Review of Thomas Mun's 1664: England's Treasure by Forraign Trade. Or The Ballance of our Forraign Trade is The Rule of our Treasure

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After centuries of experimentation and theorizing, freedom of international trade has emerged as one of the most fundamental and widely accepted propositions economics has to offer for the prosperity of the world. This eventual conclusion was the result of a slow process which first displaced Protectionism and Mercantilist trade doctrines. Yet, Mercantilists were a necessary force in economics; they provided some of the first foundations to study the mechanisms of international capital flows, taxes, tariffs and subsidies, and most notably, the nature of trade. Thomas Mun's, England's Treasure by Forraign Trade, was amongst the most important tracts outlining Mercantilist trade and economic ideals. The book was written by Thomas Mun in the 1630's and published posthumously by his son in 1664, who offered it to the King of England as a trade policy guide. Thomas Mun (1571-1641) was a wealthy merchant who was appointed to several British economic and trade committees, and was elected a director of the East India Company (EIC) in 1615. During Mun's time at the EIC, a sharp recession and silver shortage struck England. When the British public blamed the EIC and its silver exports to the East Indies for the recession, the company called on Mun to justify their trade. Thus, Mun became a so-called merchant economist and began writing about trade and economics. Mun's first book (1621) sought to disassociate the EIC from the recession. His second book, England's Treasure by Forraign Trade sought to make general assertions about desirable and undesirable trade relationships.

For the contemporary reader, England's Treasure by Forraign Trade is at times difficult to decipher: the combination of old English writing, archaic references, and occasional confused arguments, make reading Mun quite challenging. However, some chapters are surprisingly insightful for the time. The book begins with a chapter enumerating the qualities Mun and other successful merchants must posses. The list is long, twelve points: from being precisely knowledgeable of foreign currencies, languages, products, and taxes, to knowing everything about ship repair and being a good accountant. This chapter serves two functions; a vain glorification of the merchant's profession, but more importantly, a qualification of Mun's authority on the subject of international trade and money – the book is destined for Royalty, after all. The rest of his book can be roughly divided into two categories. In the first category, spanning chapters 2 through 12, Mun formalizes the balance of trade for the first time in history, describes how to increase trade surpluses, and goes to great lengths to establish the premise that a nation without gold mines can only change its money supply through trade flows. The second category, spanning chapters 13 through 20, examines the benefits of trade surpluses on many aspects of the nation's economy; from lowering required tax rates and increasing employment, to increasing military strength.

Mun paints a world of Empires in perpetual struggle; where trading partners are also potential enemies, and where domestic production must be managed in case of unexpected armed or trade wars. In this world, there is only so much gold and silver money, and a King without reserves is vulnerable in his home and from overseas. Mun says that in this world; it is of paramount importance that a strong Britain maximize its military resources, and manage external trade to avoid depleting its treasury. To accomplish this, Mun's thesis argues, Britain must run persistent trade surpluses, so that each year it receives more from foreigners than it pays them in gold. Mun's thesis would establish a pillar of mercantilist ideology for centuries to come; the Balance of Trade doctrine, which although it was invoked by prior authors, Mun rigorously defines. Thus, though Mun's book covers other subjects, given the central importance of the Balance of Trade doctrine to all his subsequent work, this review will concentrate on that subject.

Mun says that Kingdoms are little enriched by "gifts received or by purchase taken from some other Nations", so that "the ordinary means therefore to increase our wealth and treasure is by *Forraign Trade*, wherein wee must Ever observe this rule; to sell more to strangers yearly than wee consume of theirs in value", and he continues, if "we do yearly export the overplus to forraign countries to the value of twenty two hundred thousand pounds; by which means we are enabled beyond the Seas to buy and bring in forrain wares for our use and Consumption, to the value of twenty hundred thousand pounds; By this order duly kept in our trading, we may rest assured that the Kingdom shall be enriched yearly two hundred thousand pounds, which must be brought to us in so much Treasure; because that part of our stock which is not returned to us in wares must necessarily be brought home in treasure" (Mun, 5). As we can see, Mun views the gains of trade between nations as if they were transactions on a merchant's income statement; there are revenues and expenses, and he contends that Britain is only "profitable" in international trade when running trade surpluses.

Mun is trying to establish two premises here, that gold flows can only be significantly influenced by the balance of trade, and that gains or losses in *gold* from trade are measures of gains and losses to the *economy* from trade.

The Balance of Trade doctrine, is best described as containing two tenets. The first tenet: if a nation runs persistent trade surpluses it will continuously accumulate gold. And the second tenet: this gold accumulation will benefit the general public, and "enrich the Kingdom". At first glance the Balance of Trade tenets are actually quite tempting, but we know that deeper economic analysis by Mun's successors would expose major flaws in his logic.

The first tenet will be dethroned by David Hume in his treatise: Essays, Moral, Political, and Literary (1758), in which, using the "Quantity theory of Money" Hume established the price specie-flow mechanism. The price specie-flow mechanism (PSFM) states that a surplus nation who accumulates gold will experience price level inflation (because more money will chase the same amount of goods in the domestic economy), and the higher domestic price level will discourage exports and encourage imports in the next period, which should eventually lead to a stabilizing balance of trade against whichever nation was running trade deficits. Meanwhile, deficit nations experience deflation and there the price level leads to the opposite trading incentives; which also serve to stabilize trade flows. Thus, according to the price specie-flow mechanism, the first tenet of the Balance of Trade doctrine does not hold water, gold accumulation through trade surpluses are redistributed by deficits once inflation occurs. The modern reader has already found a major hole in Mun’s simple analogy, achieving persistent surpluses appears to be a hopeless task.

Mun suggests numerous ways to increase trade surpluses in his third chapter. It is noteworthy that he only mentions taxing foreign goods in one particular situation. He suggests taxing domestic consumers when consuming goods which are being imported for future export (Mun, 12). The rest of his policy recommendations are surprisingly liberal compared to the modern pejorative use of the Mercantilist label: he wants to persistently stimulate exports by encouraging production in export competing industries, liberalize import for re-export, and discourage import by “soberly refrain[ing] from excessive consumption of foraign wares in our diet and raiment” (Mun, 7). Yet, the Balance of Trade doctrine is dangerous when put in the hands of more Protectionist pundits. If a nation, or worst, group of nations, pursue the hopeless goal (hopeless by PSFM) of perpetual surpluses through tariffs and import quotas, they may find themselves choking off trade entirely, and dissipating the true gains from trade: the increases in each nation’s production possibility frontier imbued by specialization of international labour. We conclude that Mun’s lack of insight into the inflationary pressures caused by surpluses fails his position on the first tenet of the Balance of Trade doctrine.

The second tenet of the Balance of Trade doctrine; that gold accumulation enriches a nation, would probably invite even swifter dismissal from modern economists. Hume joins the anti-mercantilist bannermen by reminding us that “money is nothing but the representation of labour and commodities, and serves only as a method of rating or estimating them. Where coin is in greater plenty; as a greater quantity of it is required to represent the same quantity of goods, it can have no effect, either good or bad, taking a nation unto itself" (Hume, 160). Hume tells us that money is merely a unit of account for goods and labour, and also that it is merely a means to an end. Mercantilists are stubborn on this subject, Mun tells his King that if Britain exports 1000 gold coins worth of cloth and imports only 500 gold coins worth of French wine, the nation has gained 500 gold coins worth of wealth (we will ignore merchant profits for simplicity). Now, if Britain faced unemployment, and factors of production were idle before the increase in liquidity, it does seem feasible that the economy could be stimulated into short-term greater productivity due to a growth in demand. However, if we abstract from the idle factor argument, we are left with a situation where Britain has expended 1000 gold coins worth of British labour, in exchange for 500 gold coins worth of French labour plus 500 gold coin. Britain did this despite having the opportunity to get Frenchmen to work 500 gold coin worth more for British consumers. Let us go further, imagine a Mercantilist utopia where Britain's yearly trade is of 0 gold of imports and 1000 gold of exports – the result is clear; the nation would soon exhaust itself from working for its neighbors without actual consumption gains in return. Perhaps its coffers would be ripe with gold and ready to hire mercenaries for war, but that would come at a considerable cost. Mun seems to neglect the very object of trade; afterall a nation ought only export if it can import, because money supply growth in and of itself is no source of wealth.

England's Treasure by Forraign Trade is unquestionably a mercantilist treatise, yet it remains distinct from crude protectionism. In fact, quite to the contrary; it exhorts trade as a great means to increase Britain's wealth. That being said, Mun's approach to measuring these increases in wealth, are swiftly revealed to be antiquated. But before exposing the flaws in Mun's book, one should take careful note of the times and circumstances in which he wrote it. Mun paints a picture of a world with Empires in perpetual struggle, where trading partners are also potential enemies, and where domestic production must be managed in case of unexpected armed or trade wars. In this world there is only so much gold and silver money, and a King without reserves is vulnerable in his home and from overseas.

Having said all this; I will now conclude by defending Thomas Mun's goals even though I contest his reasons for aspiring to them and his mechanisms to achieve them. So let us try to rebuild the mercantilist position. We begin by hypothesizing that, by some manipulation of various tariffs, quotas and subsidies, Mercantilists might achieve a *period* of sustained gold inflows from trade surpluses. Of course, we still maintain that if the new gold is left to exclusively circulate within the domestic economy, then surpluses are rather useless, if not *wasteful* of economic resources. However, I contest the assumption that surpluses necessarily imply a commensurate increase in the domestic gold stock in circulation.

There is an underlying assumption in the PSFM that surplus gold is never being exchanged for foreign goods - it simply circulates domestically and causes inflation. But I disagree with this presumption on three fronts. Firstly, if trade flows are increasing every year (larger exports *and imports*), then it may be that last year's surplus induced gold accumulation is indeed being used to purchase imports, but that exports are still surpassing these imports. Then the surplus gold which can actually cause inflation is only the gold leftover between flows, not the entire new stock. To express this in the merchant's way of thought, we can consider a company which has high income, but never accumulates cash on its balance sheet because it constantly reinvests. Secondly, the "Quantity theory of Money", and the PSFM both only hold if we assume that the domestic economy is not growing as fast as, or faster than, the money supply has grown. Indeed, more money chasing more goods need not cause inflation. Finally, if some monetary authority, the King's Monarchy, in Mun's time, were to sterilize the money inflows by locking up some gold and keeping it in a war chest for future imports, or by lending it to a friendly Kingdom for interest, the nation *is* arguably wealthier due to past gold inflows, as measured by its government's purchasing power and lower future tax obligations.

No doubt, Mun's thesis is misguided, he sees gold as wealth and does not consider any inflationary effects due to money supply increases. Yet, I believe Mun deserves some credit for wanting to increase the money supply, because under the bimetallic system, as he notes, "[Britain has] no other means to get Treasure but by forraign trade, for Mines [they] have none" (Mun, 14). We know merchants were heavily influenced by lending rates in their business and they, therefore, would find it desirable to see inflows of gold and silver to the nation from which they received credit because this (at least temporarily) would lower nominal interest rates and increase their profits. But more importantly, using the "Quantity theory of Money" again, we can distinguish a great incentive for seeking trade surpluses that the bimetallic system could create; if it were the case that seventeenth century output rates were growing faster than gold and silver mining output rates, then goods could have been growing more plentiful compared to money. This hypothetical situation would lead to general deflation for all nations using gold and silver coins as money, and this deflation should theoretically be doubly accentuated when running trade deficits (more goods, less money), but mitigated when running surpluses. Hence, insofar as we maintain that persistent deflation is bad for growth and some inflation is good, then when money supplies are tied to a fixed (or slow growth) quantity of money, it appears the Balance of Trade doctrine caters to anti-deflationary goals, and perhaps this notion was influencing Mercantilists to seek ways to increase gold in circulation, because they would have associated them with better economic conditions. While it may not be true that global economic output rates outpaced global gold and silver output rates, this assumption must be true for a particular case like Britain. As we saw earlier, Mun's debut as a merchant-economist came on heels of a British recession that coincided with a silver coin shortage, so it seems natural that the money supply loomed large in his mind when he advocated gaining wealth through the Balance of Trade doctrine.

References:

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