Chapter 2

The Evolution of Economic Systems
Basic role of any economic system is to provide for people

- We spend most of our lives working
  - And, sustenance is the most immediate necessity,
  - So economic relationships have a huge influence on people, society
- The economic system is a ‘mode of life’ (RSSS)
  - That fundamentally shapes what our lives are like
Institutions

• All economic systems are based on a set of underlying *INSTITUTIONS*
  – Legal system, cultural beliefs, norms and values, resource base, technology
  – Patterns of behavior and organizations that form the essential structures of society
Surplus

• Why is the production and usage of economic *surplus* crucial in a society’s economic development?
Surplus and Economic Development

• A society’s surplus is the primary pool from which it can invest in capital goods, new ventures
  – And therefore, the primary source of economic growth and development
Feudal institutions

• How were resources (land, labor, natural resources) allocated in tribal societies?
  – Under Feudalism?
Precapitalist economic structures: Tribal societies

- Before capitalism, allocation of resources was determined by Tradition and Authority
  - Jobs allocated by tradition,
  - Resources allocated based on age, social status
- Often very egalitarian
Precapitalist economic structures: Feudalism

- Feudalism: Everyone had an established role in society:
  - 1 blacksmith in each community; son took over the business.
  - Lords dictated conditions for the serfs
    - Relationships were governed by traditions
    - Not entirely authoritarian
- Your job and role in life were inextricably linked to the social context
  - Religious, cultural institutions
Greed in human history

• What were early attitudes towards Greed?
  – How would the medieval preoccupation with salvation affect market activity?
Precapitalist views on Greed

- Before the market system, GREED was considered to be a SIN.
- The profit motive is only as old as ‘modern man.’
  - When people of traditional cultures get higher wages, they often work LESS not more
  - Other aspects of life mean more to them
    - Wage work is unattractive compared to the leisurely pace of most traditional societies
    - Increasing one’s standard of living is a lower priority than spending time with family, participating in cultural activities
    - The object of life for the ordinary citizen was not to advance his station in life, but to maintain it.
  - Work was an end in itself, not a way to earn money
- First capitalists were outcasts, often looked down upon
Land, Labor and Capital did not exist in a modern sense

- They were not bought and sold,
  - But instead were allocated by tradition or authority
- Land was part of a family estate, family identity (and a source of power)
  - Only someone desperate would sell it
- Labor was allocated by duty, tradition
- Capitalists shunned efficiency, produced things in labor-intensive, traditional fashion
Little or no surplus existed

- Few resources to spare to invest in productive inventions (production for subsistence)
  - Surplus can generate growth if it is invested, but if it is wasted by the elites, then growth will not happen
- By the time of feudalism, there was some limited manufacturing, trade
- But feudalism itself was quite static
  - Only a handful of major inventions for the 1000 years after the fall of the Roman empire
    - Including the printing press, firearms, glass windows
  - Change, new inventions were resisted
    - People are fined, jailed, killed for inventions which threaten entrenched ways of life!
• What were some of the changes that undermined the Feudal economic system?
Feudalism is finally undermined by a series of changes

1. Improvements in **agricultural productivity** from crop rotation, use of animals, better transportation

2. **Urbanization & Specialization** b/c of increase in surplus

3. Increasing **TRADE** w/ Asia, manors => more interdependence
Feudalism is finally undermined by a series of changes

4. Trade was further facilitated by Crusades, Exploration

5. Rise of the Nation State as manors, merchants gained a common interest

6. More trade => nobles desired more CASH, manor system became monetized
7. The Enclosure Movement

- Serfs kicked off land they had farmed for 100s of years
- Common land seized
- All for lords to graze sheep for wool to trade
  - Lords could make money exporting wool,
    - Used that money to buy the fantastic silks, spices, luxuries from the East, and thereby enhance their status

- PRIVATE PROPERTY BEGINS with the expropriation (stealing) of land,
  - paupers everywhere, poor houses
    - No labor market existed to soak up excess labor
Private Property

• Why was the creation of private property a crucial step in the movement from feudalism to capitalism?

• Why were some economists distrustful of the institution of private property?
Changes undermining feudalism (Cont.)

8. Trade/manufacturing increasingly taken over by merchant capitalists, power of independent crafts people declines.

– Once they own the means of production, everything changes for craftspeople
9. Creation of centralized industries where production was controlled by capitalists
   - Laborers have no resources but their labor (CAPITALISM)
     - Role of tradition in the economy is replaced by the market (dollar)
     - Productivity increases w/ centralization & specialization, but more inequality
10. REFORMATION: decline in power of Catholic church, which opposed materialism;
   – Protestant religions such as Calvinism promoted individualism, profit-seeking behavior
   – Worked perfectly with the new market system
Mercantilism

- Huge profits allow merchants to engage in CAPITAL ACCUMULATION, expand and become more powerful
  - Lords & Kings want some of this action, and trade becomes a major focus
Mercantilism

- Countries attempt to increase their wealth by insuring an inflow of gold (bullionism)
  - Increase exports, decrease imports, exploration
    - To find additional gold supplies
  - Trade monopolies, tariffs all used increase wealth
  - East India Co. & other trading companies given huge territories to exploit to increase revenues
  - Wages must be kept low so businesses can profit:
    - Mercantilists believed poor must be kept poor to keep them working
      - Pay them more and they'll just drink or be lazy
Adam Smith developed his economic ideas in this context

• Believed that state *should not intervene* on behalf of powerful merchants

• *Competition* should be allowed; it would lead to benefits for all:
  – low prices, more productivity, better wages for laborers
Adam Smith developed his economic ideas in this context

• Smith was criticizing a government that acted on behalf of business
  – Not necessarily a critique of all forms of government intervention
The Market System

• Everyone does what is in their own best interests
  – Laws of supply and demand, competition insure that necessary goods are provided:
• The market system is not just a means of exchanging goods
  – It is a mechanism for sustaining and maintaining an entire society
  – But this wasn’t clear to people early on in capitalism
    • People weren’t sure that everything that used to be done by tradition would still be done by the market
The Rise of the Market System

• With the decline of mercantilism, there was an explosion of inventions and growth in England

• Market system expanded all over the world,
  – Land, labor and capital were now commodities to be bought & sold

• Also extreme poverty
  – Worse than under feudalism
    • Peasants no longer had a claim on land
    • There were no common lands
  – Child labor, dangerous working conditions, vast slums existed under early capitalism