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# Political Economy

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Crisis? What crisis?

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# Objectives

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Understand and describe ...

1. concept *political economy*
  2. mercantilism and capitalism
  3. basic elements of Keynesian economics
  4. globalisation and neoliberalism
  5. the basic elements of the 2007-2009 world financial crisis
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# 1. What is political economy?

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How economic systems (e.g. capitalism or socialism) affect different parts of the state (e.g. law, regulations, government, institutions). And vice versa.

- how the ***economy affects*** politics
- how ***politics affects*** the economics.

Often blends many fields of study including law, economics, trade, politics and political theory.

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## 2. Early political economy

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### Mercantilism

- economic nationalism
- state & business co-operate
- state control of economy
- increase state power & wealth by increasing exports, collecting metals
- England, France and Netherlands, 16th to 18th centuries
- frequent wars over routes & colonies

The Mercantilist Argument for Colonial Expansion



Source: Philip Dorf, *Our Early Heritage: Ancient and Medieval History*, Oxford Book Company (adapted)

# Early political economy

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## Mercantile policies

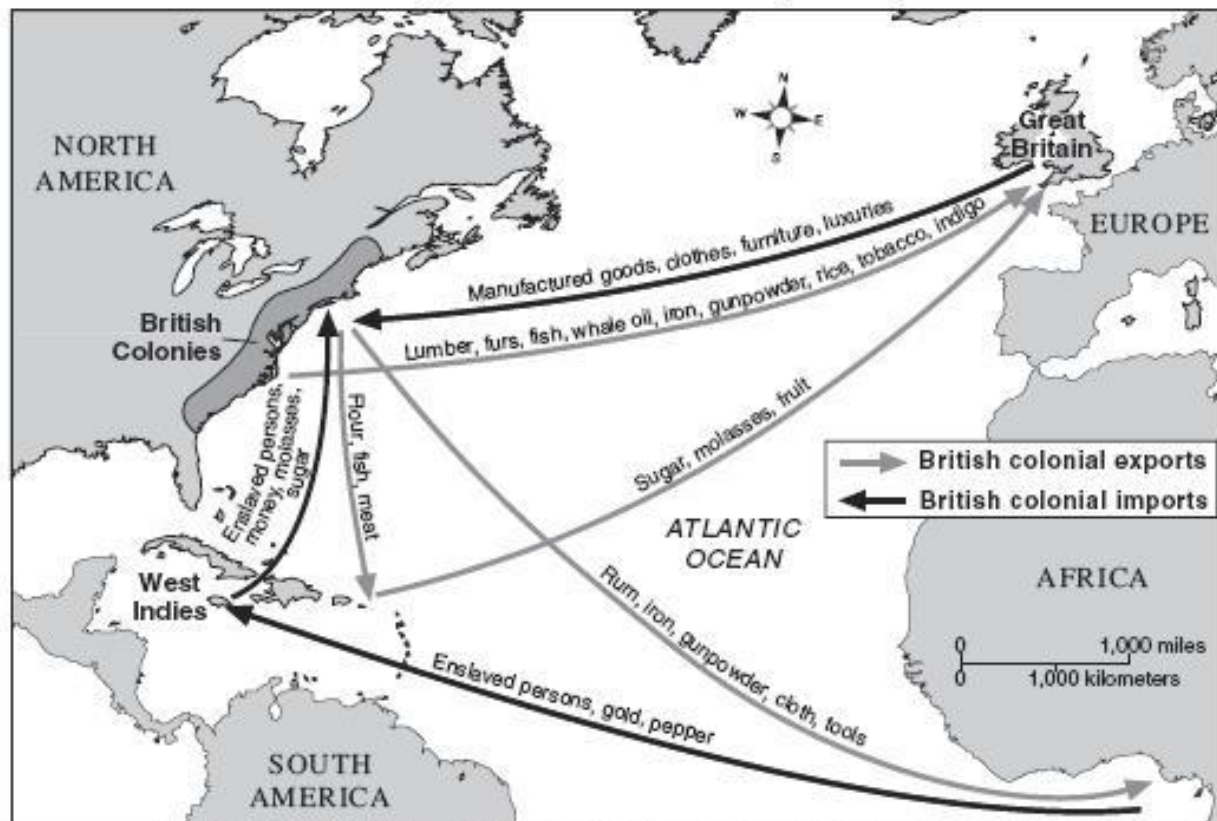
### International

- promoted positive balance of trade by restricting imports
- subsidized exports
- government control over economy via monopolies and powerful corporations
- tried to become self sufficient in food production
- protected trade routes and access to supplies, markets with navy
- built colonies as base for resources and markets for finished goods

### Domestic

- protected local industries through import bans and tariffs
  - emphasized production over consumption
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## Triangular Trade Routes (1700s)



Source: Joyce Appleby et al., *The American Journey*, Glencoe/McGraw-Hill (adapted)

# Early political economy

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Mercantilism eventually replaced by laissez faire trade policies.

- European powers saw trade can benefit all parties (mercantilists believed that wealth was limited)
- idea comparative advantage
- fewer trade restrictions could benefit all countries
- high cost of protection and intervention (e.g. military)

Mercantilism affected commerce, trade, domestic policy, domestic quality of life, the price of domestic goods and international relations

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# Case Study: 1839-1842 Opium War

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A mercantile trade dispute between Britain and China ended in war.

- since 1600 the East India Company was a private firm with exclusive rights for trade between UK and Asia
  - active in India and China - silk, tea, opium, cotton and salt
  - England had a great love of Chinese tea
  - China wanted to be paid with silver; no interest in finished goods
  - obtaining enough silver was very costly for the East India Company
  - EI company wanted to pay with opium, which was plentiful in India
  - China said no, they had too many drug addicts, between 4 and 12 million opium users (mostly under 40 males)
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# Case Study: 1839-1842 Opium War

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- War broke out after many small troubles
- British had better ships, cannons and rifles
- sailed up Yangtze river
- swiftly defeated the Chinese
- in peace treaty, England got Hong Kong and trade routes
- set the stage for another war 1856-1860



## 2. From Mercantilism to Capitalism

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Mercantilism was a trading system that saw gold and silver as wealth.

Decline started with industrial revolution in England (1750s).

- production more important than trade to generate wealth.
  - factories replaced small craft shops
  - enormous production output and economies of scale.
  - owners of capital (means of production) had more power than the merchant class
  - industrialists (capitalists) wanted less government intervention and free markets to expand sales and increase profits
  - writers like Adam Smith promoted *laissez faire* markets
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# Mercantilism vs Capitalism

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	Mercantilism	Capitalism
economy	size of the economy is limited; growth means taking a bigger piece of the pie	wealth can be created through production
business environment	protected monopolies	competitive companies
consumers	discourage spending; prevent outflow of money	encourage spending; consumption creates growth

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# 3. Keynesian Economics

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Developed an idea to help countries get out economic crisis, especially the 1929 depression.

Basic idea: economic depression happens when people stop spending.

- Governments can play an important role to reduce recessions
  - Increase spending and lower taxes in recession
  - This will increase total spending and lead to recovery
  - When economy recovers, governments spend less and tax more
  - State intervention reduces impact of boom and bust cycles
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# 4. Globalisation

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What is it?

- The dominance of developed countries over less powerful nations?
  - A force for economic growth, prosperity, and democratic freedom?
  - Environmental devastation, exploitation of the developing world, and suppression of human rights?
  - Does globalization only benefit the rich or can the poor take advantage of it to improve their well-being?
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# 4. Globalisation

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Here is one definition from [Globalization101.org](https://www.globalization101.org/).

1. Globalization is a process of interaction and integration among the people, companies, and governments of different nations.
2. It is a process driven by international trade and investment and aided by information technology.
3. This process has effects on the environment, on culture, on political systems, on economic development and prosperity, and on human physical well-being in societies around the world.

Is globalization good or bad and for whom?

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# 4. Globalisation

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Globalisation has economic, cultural and political consequences.

**ECONOMIC:** production and finance are international; national governments have less ability to manage economies

**CULTURAL:** local and regional values, attitudes and beliefs become less distinct

**POLITICAL:** supranational organisation like the IMF, WTO, EU and World Bank have growing authority over states

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# 4. Globalisation and Neoliberalism

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## Neoliberalism

- less regulated markets
- emphasis in the individual
- greater privatization
- less public spending
- social welfare program cuts

Neoliberalism ideology seems to follow globalisation.

Why?

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# 4. Globalisation and Neoliberalism

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1. Some states willingly make changes to attract or keep TNCs.
  2. Long term growth in the US and Western Europe is proof that an emphasis on free markets and individualism stimulates prosperity.
  3. International organisations like the IMF and World Bank link aid to neoliberal ideological changes.
  4. Growing importance of financial sector. Increase capacity to borrow money, which stimulated economic growth. To be successful, this system needs continued growth and consumption, both of which can be supported in the short term by liberalisation.
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# 4. Globalisation and Neoliberalism

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Critics say neoliberal globalisation has many problems related to state legitimacy:

- increases social inequality
  - governments respond to needs of global economy rather than citizens
  - environmental damage is significant
  - far less stability, far more disasters including 2007-2009 financial crisis
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# 5. Financial Crisis 2007-2009

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It was caused by three important factors:

- sub prime mortgages and a housing bubble
  - change in US government investment law which allowed the biggest investment companies to leverage investments up to 30 or 50 times
  - bundles of house mortgages as an investment which were incorrectly rated as excellent by investment rating agencies
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# 5. Financial Crisis 2007-2009

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## Impact

- millions of people lost their own
  - pension programs bankrupt
  - investors lost in stock markets around the world
  - sovereign debt threats especially in Europe
  - demands for social welfare cuts to pay for debt
  - campaigns to protest legitimacy of governments not long lasting
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