

Politics and the World Economy

Lecture Outline

1. Our Political Economy Framework
 - a. Things we want to explain
 - b. Variables we use to explain things
2. Prologue to the Modern World (17th-19th century)
 - a. International conditions
 - Political: mercantilism, colonialism
 - Technological: innovations of the industrial revolution
 - b. Domestic conditions
 - “Endowments,” “Interests,” and “Institutions”
 - Case Study: America and the World Economy, 1600-1865

2. Explanatory Framework

Things we want to explain (outcomes)

- Economic growth, over time and across countries.
 - Economic growth is the source of material improvements in human welfare
 - Growth a modern phenomena (Figure 1)
- Distribution of wealth and income, across countries and within them.
 - When wealth is distributed inequitably, the benefits of economic growth may not be shared by most people
 - Inequality between countries has increased dramatically (Figure 2)
- Link between globalization, economic growth, and the distribution of wealth
 - Does integration with the world economy promote economic growth and greater *equality* among nations? Does globalization create *inequality* within nations?

Explanatory Framework (cont.)

Variables we use to explain things

- explanatory variables are of two types: int'l and domestic

INTERNATIONAL variables:

1. Global political conditions

- Variation in military conflict
- Trends in colonization and decolonization
- Existence of a dominant global power (e.g. *Pax Britannica*, *Pax Americana*)

2. Global economic conditions

- Global price trends and shocks (inflation/deflation)
- Global financial conditions (interest rates, financial crises)

3. Technological change

- Innovations that promote growth or encourage globalization
- Technology is “international” (available to all)

Explanatory Framework (cont.)

DOMESTIC variables:

1. Endowments

- Nations differ in terms of their endowments of capital, labor, and land and this shapes their relationship to the world economy
 - Recall Heckscher-Ohlin Theorem

2. Interests

- People differ in terms of their interests toward the world economy; some gain while other lose from globalization
 - Recall Stolper-Samuelson Theorem

3. Institutions

- Nations differ in terms of their domestic political institutions, which shapes the interplay of endowments and interests

3. Prologue to the late 19th Century

- **Mercantilism and Colonialism** (late 17th –mid 19th centuries)
 - Use American case to illustrate INTL and DOMESTIC variables.
- **INTERNATIONAL variables**
 - Global political conditions
 - Highly conflictual due to mercantilism (e.g. Navigation Acts of 1660) and colonialism
 - frequent wars between European great powers
 - Global economic conditions
 - Slow economic growth until the eve of the industrial revolution
 - Wars, economic embargos, and mercantilism reduce the attractiveness of the global economy
 - Technological change
 - Innovations in textiles, metals, and power promote the industrial revolution in Great Britain

DOMESTIC variables:

Case study of America 1700 - Civil War

– Endowments

- American colonies abundant in raw materials; scarce in capital and skilled labor

– Interests

- Opposition to British rule tied to ownership of endowments: people that owned abundant resources opposed mercantilism and empire (Virginia planters, Boston shipowners and merchants, primitive manufacturing).
- Support for British rule on the frontier (Ohio Valley), for security reasons. Ended with defeat of the French in 1763

– Institutions

- Imperial rule allowed little opportunity for colonists to shape policy

Independence to the Civil War

– International setting

- Napoleonic Wars (1793-1814), Embargo of 1807, War of 1812 cut US off from world markets (Figure 3). Isolation from the world economy stimulates rise of manufacturing (e.g. MA textile industry)

– Interests

- After War of 1812, nascent US manufacturers appeal to government for protection (tariffs on British imports)

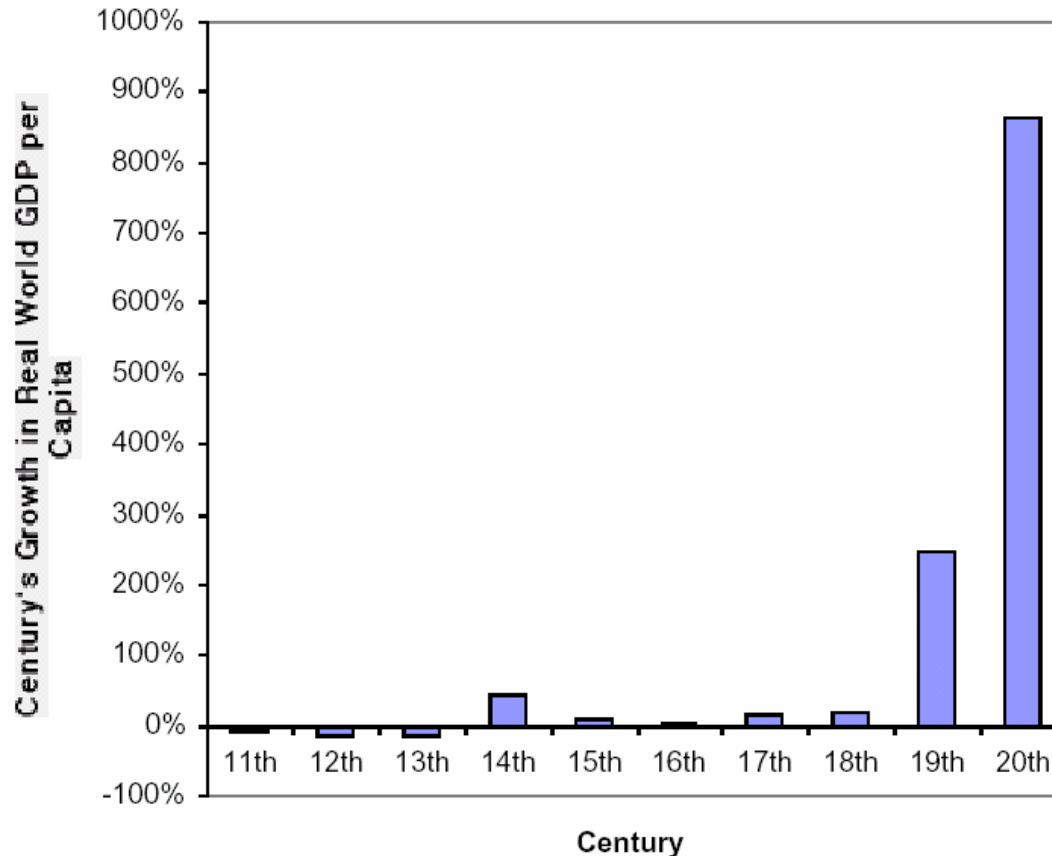
– Institutions

- Alexander Hamilton's economic nationalism, and the government's need for revenue (a tariff is a tax that the govt can collect even with primitive bureaucracy), meshes with the protectionist interests of manufacturers.
- Origins of revenue-generating/protective tariff date from this period.

Economic Origins of the Civil War

- International conditions
 - With the industrial revolution, England’s demand for raw cotton explodes (5% growth annually 1820-1860). Also, growing demand from U.S. textile mills.
- Key technological change
 - Rise of “short-staple” cotton / Whitney’s cotton gin (Figure 4)
 - U.S. South become major supplier of world’s cotton (Figure 5).
- Interests
 - South wants free trade; Northeast wants protection (Midwest aligns with Northeast)
- Institutions
 - Stalemate in Congress but South at a growing disadvantage
 - When Democrats (party of Southern planters) were in office, tariffs went down; when Republicans (party of Northern industry) controlled government, tariffs went up (Figure 6).
 - Civil war settles the issue. With South out of Congress, tariffs skyrocket.

Figure 1: Growth is a recent phenomena



The era of rapid economic growth, when the material wealth of humankind explodes, does not start until the 19th century

Figure 2: The Distribution of Wealth has become more inequitable over time.

Year	Ratio between incomes of richest and poorest country
1870	9:1
1960	39:1
1990	45:1

- Rapid economic growth over the last two centuries has *increased* the gap between rich and poor countries, not lessened it.
- The gap is not increasing because poor countries are growing poorer, but rather because the level achieved by the richest country keeps increasing.

Figure 3: Napoleonic Wars and Embargo of 1807 reduce trade

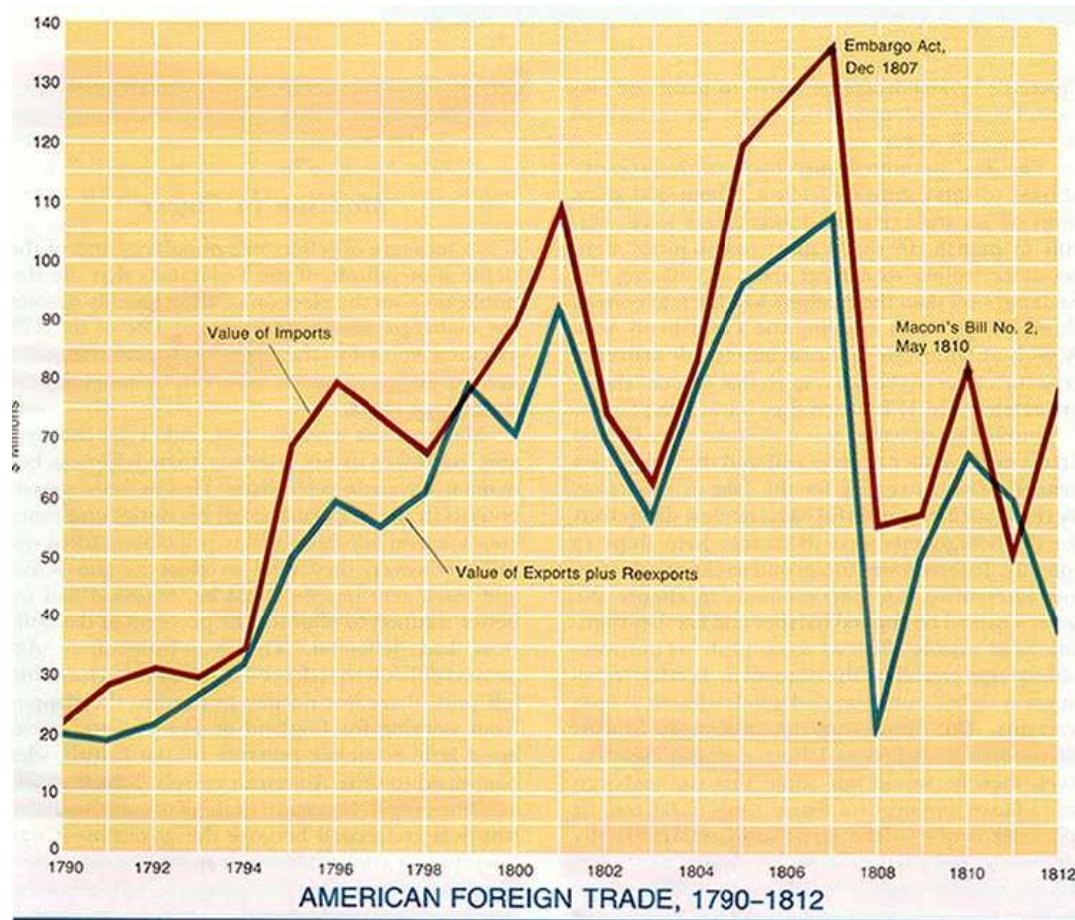


Figure 4: The Cotton Gin



To do the work of the fingers which pulled out the “lint,” Whitney had a drum rotate past a sieve, almost touching it. On the surface of the drum, fine, hook-shaped wires projected which caught the lint. The restraining wires of the sieve held the seeds back while the lint was pulled through.

Before Eli Whitney's cotton gin, the laborious hand method of picking out cotton seeds restricted the amount of cotton that could be produced. The influence of the cotton gin was almost instantaneous. The gin made practical the use of the heavily seeded “short-staple” cotton, which could be grown in upland areas more readily than long-staple cotton. England's textile industry ensured favorable prices and increased market demand.

Whitney's patent application is at <http://www.ourdocuments.gov/doc.php?doc=14#>

Figure 5: U.S. Cotton Production 1791-1860

	<i>1791</i>	<i>1831</i>	<i>1860</i>
<i>Million lbs.</i>	2.0	385.0	1,650
<i>Percent of world total</i>	0.4	49.6	66

Eli Whitney's cotton gin (1794) allowed for the cultivation of short-staple cotton in a wide area of the American south

Figure 6: U.S. tariffs

