Japanese competitors from foreign competition (Tariff and non-tariff protection)
- Study foreign markets to seek out opportunities for Japanese firms
- Assist targeted Japanese firms with market studies and business advice
- Assist Japanese firms in export markets/foreign investments

Not everything that MITI did was protectionist; the emphasis on spotting future growth industries for Japanese firms to expand into was more akin to planning than protectionism. However, it is clear that MITI had the tools for practicing protectionism and used them extensively. This was very much in the realm of protectionism and mercantilist policies.

The real world is a messy place and cross-currents are the norm rather than the exception. The world will have to evaluate and respond to any number of programs similar to Japan's MITI. Going forward, you may be called on to figure out if China's "*Made in China 2025*" or Germany's "*Industry 4.0*" or the United States' "*Make America Great Again*" are protectionist policies and mercantilist-inspired.

## **So How Can You Spot a Neo-Mercantilist?**

Since no one claims to be a mercantilist or neo-mercantilist today, how do you spot them? This is especially important because neo-mercantilism remains one of the most important and potent economic paradigms in the world today. At times, you will see neo-mercantilist arguments but never labeled as such. At other times, the argument is never articulated beyond fear or concern. So how do we know when we are dealing with neo-mercantilism?

The following simple question may be of help. Ask someone to fill in their response to this question:

***“Our economic problems today are primarily caused by \_\_\_\_\_”***

The (honest) neo-mercantilist response to this question is almost always: “them,” or “foreigners,” or a particular country. Of course, one must not overlook the possibility of deliberately disguised responses. After all, this is a world of political correctness. But, a little digging will usually uncover the characteristic response.

In the case of the unarticulated neo-mercantilist position, look for the unspoken fear of “them.” And who is the “them?” Simple: ***Them*** are not ***us***!