

<http://www.youtube.com/watch?v=-CvQOuNecy4&feature=related> (3.00-5.00)

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”

1. **Albania.** Communist party still retains Leninist orientation, Jan. 1990. Parliament backs liberal reforms, May 1990.
2. **Yugoslavia.** Government decides to hold free elections, Dec. 1989.
3. **Bulgaria.** Government disavows "dominant role" for Communist party; pledges free elections and new constitution in 1990.
4. **Romania.** Communist dictator Ceausescu overthrown and executed, Dec. 1989; Salvation Front led by dissident former Communists wins elections, May 1990.
5. **Hungary.** Free election sweeps non-Communists into power, April 1990.
6. **Czechoslovakia.** Communist leadership ousted, Nov. 1989; Vaclav Havel named president, Dec. 1989.
7. **Germany.** Berlin Wall breached, Nov. 1989. Reunification of East and West Germany, Oct. 1990.
8. **Poland.** Solidarity party sweeps elections, June 1989.
9. **Lithuania** declares independence, March 1990; Moscow calls move illegal.
10. **Latvia and Estonia** begin process of separation from Soviet Union, April 1990.



A foregone conclusion?

11/9/1989: The scoop that never was



Checkpoint Charlie: The crossing-point from West to East Berlin

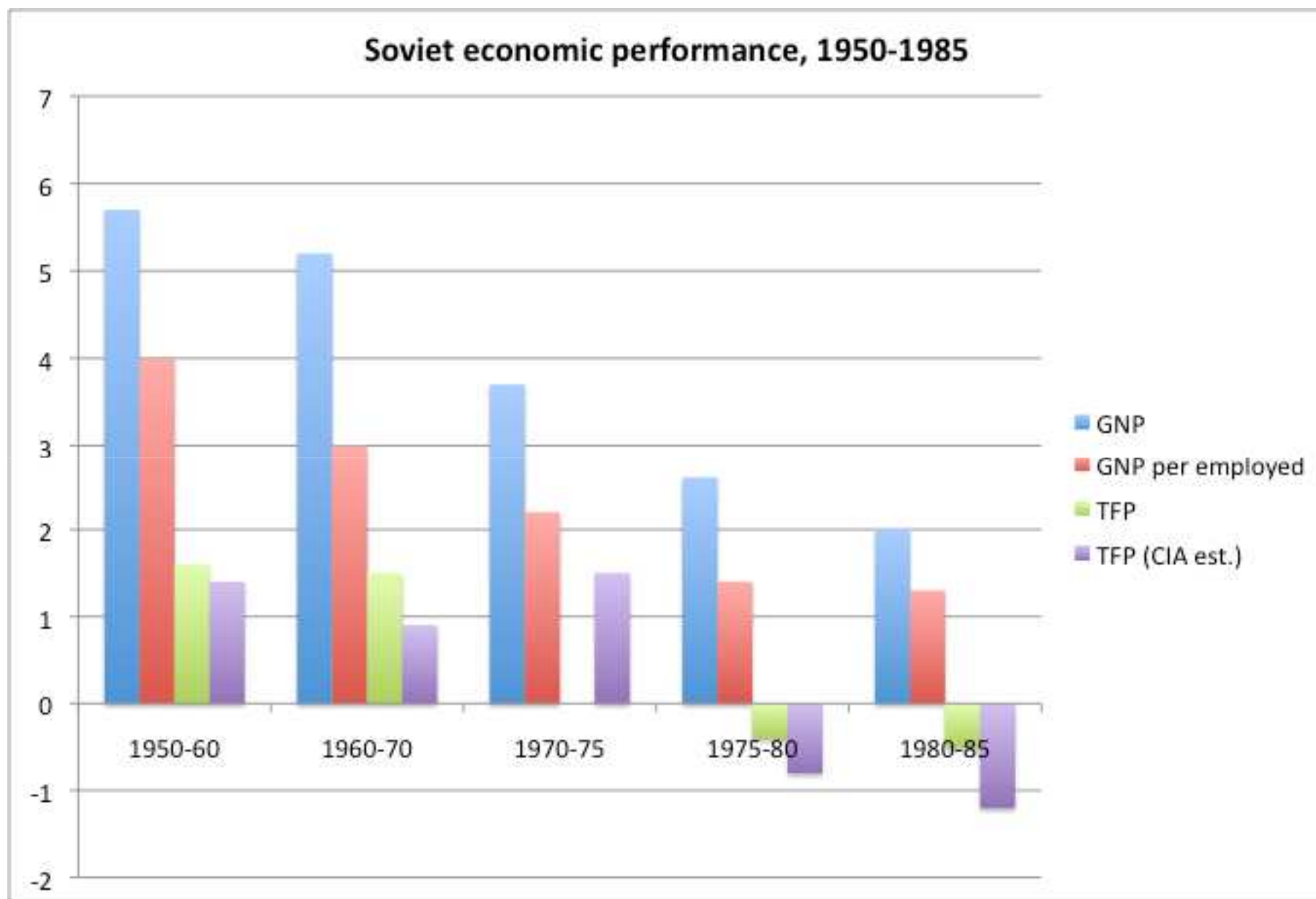
The scoop that never was



Deutsch-deutscher Grenzübergang: „Zu wenig Kitt in der Betonmauer“

A foregone conclusion?

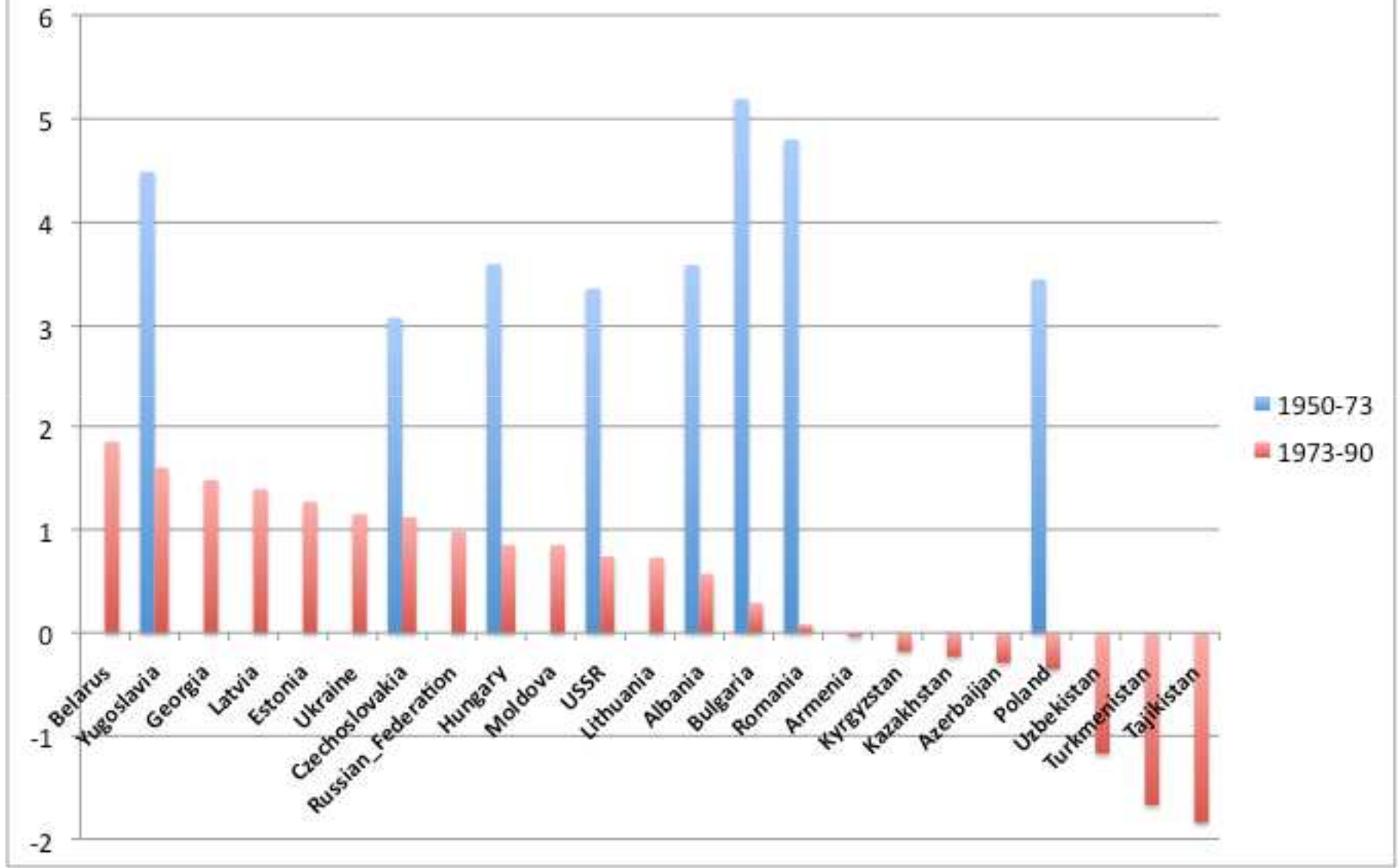
- Growth rate declined
- Total factor productivity (TFP) declined
 - Raw materials worth more than finished products
- Price controls blocked market signals (as Hayek had warned)
 - Steel consumption/GDP ratio 4 times as high as in the United States
- Only oil price hike kept show going
 - Armageddon 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 ...



TFP = Total Factor Productivity

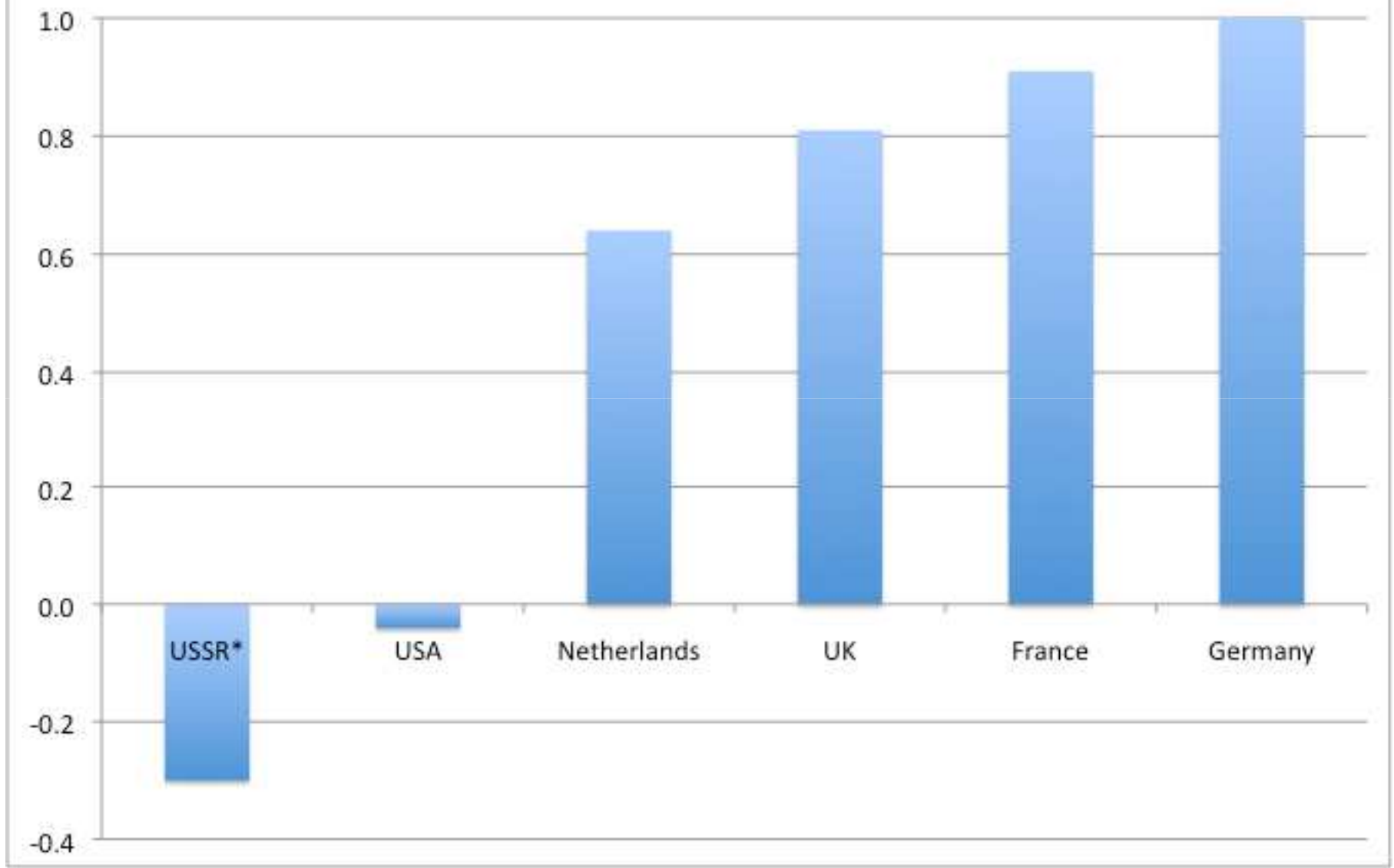
Source: HBS Case 795-060

Average annual per capita growth, USSR, satellites, 1950-73, 1973-90



Source: Maddison, *World Economy*

Rate of growth of Total Factor Productivity, 1973-87



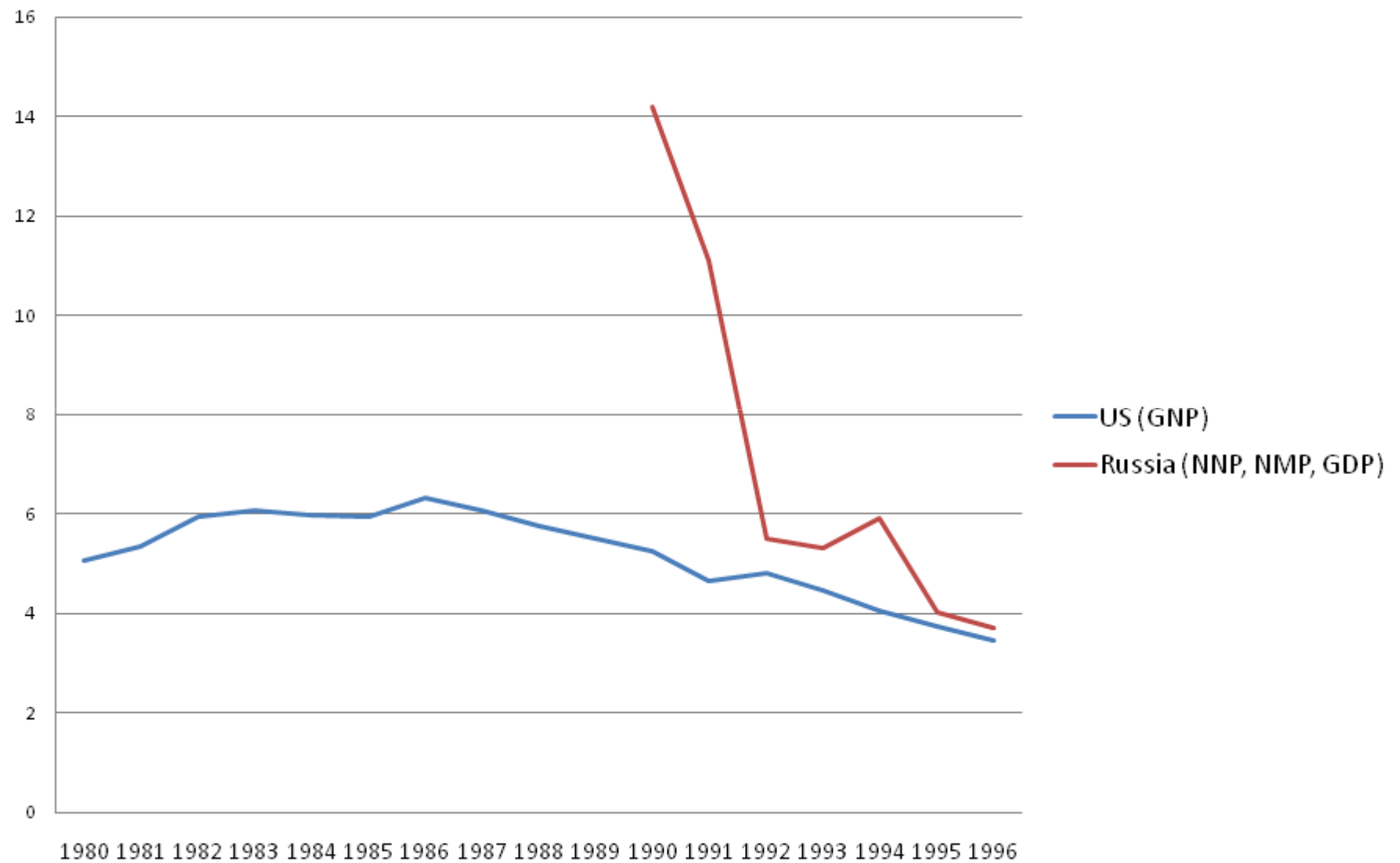
Source: HBS Case 795-060

The sad truth

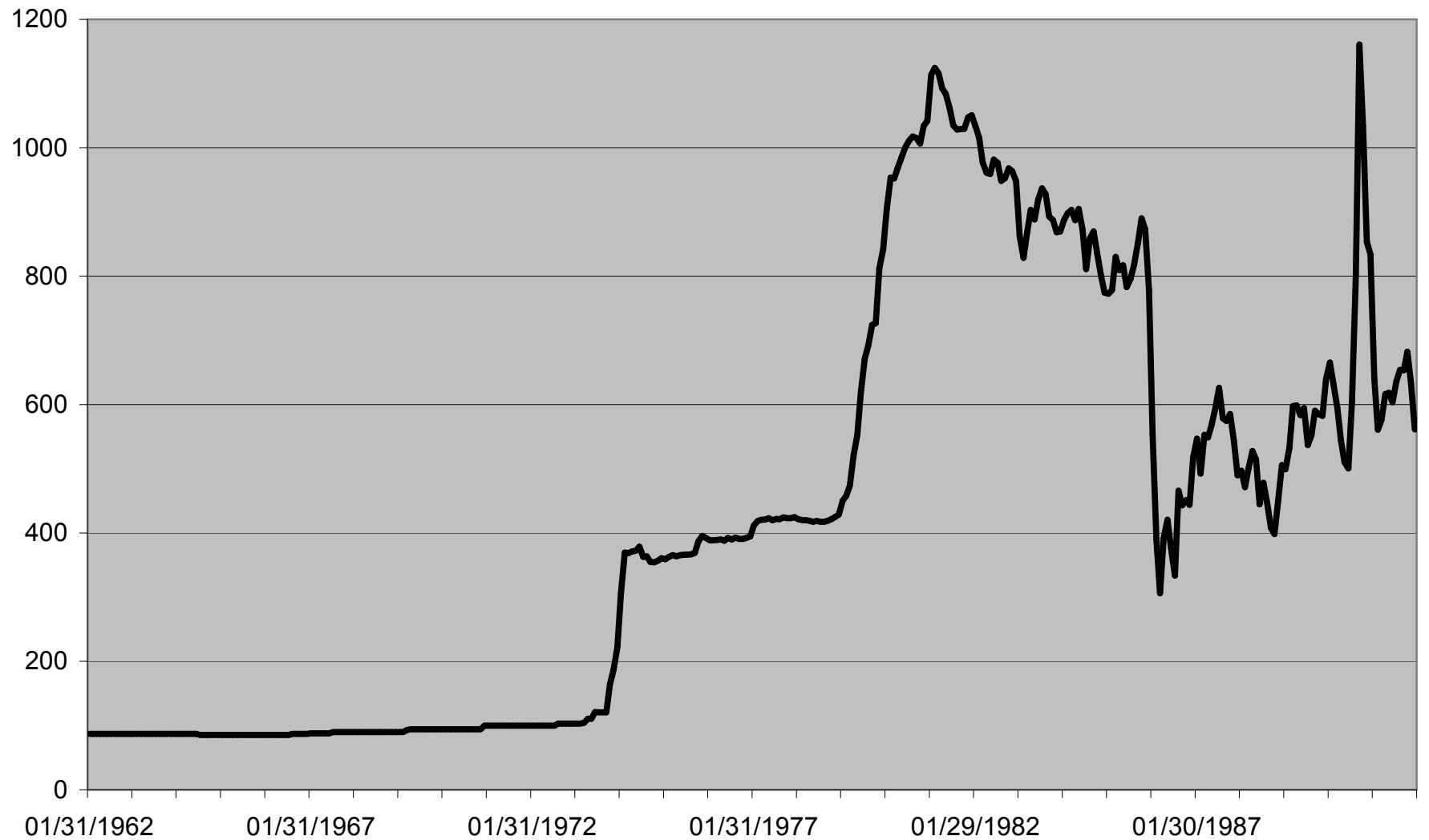
- Soviet GDP was not 49% of US level in 1990 (CIA), more like 36% (European Comparison Project)
- In 1945 it had been 27%
- Soviet per capita consumption was not 31% of US level, more like 24%
- In other words, Turkey – Bergson (1997)



Defense expenditure as a percentage of output

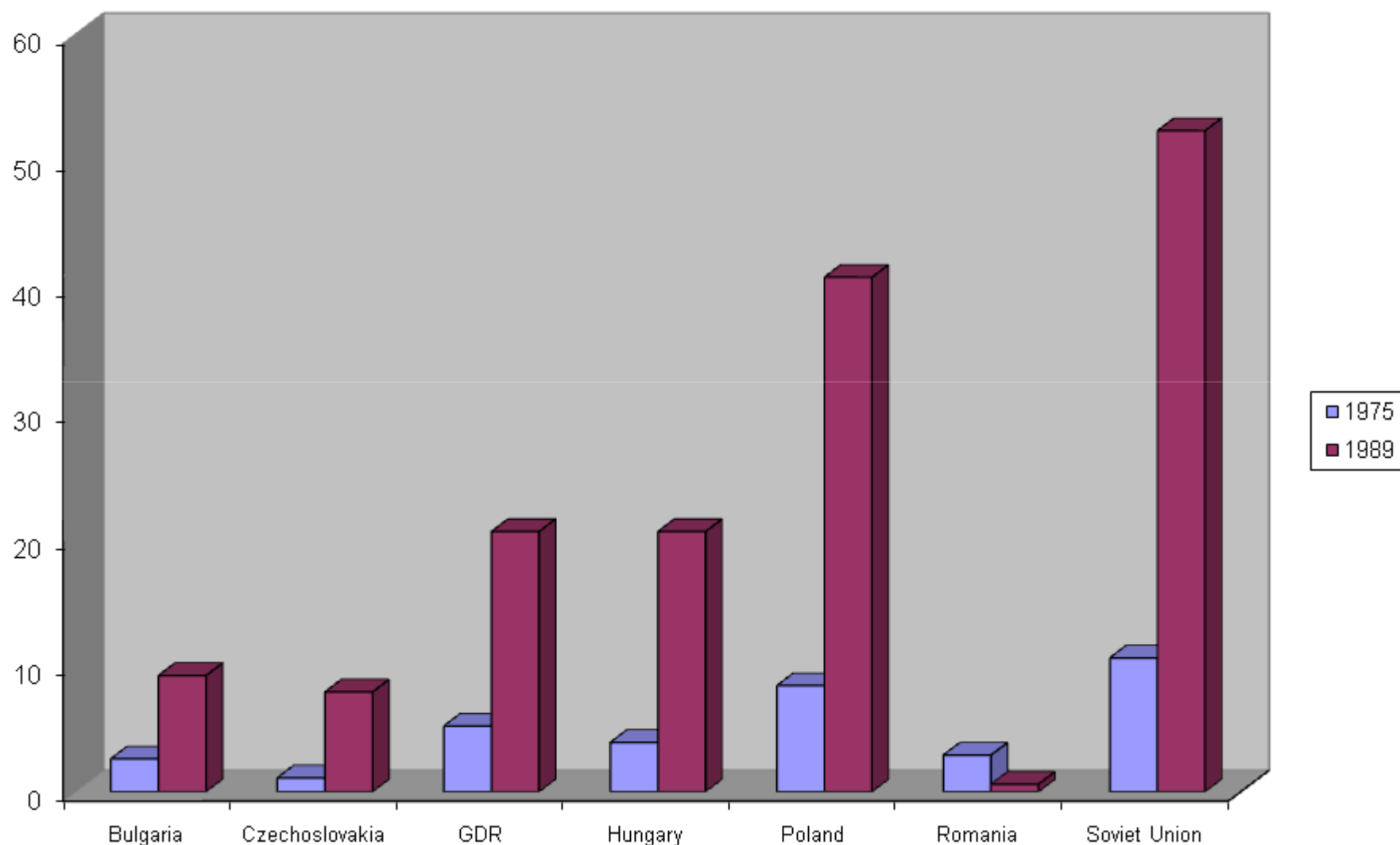


West Texas Intermediate crude (1962=100)



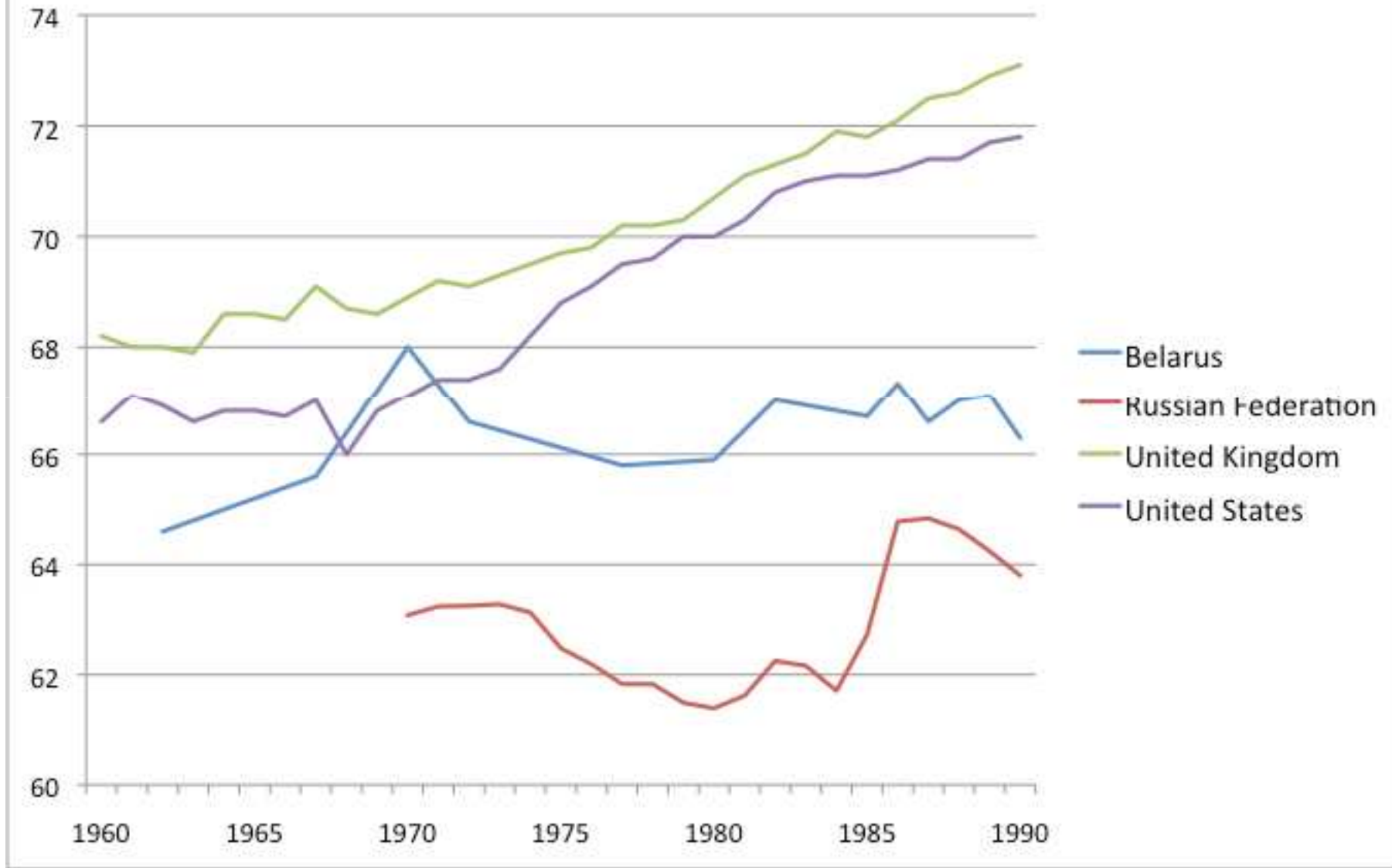
Source: Economagic

Hard currency debts, 1975 and 1989 (\$ billion)



Source: Maddison, *World Economy*

Male life expectancy at birth, 1960-1990



Source: World Bank, WDI

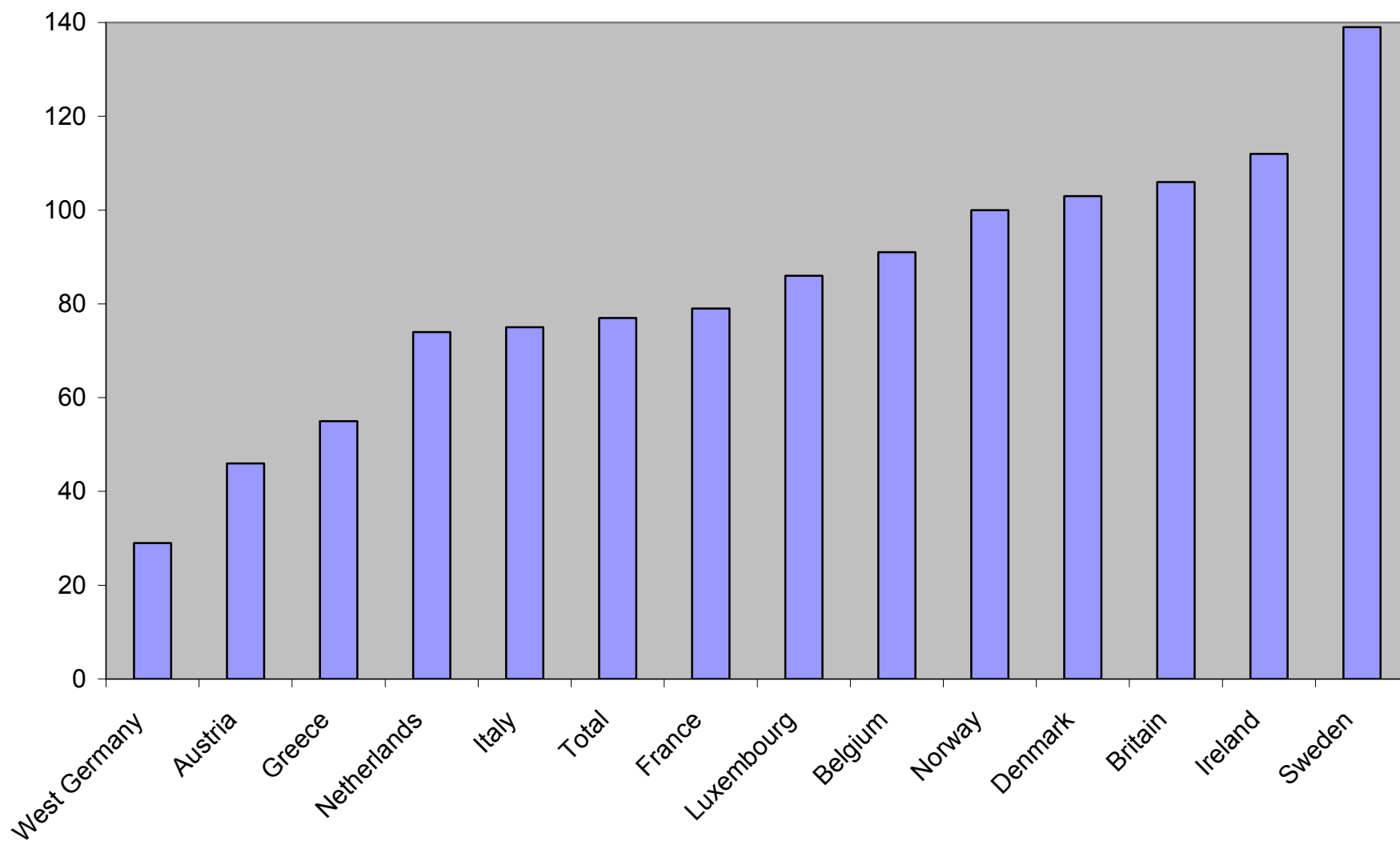
What I used to think:
The Eurocentric narrative

Europe's predicament in 1947

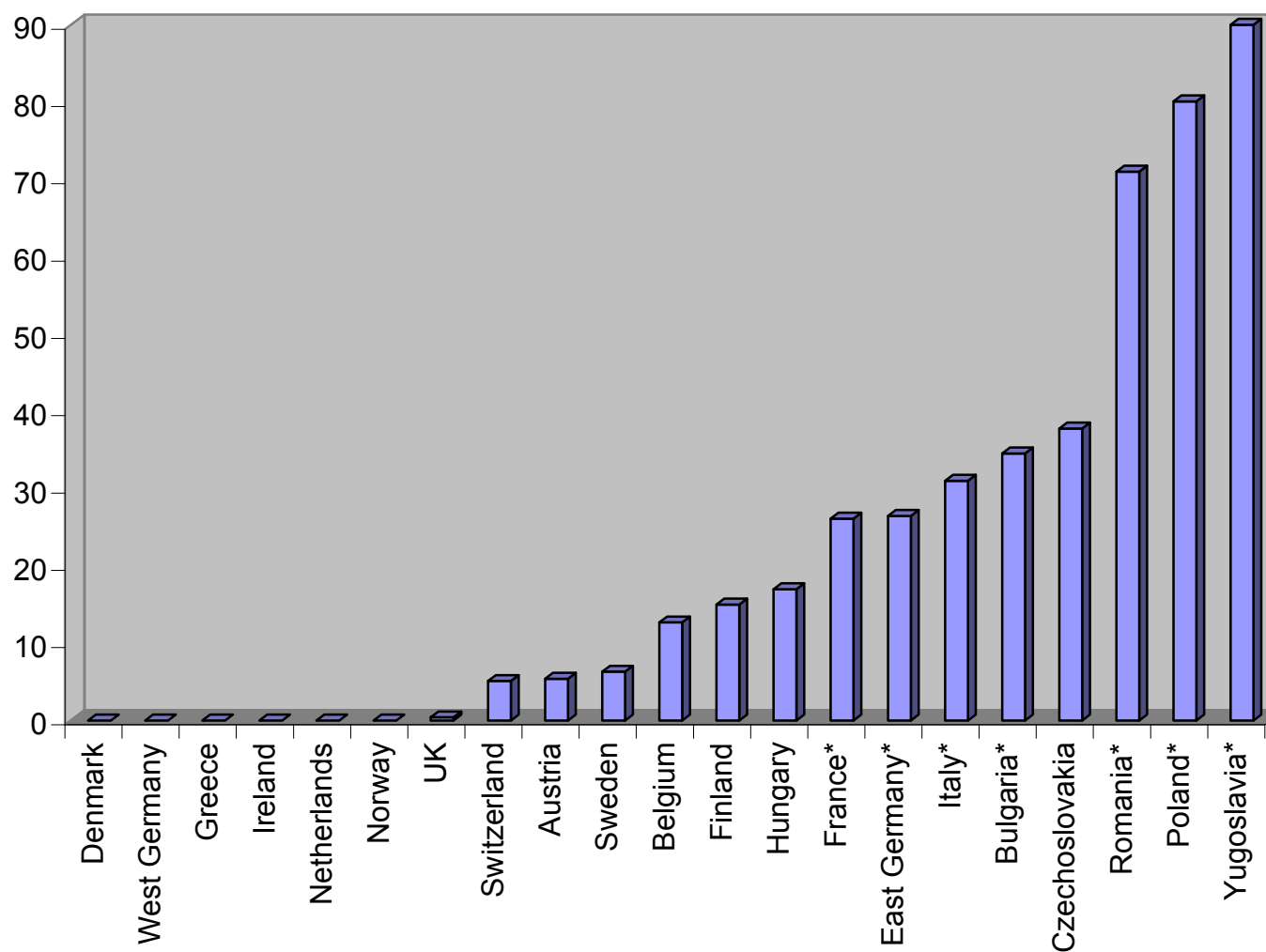
- Population up 10%, despite death toll of war
- Industrial production down 40%
- Reduction of overseas invisible earnings and worsening terms of trade reduce capacity to import by 40%



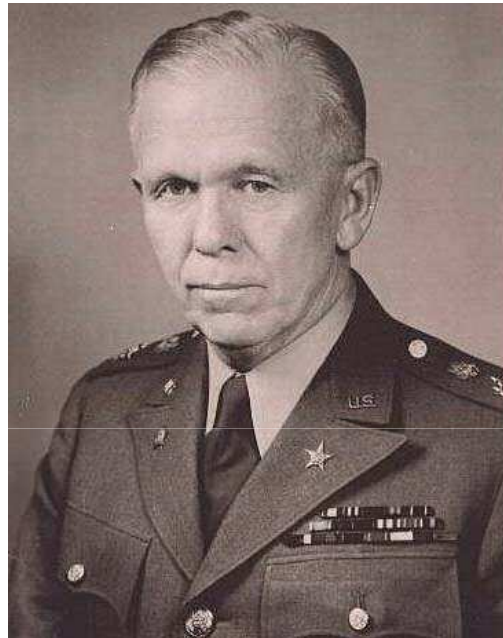
Industrial production, 1946 (1938=100)



Percentage of votes going to Communist parties/coalitions (*) in post-war elections

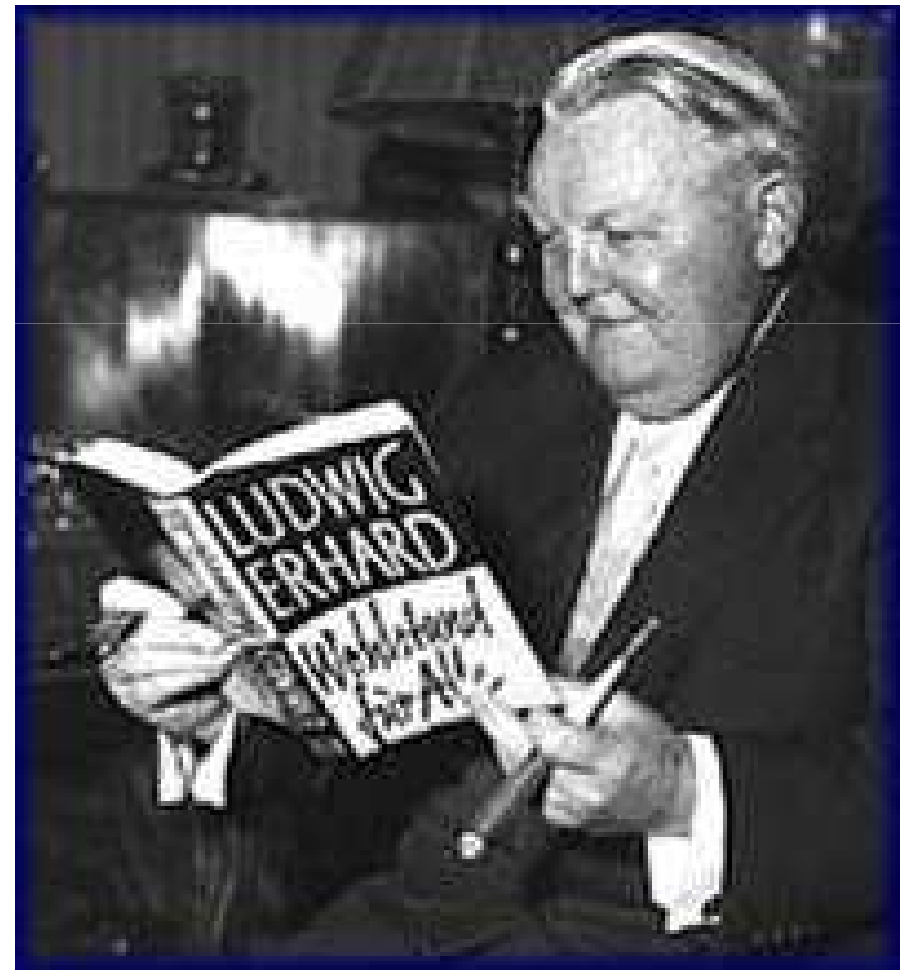


The traditional answer: Marshall's Plan

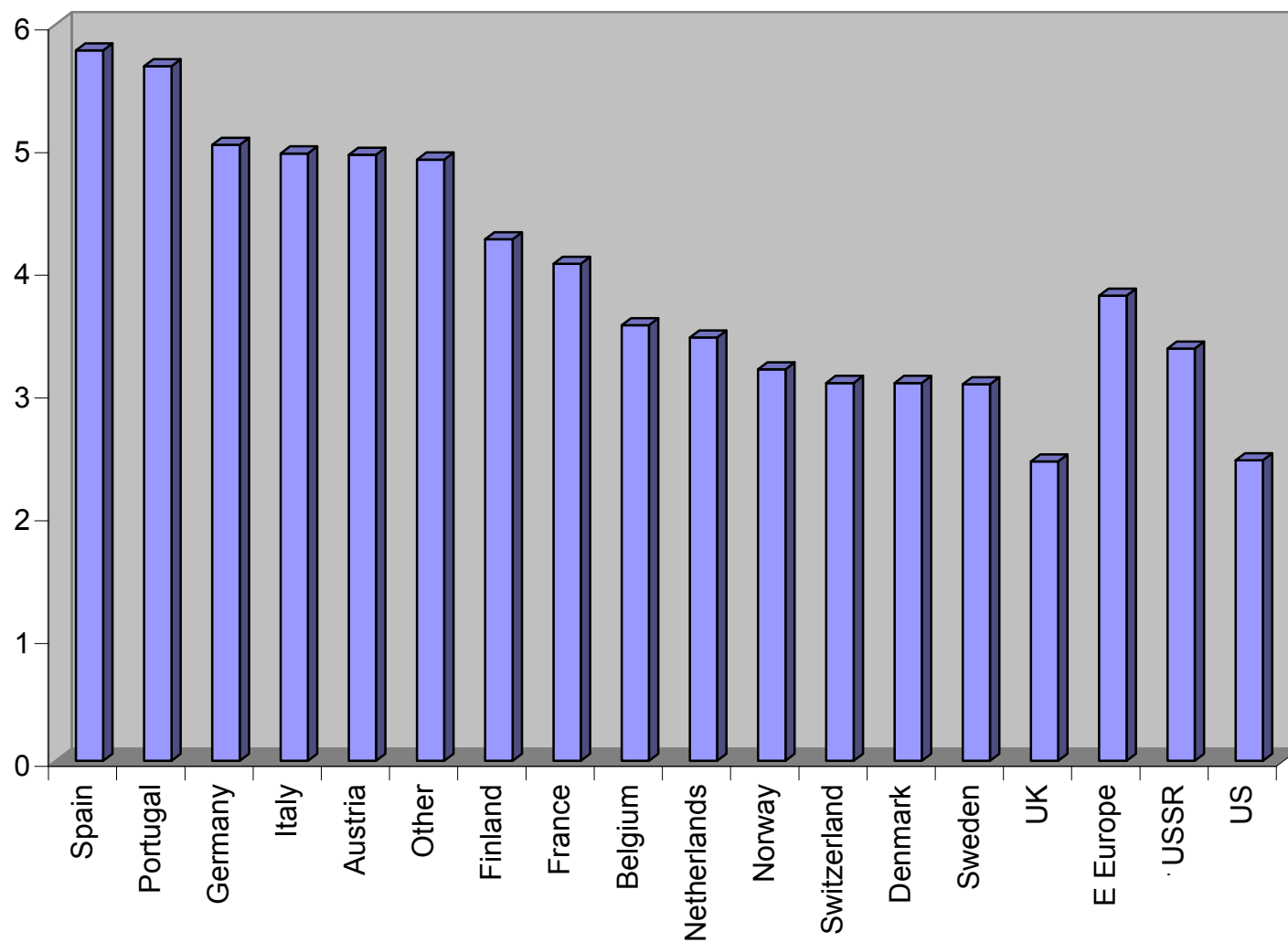


‘Europe ... must have substantial additional help or face economic, social, and political deterioration of a very grave character.’ – at Harvard, June 5, 1947

Causes of the post-war 'miracles'



Growth of per capita GDP, annual average compound rate, 1950–73

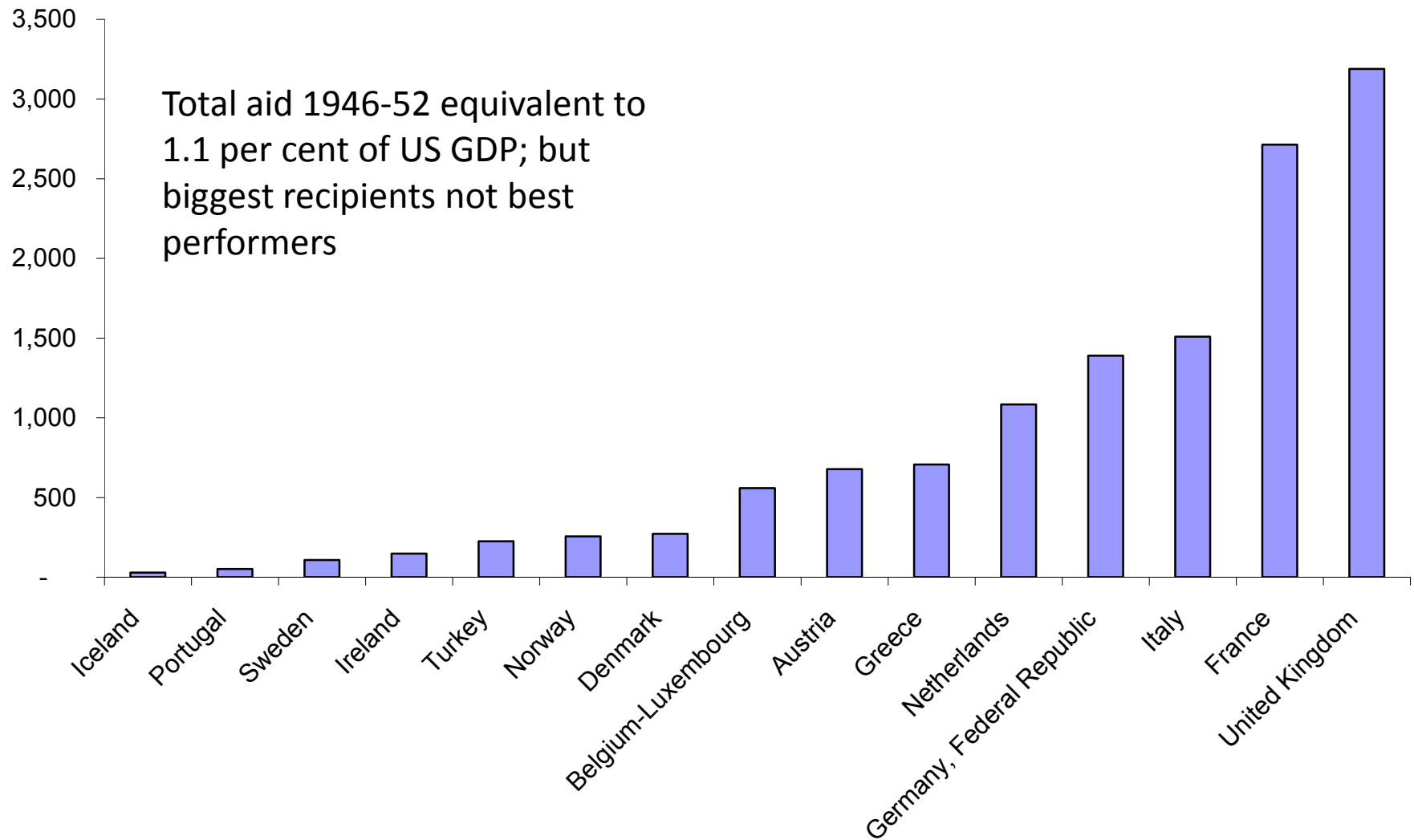


Source: Maddison, *World Economy*

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

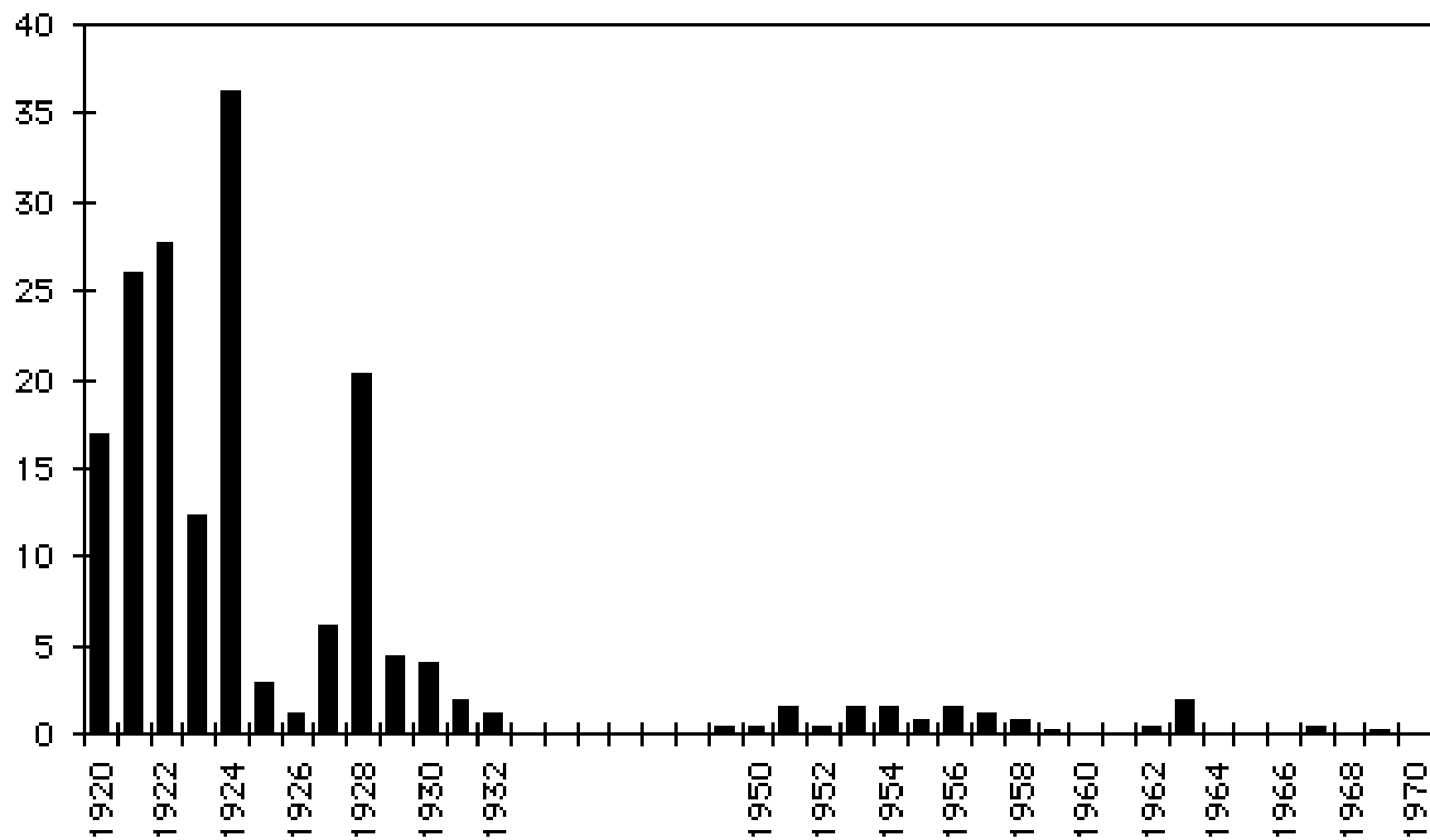
Marshall Aid: Total grants and loans, 1948-1952 (million dollars)



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

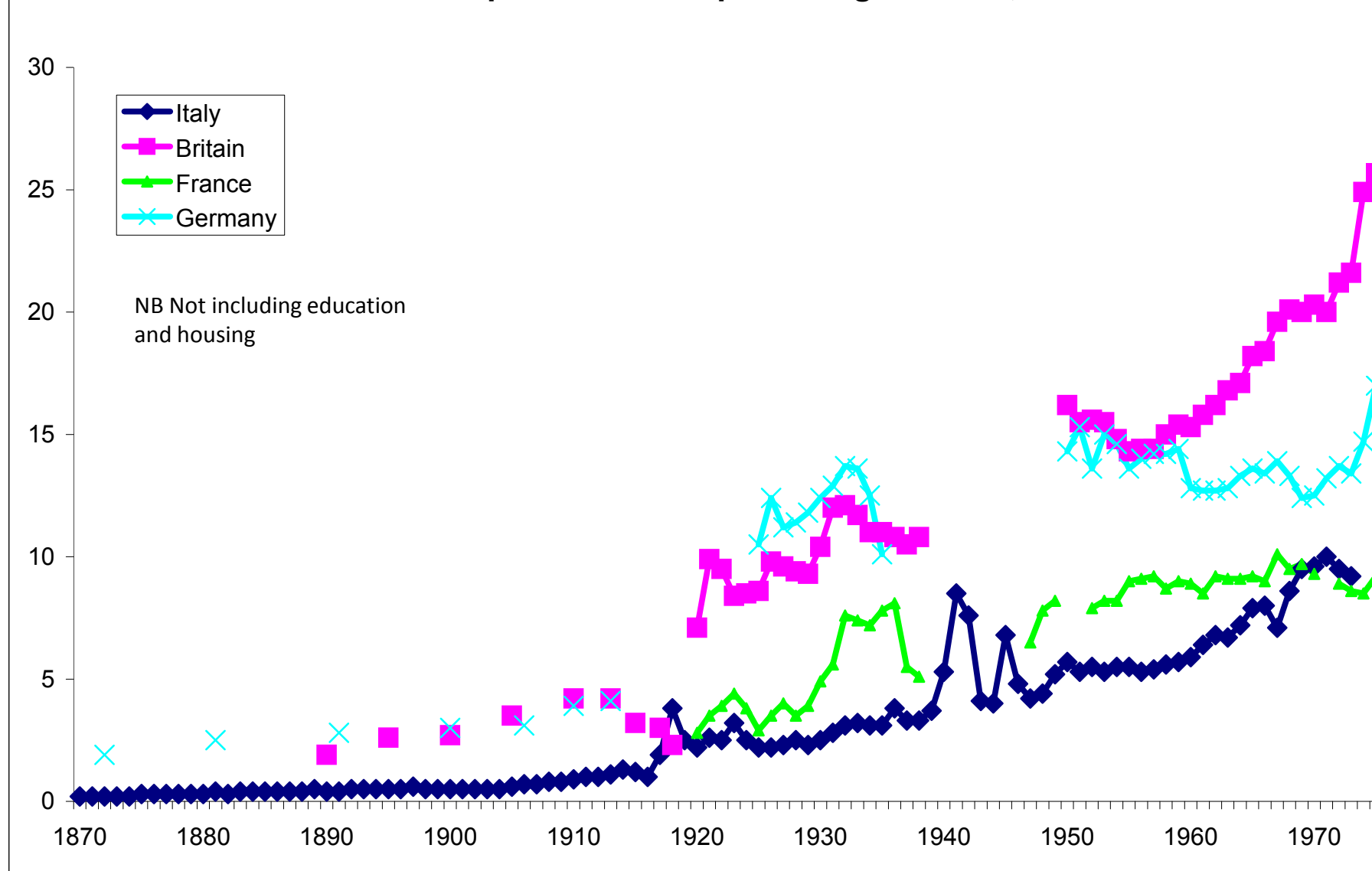
Days Lost to Strikes (Millions)



(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



(b) Versus 'real existing socialism'

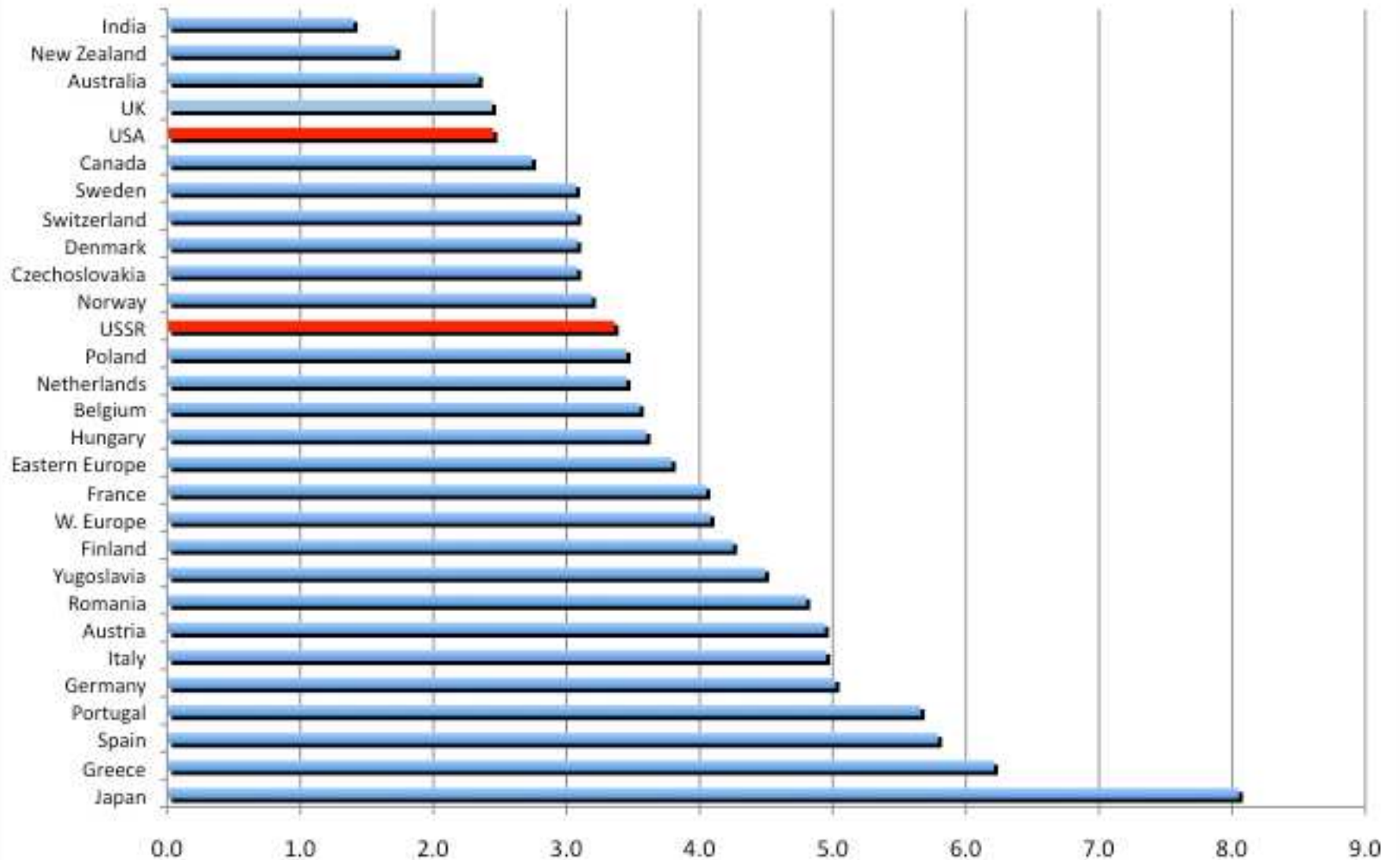
- Soviet exactions: c. \$14 bn.
- Five and Six Year Plans
 - Heavy industry and urbanization
- Collectivization
 - Esp. Baltic states, Romania
- Forced labor
 - Danube-Black Sea Canal
 - Bulgaria 100,000 slaves, 361,000 workers
- The 'New Class' (Milovan Djilas)

Catch: The West's slide into 'stagflation'



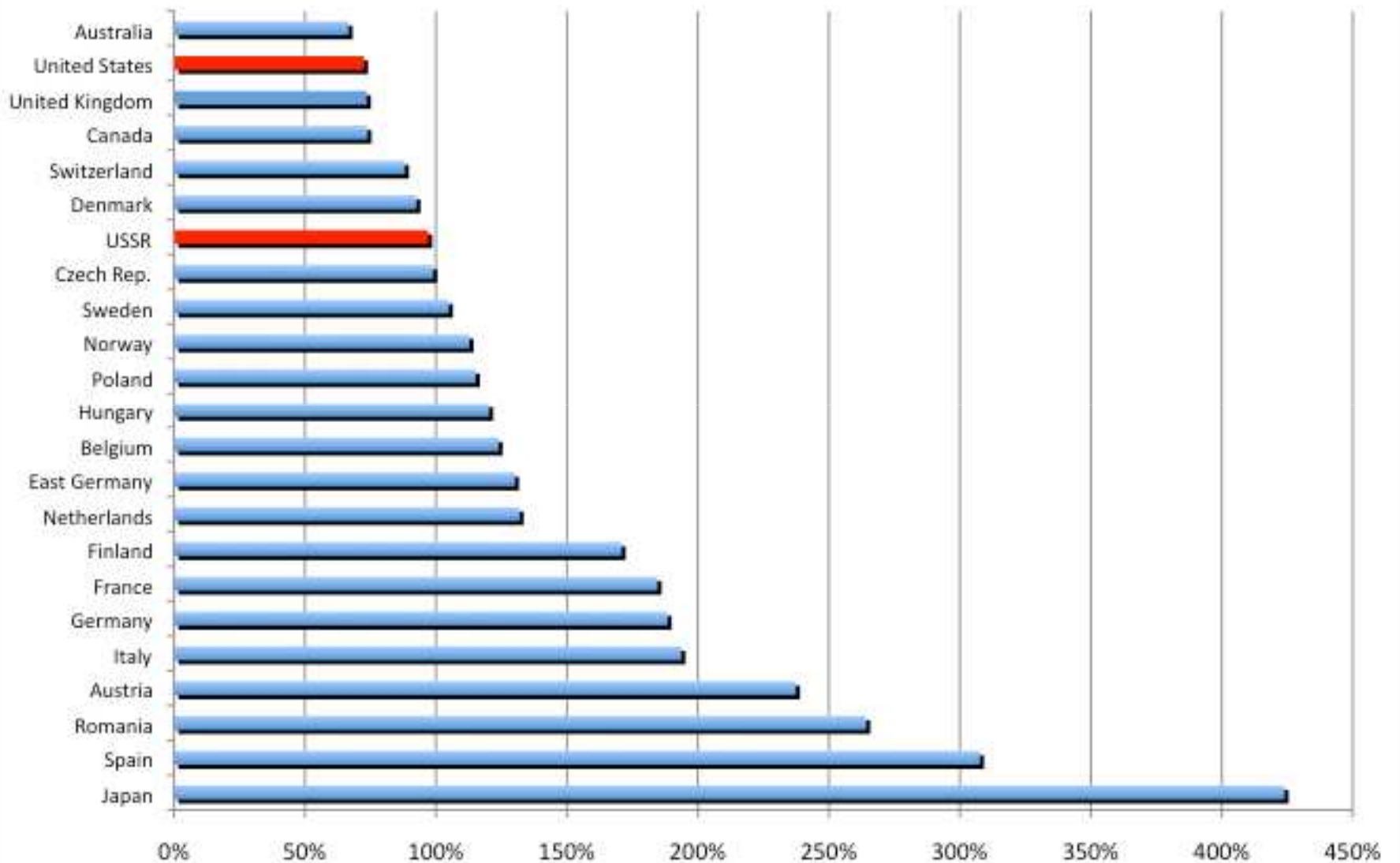
"This may not be as simple as I thought!"

Real per capita growth rate, annual average, 1950–73



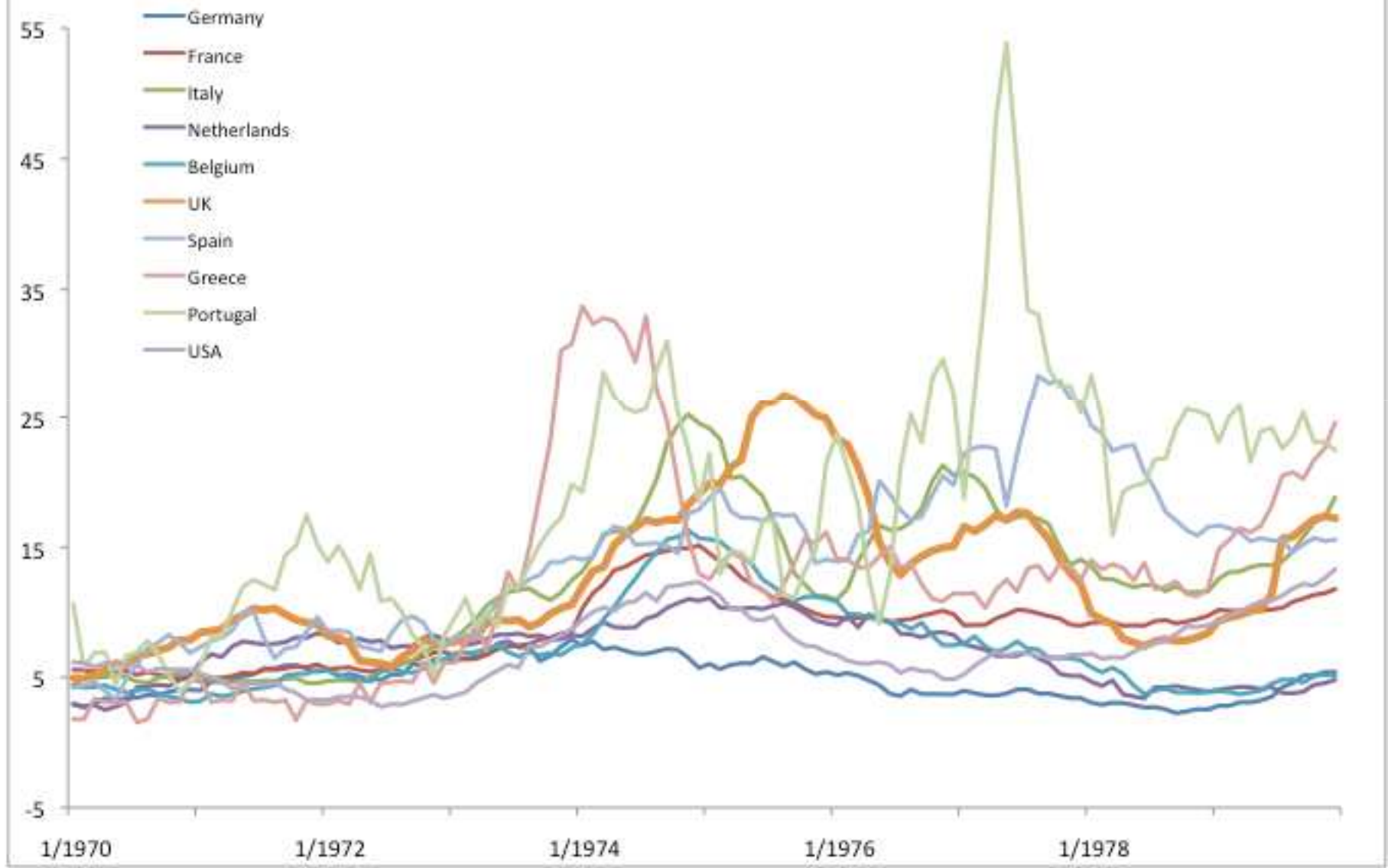
Source: Maddison, *World Economy*

Percentage increase in real GDP per person employed, 1950-1973



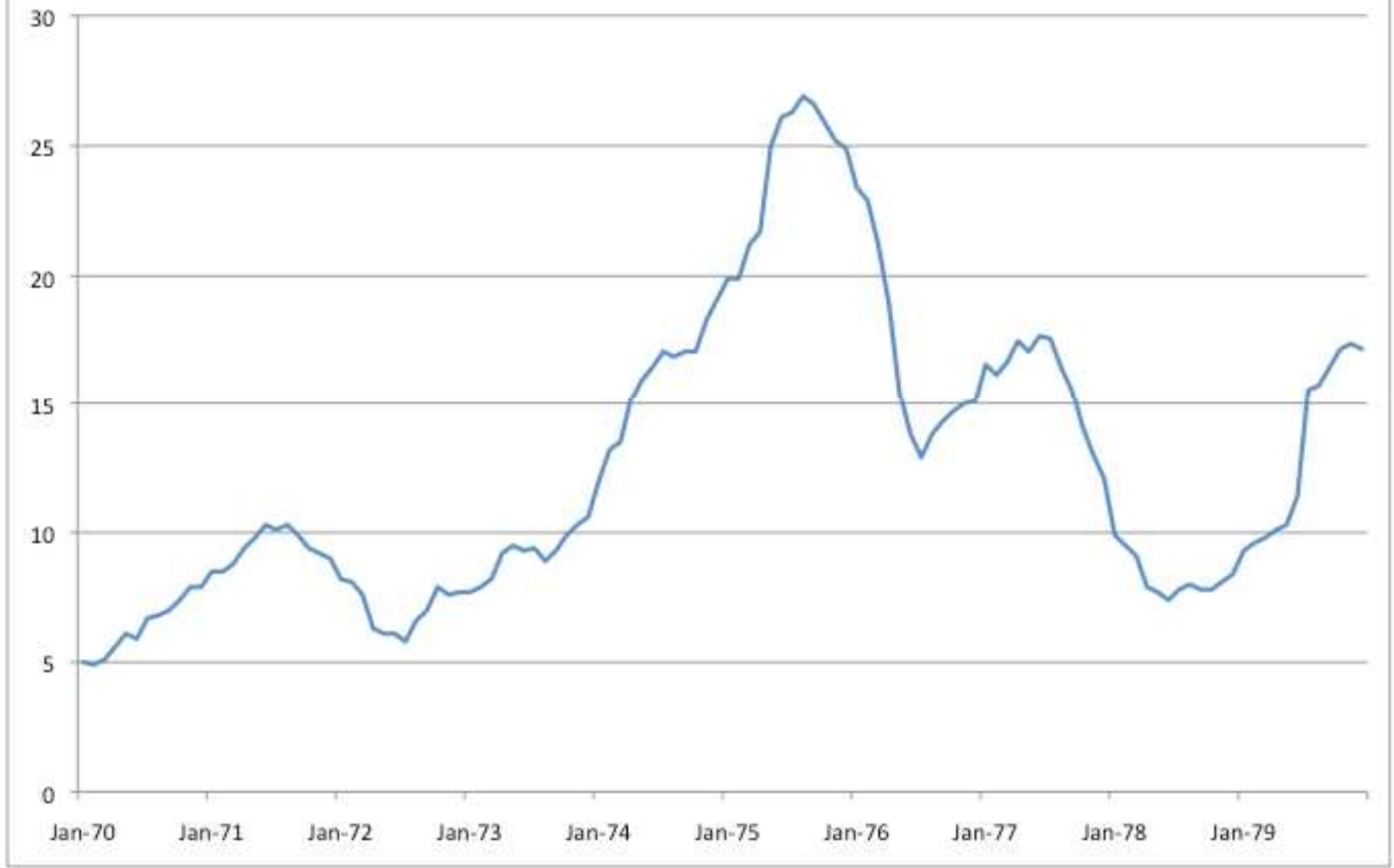
Source: Maddison, *World Economy*

Annual inflation rates, selected OECD countries, 1970-1979

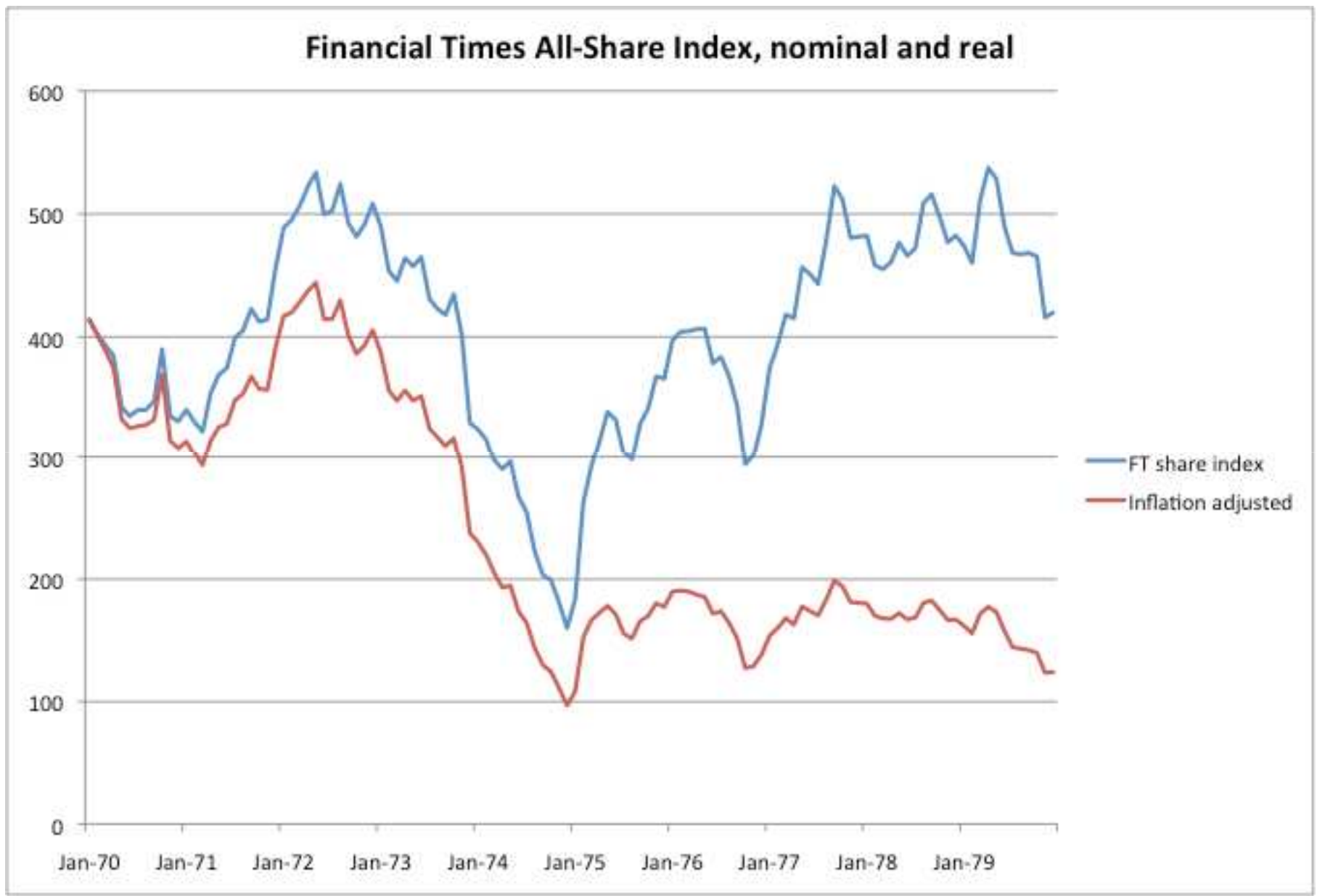


Source: OECD

UK retail price inflation rate, 1970-1979

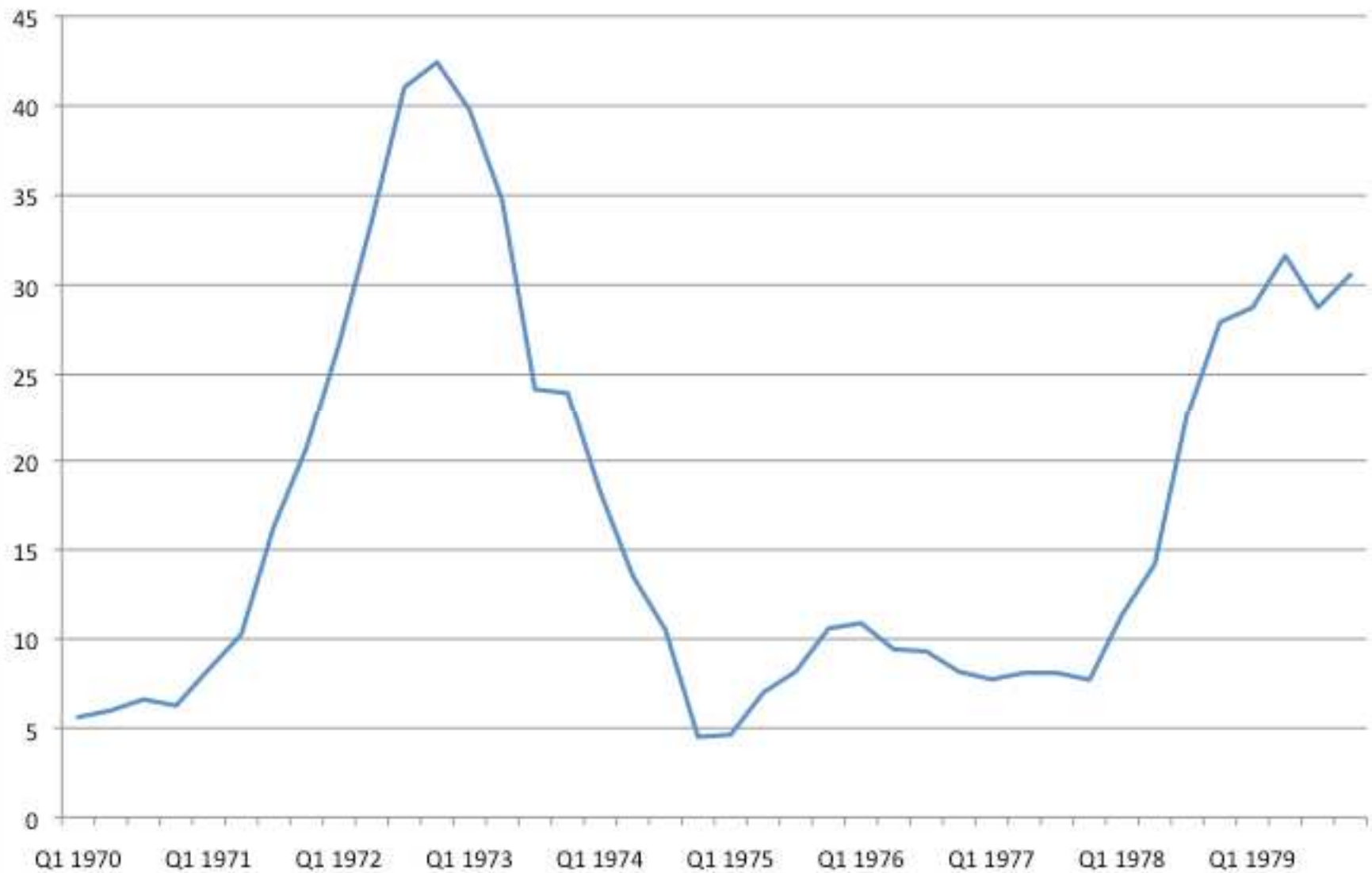


Source: ONS



Source: Global Financial Data

UK house prices, annual percentage change, 1970-1979



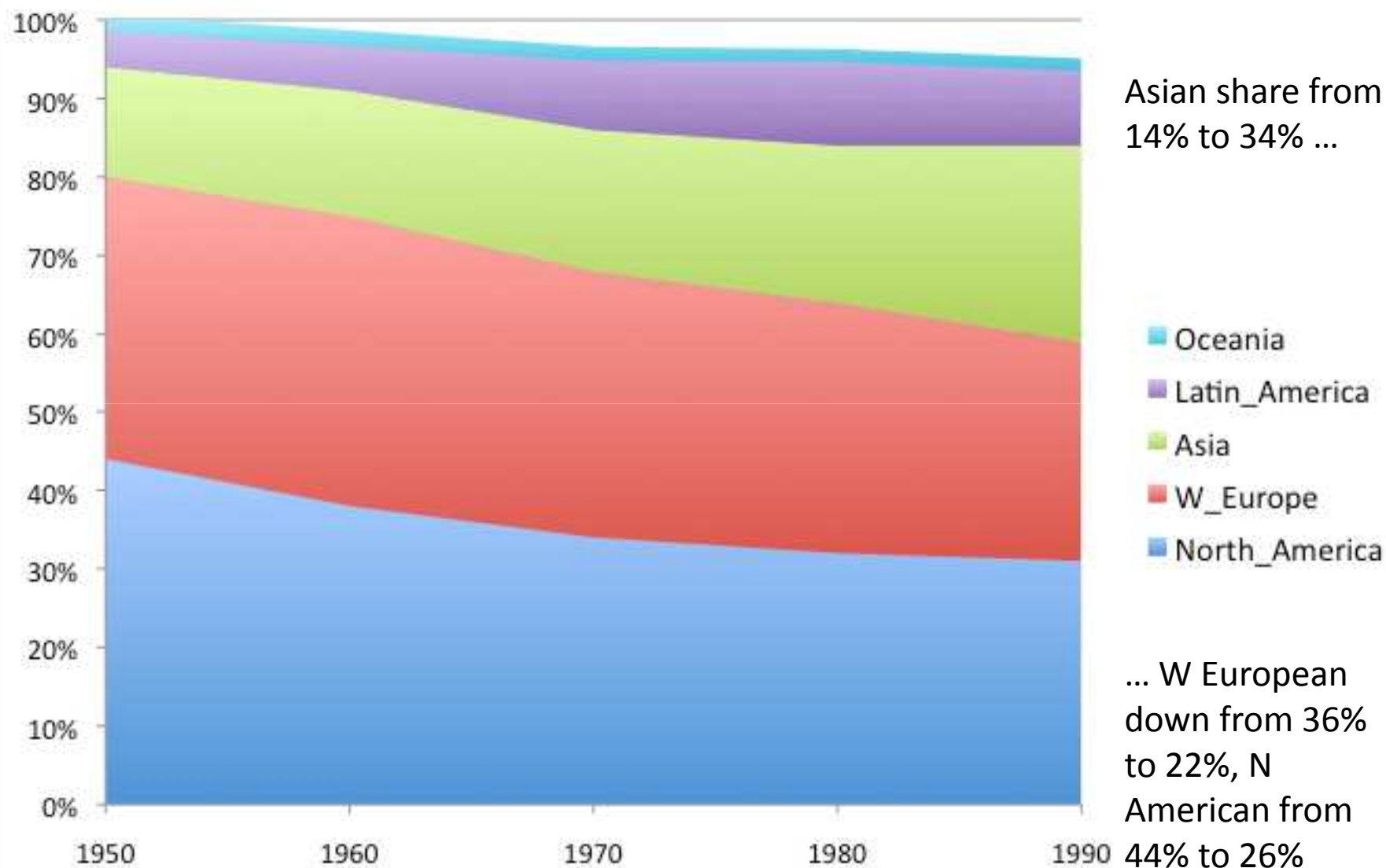
Source: Nationwide

What I think now:
East Asia as the key

The view from the East

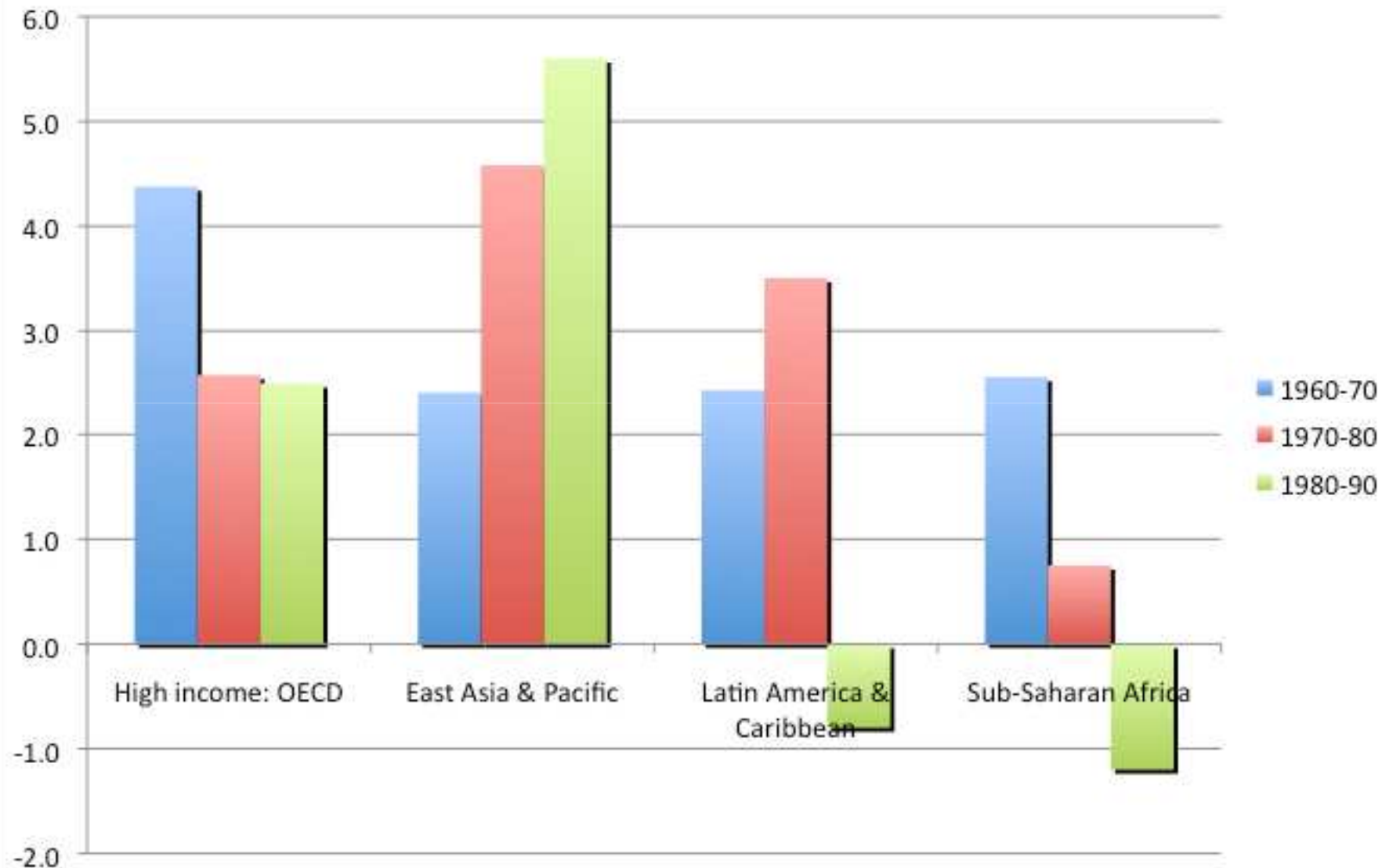
- West European success was not the surprise of the post-war period
- Asian growth was much more remarkable
- We need to give more weight to American occupations in Japan and South Korea
- Also Hong Kong, Malaysia, Singapore, Taiwan and even Indonesia
- The Soviets fared much better in Latin America 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

Shares of global GDP, 1950-1990



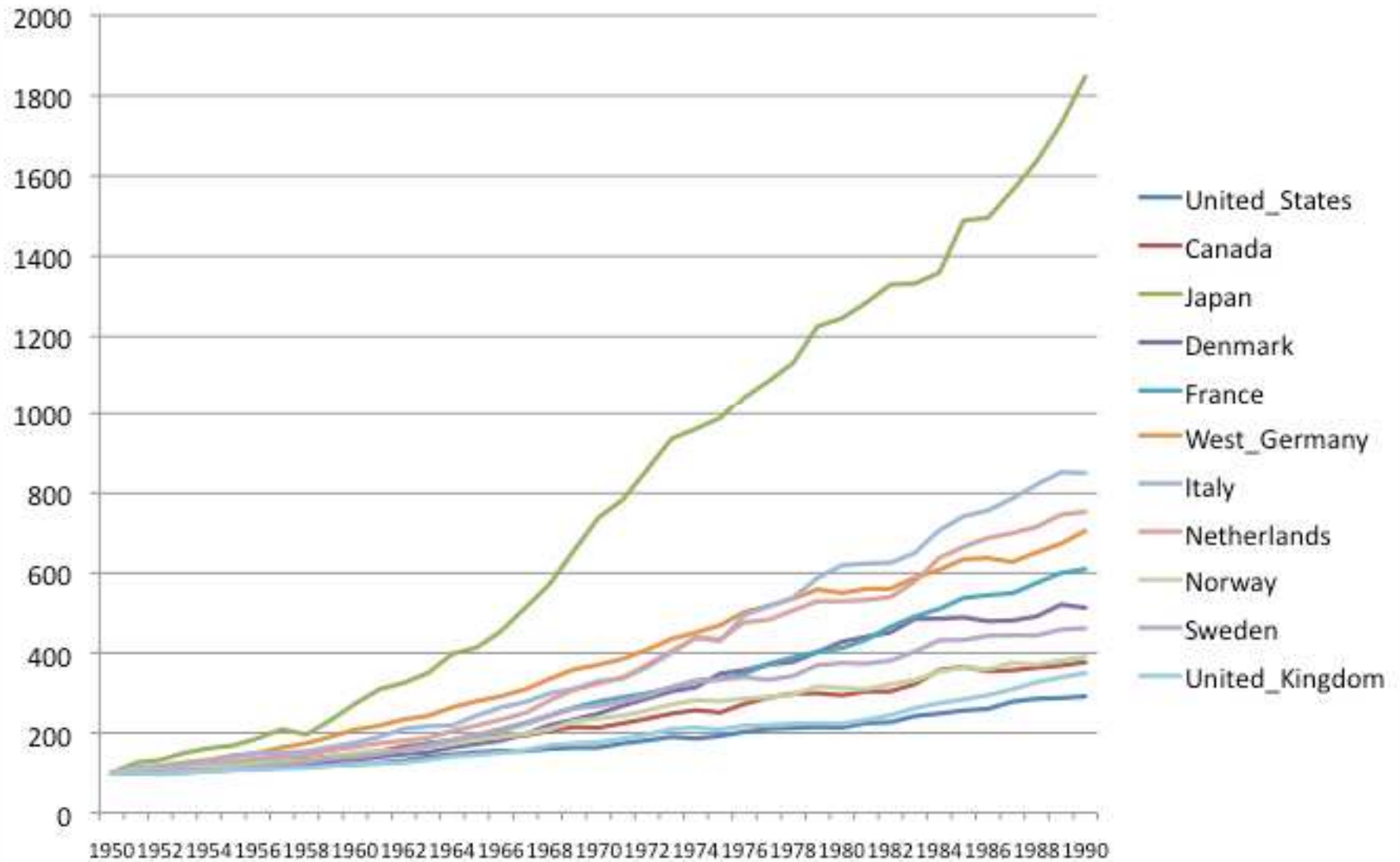
Source: Bridgewater

Real per capita GDP average annual growth rates, 1960-1990



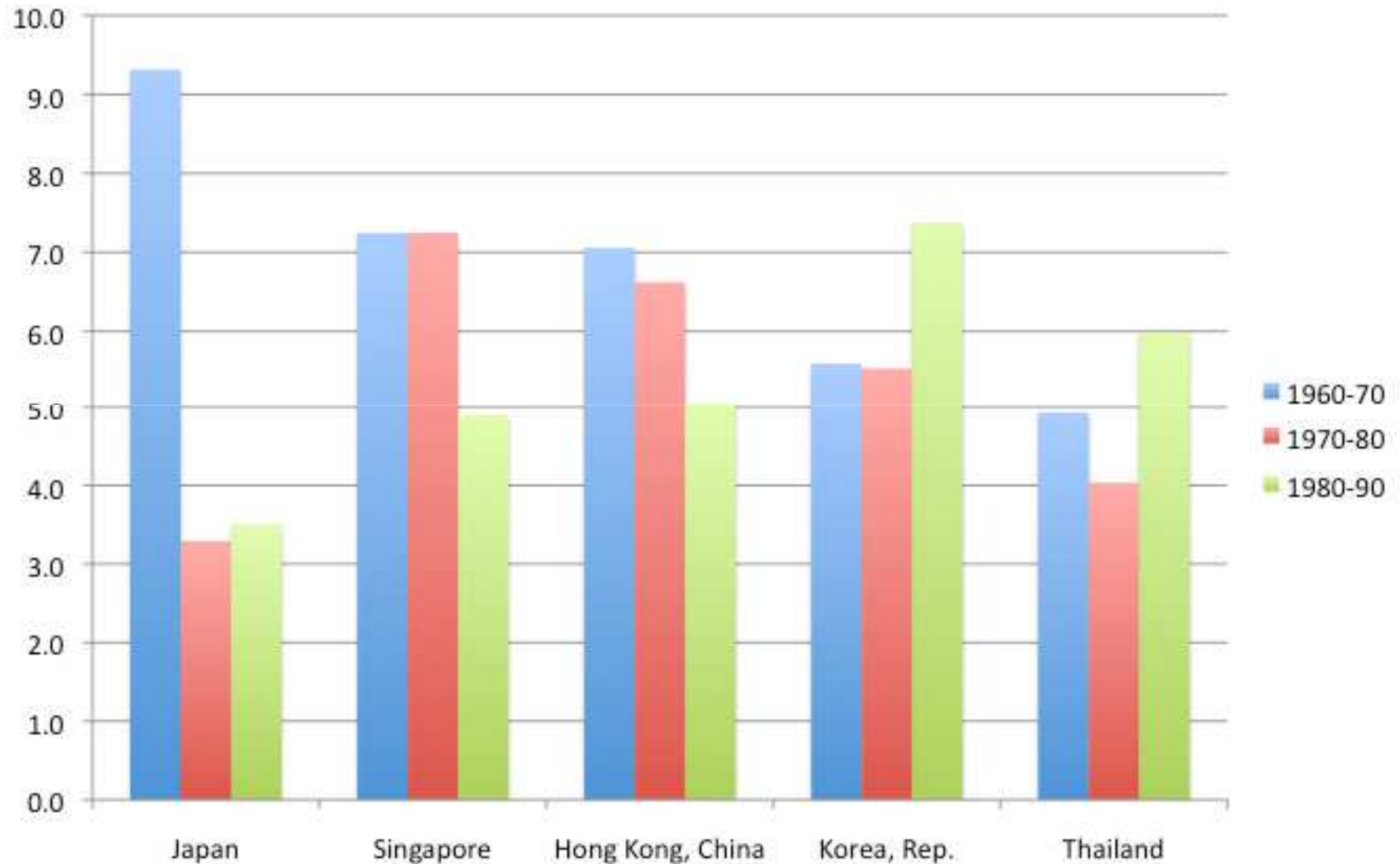
Source: World Bank, WDI

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



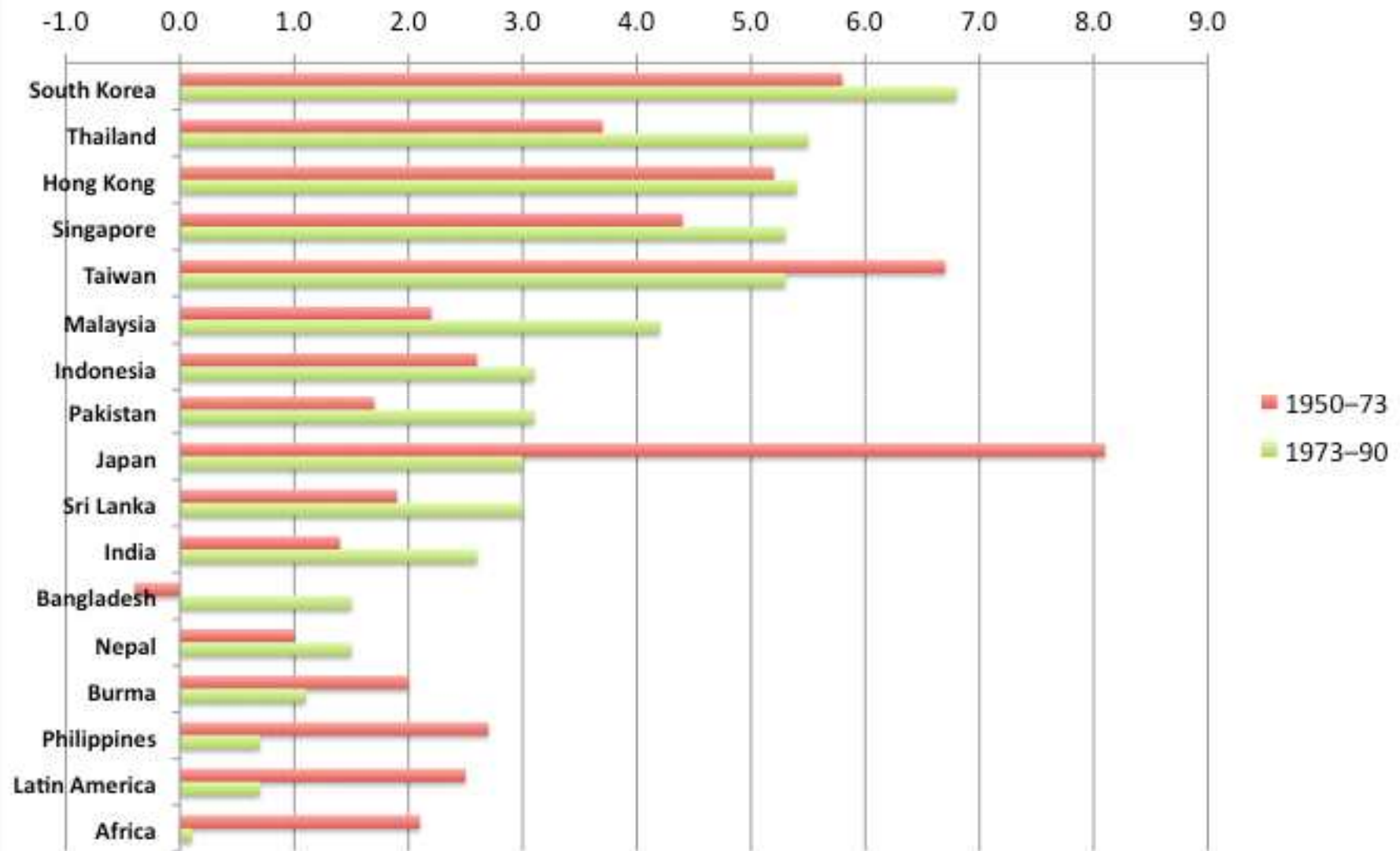
Source: OECD

Japan and the Asian Tigers, 1960-1990



Source: World Bank, WDI

Asian growth in comparative perspective, 1950-1990



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

‘Successes’

- Iran (1953)
- Guatemala (1954)
- Congo (1961)
- Brazil (1964)
- Dominican Republic (1965)
- Chile (1973)

‘Failures’

- Indonesia (1957)
- Cuba (1959)
- South Vietnam (1964-1975)
- Angola (1975-76)
- Ethiopia (1977)
- Afghanistan (1979)

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