The Political Economy of the Cold War

London School of Economics, October 18, 2010
A foregone conclusion?

Nixon and Khrushchev in the kitchen, Moscow 1959
A foregone conclusion?
A foregone conclusion?

Jules Régis Debray, French leftist philosopher and comrade in arms of Che Guevara: There is “more power in rock music and blue jeans than the entire Red Army”
A foregone conclusion?
11/9/1989: The scoop that never was

Checkpoint Charlie: The crossing-point from West to East Berlin
The scoop that never was
A foregone conclusion?

- Growth rate declined
- Total factor productivity (TFP) declined
  - Raw materials worth more than finished products
- Price controls blocked market signals (as Hayek had warned)
  - Steel consumption/GDP ratio 4 times as high as in the United States
- Only oil price hike kept show going
  - Armageddon Averted (Kotkin)
- Corruption—the ‘grabbing hand’ (Shleifer)
  - Officials have an interest in restricting output
- ‘You pretend to pay us and we pretend to work.’
  - No incentives in the workplace
- Excess defence spending
- Inadequate allowances for depreciation of capital stock
  - Chernobyl, April 16, 1986
- Ill health and alcoholism
  - 17 litres a year ...
Soviet economic performance, 1950-1985

TFP = Total Factor Productivity

Source: HBS Case 795-060
Average annual per capita growth, USSR, satellites, 1950-73, 1973-90

Source: Maddison, *World Economy*
The sad truth

- Soviet GDP was not 49% of US level in 1990 (CIA), more like 36% (European Comparison Project)
- In 1945 it had been 27%
- Soviet per capita consumption was not 31% of US level, more like 24%
- In other words, Turkey – Bergson (1997)
Defense expenditure as a percentage of output

US (GNP)  
Russia (NNP, NMP, GDP)

West Texas Intermediate crude (1962=100)

Source: Economagic
Hard currency debts, 1975 and 1989 ($ billion)

Source: Maddison, *World Economy*
Male life expectancy at birth, 1960-1990

Source: World Bank, WDI
What I used to think:
The Eurocentric narrative
Europe’s predicament in 1947

- Population up 10%, despite death toll of war
- Industrial production down 40%
- Reduction of overseas invisible earnings and worsening terms of trade reduce capacity to import by 40%
Percentage of votes going to Communist parties/coalitions (*) in post-war elections
The traditional answer: Marshall’s Plan

‘Europe ... must have substantial additional help or face economic, social, and political deterioration of a very grave character.’ – at Harvard, June 5, 1947
Causes of the post-war ‘miracles’
Growth of per capita GDP, annual average compound rate, 1950–73

Source: Maddison, *World Economy*
1. External factors?

• Marshall Aid
  – Around 2.5% of recipient GDP
  – For each $1 of aid some 65 cents went to increased consumption and 35 cents to increased investment
  – An extra $1 of investment raised national product by 50 cents in the subsequent year
  – Helped finance early trade deficits

• American sponsorship of trade liberalization

• ‘Americanization’ of business
  – ‘Taylorist’ management, U.S. marketing techniques

• Sustained American military expenditures
Total aid 1946-52 equivalent to 1.1 per cent of US GDP; but biggest recipients not best performers.
2. Internal factors

• Those who started from lowest base generally had highest growth
  – Spain, Portugal, Germany, Italy, Austria

• Abundant labour (refugees) plus wartime investment in capital stock gave Germans an advantage

• Reduction of class conflict compared with 1920s—the success of ‘corporatism’ (Maier)
  – Unemployment down from 10% (1950) to 1% (1960)
  – Lower labour radicalism, e.g. Germany
(a) Social and Christian Democracy

• ‘Scarcely anyone doubts that we must move towards socialism’ (Hayek)
  – Planning as legacy of war economy

• Britain’s welfare state
  – 20% of productive capacity nationalized
  – Welfare “from cradle to grave”
  – Healthcare free at point of delivery

• France: Monnet’s Plan—*dirigisme*

• West Germany: Erhard’s social market economy’
  – Stable currency
  – Free trade
  – Deregulation

• Italy: Church, industry plus Mafia
  – The ‘honored society’ in Sicily
Social services expenditure as a percentage of GDP, 1870-1975

NB Not including education and housing
(b) Versus ‘real existing socialism’

- Soviet exactions: c. $14 bn.
- Five and Six Year Plans
  - Heavy industry and urbanization
- Collectivization
  - Esp. Baltic states, Romania
- Forced labor
  - Danube-Black Sea Canal
  - Bulgaria 100,000 slaves, 361,000 workers
- The ‘New Class’ (Milovan Djilas)
Catch: The West’s slide into ‘stagflation’

“This may not be as simple as I thought!”
Percentage increase in real GDP per person employed, 1950-1973

Source: Maddison, *World Economy*
Annual inflation rates, selected OECD countries, 1970-1979

Source: OECD
UK house prices, annual percentage change, 1970-1979

Source: Nationwide
What I think now:
East Asia as the key
The view from the East

- West European success was not the surprise of the post-war period
- Asian growth was much more remarkable
- We need to give more weight to American occupations in Japan and South Korea
- Also Hong Kong, Malaysia, Singapore, Taiwan and even Indonesia
- The Soviets fared much better in Latin America and Africa, where economic performance deteriorated (Westad, Mitrokhin)
- South Vietnam: exception that proves the rule
- The decisive year was not 1989 but 1979 ... when China joined the Asian bandwagon
Asian share from 14% to 34% ...

... W European down from 36% to 22%, N American from 44% to 26%

Source: Bridgewater
Productivity: Output per hour in manufacturing (1950=100)

Source: OECD
Japan and the Asian Tigers, 1960-1990

Source: World Bank, WDI
Asian growth in comparative perspective, 1950-1990

-1.0  0.0  1.0  2.0  3.0  4.0  5.0  6.0  7.0  8.0  9.0

South Korea  Thailand  Hong Kong  Singapore  Taiwan  Malaysia  Indonesia  Pakistan  Japan  Sri Lanka  India  Bangladesh  Nepal  Burma  Philippines  Latin America  Africa

1950–73  1973–90

- The graph shows the comparative growth of Asian countries from 1950 to 1990, with countries listed from highest to lowest growth.
- Countries like South Korea, Taiwan, and Japan have shown significant growth over the period.
Understanding Asian success

• Long-term security guarantees vital after military interventions (especially Japan, Korea, Taiwan)

• Post-war reforms created secure institutional basis for growth – especially land reform (Japan 1946)

• Increasingly open economic order upheld by the United States principally benefited Asian countries

• They were able to export their way to prosperity thanks to American FDI plus American consumption
A problem for liberals

- A series of military interventions and occupations were successful: Japan, Korea, Malaya (UK), Philippines
- South Vietnam was the exception that proved the rule
- (In a counterfactual world, South Korea 2.0)
- Economic success in Asia was not a function of democratic institutions*
- But it was followed by democratic transitions
- Success was not based on standard market models ... but it benefited from liberalize global trade regime

E.g. Generals Park Chung-hee (1960-79) and Chun Doo-hwan (1980-87) in South Korea ... also Lee Kuan Yew in Singapore, Suharto in Indonesia 1-party states in Taiwan and Japan.
Yet *ex post* interventions were worse

<table>
<thead>
<tr>
<th>‘Successes’</th>
<th>‘Failures’</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Iran (1953)</td>
<td>• Indonesia (1957)</td>
</tr>
<tr>
<td>• Guatemala (1954)</td>
<td>• Cuba (1959)</td>
</tr>
<tr>
<td>• Congo (1961)</td>
<td>• South Vietnam (1964-1975)</td>
</tr>
<tr>
<td>• Brazil (1964)</td>
<td>• Angola (1975-76)</td>
</tr>
<tr>
<td>• Dominican Republic (1965)</td>
<td>• Ethiopia (1977)</td>
</tr>
<tr>
<td>• Chile (1973)</td>
<td>• Afghanistan (1979)</td>
</tr>
</tbody>
</table>
The counterfactual question

- Would the United States have won the Cold War if East Asia had not experienced an economic miracle?
- Weren’t the Soviets better positioned to win ...

24 November 2010

The Third World’s War