# The development of the Global Economy

## Topic 1: Reasons for the Growth of the Global Economy

SAJC History Unit, 2024

# Learning Outcomes (from the Examination Syllabus)

**Students are able to:**

- evaluate the factors that contributed to the growth of the global economy over time
- evaluate the challenges that affected the global economy over time
- evaluate the factors that contributed the factors that contributed to the economic transformation of Japan and China over time

# Essential Questions for this topic:

- ***How did the global economy develop?***
- ***How did the development of the global economy impact different countries?***

***Questions set will not require candidates to compare the economic transformations of Japan and China***

# Guiding Questions for this topic:

- What is the definition of the term, "global economy?"
- What are the factors that shaped the development of the global economy from 1945 to 2000?
- When did the growth of the global economy take place? How was it like and why did it manifest the way it did?
- When did the challenges in the global economy take place? How was it like and why did it manifest the way it did?

# 1. Defining the term, "global economy"

1. *"The global economy has always existed…What keeps changing is the nature of the global economy…"* - Louis Uchitelle, a journalist, 2002

2. The definition of what constitutes a "global economy" has changed over time: the global economy is the economy of the world, as an international exchange of goods and services.

**What are some economic concepts that would be helpful?**

### A. Free Trade

- Free trade refers to the unhindered flow of goods and services between countries.
- Trade can be hindered by trade barriers such as tariffs (an additional charge imposed on imports) or other policies such as subsidies, taxes and regulations that give domestic firms an advantage over foreign ones. The policy of imposing such barriers to trade is known as protectionism.

### B. Exchange Rates

- There are two types of exchange rates systems that you would need to know:☐ The floating exchange rate system and the fixed exchanged system.
- The **floating exchange rate system** means that the value of a country's (let's say Singapore) currency is dependent solely on the foreign demand for that country's products. Since demand changes daily, the value of the Singapore dollar will keep fluctuating.
- The **fixed exchange rate system** functions such that the government of the country fixes and guarantees the official price of the currency in terms of a foreign currency. Under this system, the government is committed to maintain the fixed exchange rate by using its reserves (gold and foreign exchange) to exactly offset the changes in foreign demand.

3. The definition of what constitutes a "global economy" has changed over time:

   a. **Immediate post-1945 period**: referred to the **developed capitalist world**, namely the **USA, Western Europe, and Japan**

      i. The Communist bloc was excluded from this "global economy" as it was politically and ideologically isolated.

ii. The Afro-Asia developing countries were also absent as they were still under colonial rule.

iii. It is in this context that the development of the international economy is laid against. All countries in the world found themselves influenced by the two superpowers (USA and USSR) and the two superpowers competed to influence everyone else, especially in the Third World after the capitalist bloc and socialist bloc were formed.

iv. **1970s:** Other blocs became more integrated with the **developed capitalist** one, resulting in the global economy witnessing greater interdependence among nations, and becoming more global in nature.

v. **1990s:** The Communist and Afro-Asian blocs joining the global economy in the 1970s had somewhat diluted its liberal Western capitalist nature.

   **a.** However, the **1990s would see a shift back to the global economy being more closely aligned with the liberal Western capitalist economy** because of changes in the Third World such as the end of Soviet control over Eastern Europe in 1989.

4. The study of History involves **periodisation**, and this involves segmenting a larger block of time e.g., 1945-2000 into smaller time periods marked by seminal events. An exploration into the growth and decline of the global economy would thus be helped by dividing 1945-2000 as follows:

   a. **1945 to ~1971:** The "**Golden Age of Capitalism**", synonymous with the period of **economic liberalisation**. This can be further subdivided into:

      i. **1945 to late 1960s:** Early growth years.

ii. **Late 1960s to ~1971:** Later growth years; U.S. deficits had emerged in the 1960s and would begin to have an impact subsequently. Issues with the Bretton Woods system began to surface by around 1971.

b. **~1971 to 2000:** The 'Crisis' Decades, included (but are not limited to) key events / periods such as:[1]

i. **1971:** Nixon's devaluation and the end of the fixed exchange rate; also known as the **'Nixon Shock'**

ii. **1973:** The "First Oil Shock / Crisis"

iii. **1979:** The Iranian Revolution (1979) and the "Second Oil Shock / Crisis"

iv. **1991 to 2001:** The "Lost Decade" in Japan

# 2. The Post-WWII Economic Situation in 1945

1. As History students, our intellectual curiosity should motivate us to investigate how a post-WWII world could see the advent of the "Golden Age of Capitalism" when WWII had ravaged many of the major economies, such as those of Britain and France. Also, against the backdrop of the Cold War and the divisions it contributed to, how did economies become increasingly interdependent and interconnected during this period?

## 2.1 Post-WWII Alignments

1. The end of World War II saw the **realignment of the world's nations into three distinct groups**, also popularly known as the First, Second (not a commonly used term) and Third Worlds.

[1] We will delve into a more detailed set of events when investigating the problems of economic liberalisation.

a. **First World** = the so-called "free world" which consisted of the USA, most of Western Europe and Japan, later known as the developed world
b. **Second World** = the socialist bloc made up of the USSR and its allies/satellite states, especially in Eastern Europe
c. **Third World** = the former colonies (mainly in Asia and Africa) which came to be known as the developing world

### 2.2 Quest for Peace and Sustained Wealth

1. When the war ended in 1945, the search for a lasting peace began. After the large-scale devastation brought upon by the two world wars as well as the misery suffered during the interwar years (depression), people all around the world yearned for peace and prosperity.
2. With the emergence of the two superpowers – USA and USSR, and the simultaneous decline of the old colonial powers, the political and economic landscape was inevitably shaped by the contrasting ideologies of capitalism and communism as both systems sought to prove that it was better than the other.
3. It is in this context that the development of the international economy is laid against. All countries in the world found themselves influenced by the two superpowers and the two competed to influence everyone else, especially in the Third World after the capitalist bloc and socialist bloc were formed.

## 3. Analysing the growth of the "global economy": The "Golden Age of Capitalism" (1945 to ~1971)

1. The learning outcome of the syllabus requires us to "evaluate the factors that contributed to the growth of the global economy over time" and to do so, we need to understand what contributed to the "**Golden Age of Capitalism" (1945 to ~1971)**, a period synonymous with **increased economic liberalisation**.

2. It is critical to avoid seeing the period of 1945 to ~1971 as a period of linear growth for all countries. Instead, it is imperative that we understand the arguments for and against terming the period as the "Golden Age of Capitalism".

## 3.1 Evidence Supporting 1945 to ~1971 as the "Golden Age of Capitalism"

1. The period of 1945 to the early 1970s witnessed impressive unprecedented economic growth compared to the pre-WWII period

2. The "Golden Age of Capitalism" was validated by a range of quantitative and qualitative economic indicators e.g., % GDP and GNP growth; low costs of production and prices; high employment; low taxes; high and rising income; mass consumerism; and so on.

   a. For example, these were the **rate of economic growth averages** (in brackets) for the following countries from the **1950s to the 1960s**: Japan (9.8%); West Germany (6.3%); Italy (5.6%); Finland and France (5% respectively); USA (3.5%); UK (2.8%).

3. It was the **capitalist world that dominated much of the early development of the international economy**. The world witnessed unprecedented growth from the 1950s till the early 1970s. This period would be known as the "Golden Age of Capitalism".

### 3.1.1 Rates of Growth

1. The world economy indeed grew at an explosive rate. World output of manufactures quadrupled between the early 1950s and the early 1970s. World trade in manufactured products grew tenfold. World agricultural output also shot up, mainly through increases in productivity; grain yields per hectare almost doubled between the early 1950s and the early 1980s and more than doubled in North America, Western Europe and East Asia. World fisheries trebled their catches.

2. The OECD (Organization for Economic Cooperation and Development) countries had an average GDP growth rate of over 4% in the 1950s, 5% in the 1960s as compared to 3% in the 1970s and 4% in the 1980s.

3. From being one of the most devastated countries after WWII, both Japan and Germany recovered to consistently achieving double-digit growth. At its peak period, 1966-1970, Japan experienced a staggering 14.6% growth.

4. Most developed economies enjoyed almost full employment in the 1960s, with Europe's unemployment rate only at an average of 1.5% (though Italy's was 8% in the 1950s) and Japan's only 1.3%.

5. It was a period of remarkable financial stability. Martin Wolf of the Financial Times reported that in the 27 years between 1945 to 1971, there were only 38 financial crises, while in the 24 years from 1973 – 1997, there were 139 crises!

### 3.1.2 The Rise of Industrialism

1. Industries emerged and re-emerged everywhere. Besides the recovery of West Germany and Japan to their pre-war industrial capacity <u>and beyond</u>, there were other dramatic examples of industrial 'revolutions' in Spain and Finland. Previously purely agrarian countries like Bulgaria and Romania acquired massive industrial sectors.

2. In the Third World the most spectacular development of the "newly industrializing countries" (NICs) occurred after this period, but everywhere the number of countries depending primarily on agriculture diminished sharply such that by the 1980s, a mere 15 states paid for half their imports or more from farm exports.

### 3.1.3 The Growth of the Automobile Industry

1. Initially, this astonishing explosion of the economy seemed merely a gigantic version of what had gone before in that it seemed a globalization of the pre-1945 US economy and society.

2. The age of the automobile had long arrived in North America, but during the "Golden Age," it came to Europe and, later and more modestly, to the socialist world and to the Latin American middle classes.

3. Cheap fuel made the bus and the truck the major means of transport over most of the globe's land mass.

4. The rise of European affluent society could be measured by the increase in car ownership (in Italy from 469,000 in 1938 to fifteen million in 1975). The economic development of many Third World countries could be measured by the increase in the number of trucks on its roads.

### 3.1.4 The Consumer Boom

1. Much of the great world boom was a consumer boom. The rest of the world caught up with the USA while, in the USA itself, old trends continued in new ways.

2. The principle of mass production pioneered by Henry Ford spread to other countries, while in the USA Fordist methods were extended to new kinds of production, from house building to junk food.

3. Benefits previously enjoyed exclusively by the ‘affluent society’ became general by the 1960s and were now produced for a mass market. In the home, what had once been luxury became the expected standard of comfort - the refrigerator, the washing machine, the telephone. It was now possible for the average citizen in the developed countries to live as only the very wealthy had lived in his parents' day.

### 3.1.5 Technological Innovation

1. The most striking feature of the economic surge is the way it was powered by technological innovation   television, recording on magnetic tape, integrated circuits, lasers, various spin-offs from space research, nuclear energy, electronics, information technology.

2. More than any other period, the "Golden Age" rested on the most advanced scientific research, which often found practical application within just a few years, bringing about significant impact:

3. **First, it totally transformed everyday lives of people worldwide.**

    a. In the rich world, the contents of fridge or freezer (neither of which most homes would have owned in 1945) attest to this: freeze-dried food; factory farmed poultry produce; meat stuffed with enzymes; products imported by air from halfway across the world.

    b. Likewise, the possessions of a "normal" household in the rich world TV, vinyl records (LPs came in 1948), tapes (cassettes came in the 1960s), compact discs, digital watches, pocket calculators point to how the benefits of technology were widely spread.

    c. Not the least significant feature of these innovations was the systematic process of miniaturization, i.e. portability, which vastly extended their potential range and market.

    d. To a lesser extent, the poor world also witnessed tremendous changes - radio could now reach the remotest village thanks to the transistor and the miniaturized long life battery, where the "green revolution" transformed rice and wheat cultivation and where plastic sandals replaced bare feet.

4. **Second, ‘Research and Development’ (R&D) grew more prominent.**

    a. With the involvement of more complex technology, naturally, the progress from discovery or invention to eventual practical production grew more complex.

    b. The tremendous costs involved in R&D also saw the rise of patents – in industries such as pharmaceutical chemicals, drugs were protected from competition by patent rights, generating many profits which were rationalized based on grounds of future research and innovation.

c. The growing primacy of R&D in the global economy thus reinforced the already enormous advantage which the advanced economies enjoyed over the less developed countries, and which large firms enjoyed over small.

5. **Third, the new technologies were, overwhelmingly, capital intensive and labour saving or even labour replacing.**

    a. The major characteristic of the "Golden Age" was that it needed constant and heavy investment and, increasingly, that it did not need people except as consumers of goods and services.

    b. Automated robots assembled cars, computers controlled output of power and trains could function without drivers. Mechanization of various industries rendered labour less critical except for the highly skilled scientists and technicians, who could then command high wages.

    c. Such innovation plausibly allowed new technologies and industries to thrive due to a reduced dependency on labour.

6. In light of the abovementioned economic situation, the 1960s led to some observers beginning to assume that everything in the economy would go onwards and upwards forever. The remarkable period of growth gives one the impression that all the problems which had haunted capitalism in the 1930s seemed to dissolve and to disappear.

7. The terrible and inevitable cycle of boom and slump became a series of mild fluctuations (though the Keynesian economists who advised governments were convinced that this was due to their intelligent macroeconomic management).

8. Mass unemployment was history - in the 1960s, the unemployment rate in Europe averaged 1.5% and in Japan 1.3%.

9. Poverty? Of course, most of the world remained poor, but, in the rich countries, the ordinary industrial worker expected to own a car and to take his annual paid vacation abroad and, if he fell on hard times, to enjoy the protection of a

universal and generous Welfare State. His income rose year by year and he expected it to keep on rising forever. The range of goods and services offered by the productive system widened year by year and made former luxuries part of everyday consumption.

10. It should be said that the people of the era did not actually notice the golden age at the start. But in the course of the 1950s, many people, especially in the increasingly prosperous "developed" countries became aware that times were indeed strikingly improved, especially if their memories reached back to the Depression of the Interwar Years.

11. Yet really, it was not until the great boom was over, in the 1970s and 1980s (which were filled with problems), that people began to realize that the world, particularly the world of developed capitalism, had passed through a phase exceptional - indeed unique - in its history.

### 3.1.6 Positive Economic Indicators in the Third World

1. The "Golden Age" was considered a worldwide phenomenon. Even though popular affluence never came within sight of the majority of the world's population (those who lived in the Third World), their economic situation was not bad.

2. Though the population of the Third World grew at a spectacular rate - more than doubling in Africa and Asia 1950 1985 and even more so in Latin America - there was no mass starvation during this period, except as the result of war or political madness, as in China.

3. Indeed, as population multiplied, life expectancy increased by an average of seven years, showing that food production rose faster than population, particularly in the "developing" world. Even so, food production in the developed countries so far exceeded demand by the 1980s that "butter mountains" and "milk lakes" were dumped below cost by the EEC in poor countries, thus undercutting local producers.

## 3.2 Evidence Undermining 1945 to ~1971 as the "Golden Age of Capitalism"

### 3.2.1 The Capitalist Bloc > The Socialist Bloc and the Third World

1. It is now evident that this "Golden Age" belonged essentially to the developed capitalist countries. At the time, however, it looked as if the socialist part of the world had the advantage. The growth rate of the USSR in the 1950s was faster than any western country and the economies of Eastern Europe grew almost as rapidly - although the German Democratic Republic (East Germany) always lagged behind the Federal Republic of Germany (West Germany).

    a. However, the stellar economic performance of socialist economies prompts us to reconsider the title of the **"Golden Age of Capitalism"** because the **Socialist bloc comprised closed economies that were not plugged into the capitalist system**.

        i. The communist world had a closed economy system centred upon COMECON with limited interaction with the rest of the world.

2. Even though the Eastern Bloc lost pace in the 1960s, its per capita GDP over the whole of this period grew slightly faster (in the case of the USSR alone, slightly slower) than in the major capitalist economies. We now know, however, that the enormous natural resources of the socialist economies (especially the USSR) were obscuring their fundamental defects.

3. The 1962 World Economic Survey noted that trade of the developed market economies, as well as of the centrally planned economies, became **increasingly concentrated within their own group**.

    a. **Industrialised economies led the increase in the share of trade**, accompanied by a rising share of centrally planned economies, while underdeveloped countries saw, instead, a decrease in their share, except in Western Asia, which benefited from the petroleum industry.

4. Economic growth in some Third World countries was eventually limited because of issues such as high population growth rates and political instability.

5. In addition to the domestic issues that curtailed the ability of Third World countries to experience sustained economic growth, these countries tended to **benefit less from free trade than developed countries**.

    a. Free trade was seen mostly in manufactured goods among developed countries and only tariff (non-monetary) barriers were reduced.

    b. The 1950s also saw the formation of **trade blocs** whose members discriminated against non-bloc members in sectors such as agriculture.

        i. For example, the European Economic Community's (EEC)[2] Common Agricultural Policy (CAP) saw the government giving high subsidies to farmers to reduce their cost of production so that they compete more efficiently - and unfairly - with foreign imports.

6. The **non-industrial Third World countries** benefited far less from the positive effects of the growth of the global economy from 1945 to around 1971 than more industrialised economies.

    a. One sector that really exploded in growth during the period was **trade in industrial products, mainly between the industrial core companies**.

    b. World trade in manufactures multiplied over tenfold in the twenty years after 1953.

    c. The non-industrial Third World economies were <u>not</u> in a position to contribute or benefit significantly from the boom in trade within this sector.

[2] Formed in 1957.

7. It is also noteworthy that one of the most significant developments in world trade in the period from **1950 to 1960** was the **decline of exports from the underdeveloped (Third World) countries as a share of total world exports and as a share of intra-trade among undeveloped countries themselves**.
    a. In contrast, both developed countries and centrally planned (Socialist) economies increased their intra-trade area quite sharply.
    b. Exports from developing countries lagged behind those of advanced economies between the late 1950s and early 1960s, due to slower growth of export volume and the deterioration in the terms of trade.
8. Developed capitalist countries' dominance of the benefits of the "Golden Age of Capitalism" is evidenced by how, according to a 1979 Organisation for Economic Co-operation and Development (OECD) report, "the Golden Age essentially belonged to the developed capitalist countries, which throughout these decades, **represented 3/4 of the world's production and over 80% of its manufacturing exports. In the 1960s, capitalism was forging ahead rather than socialism.**"

### 3.2.2 Onset of Economic Decline and Issues from the 1960s Onwards[3]

1. Another fundamental issue arises when attempting to justify that the *entire* period from 1945 to around 1971 can be unequivocally understood as the "Golden Age of Capitalism".
2. The "Golden Age of Capitalism" (1945 to ~1971) depended on the continuation of a unique balance, that between the rate of growth of productivity and the rate of increase in wages.
3. A dip in the continuous rise in productivity and/or a disproportionate rise in wages would destroy this equilibrium. Wages had to rise fast enough to keep

[3] We will revisit content from this section at the start of the next topic of "Problems with Economic Liberalisation" to set the context for the "Crisis Decades" that followed the "Golden Age of Capitalism".

purchasing power buoyant, but not so fast that they squeezed profits and, therefore, investment.

<u>The Late 1960s: Decline in Productivity and the Onset of Inflationary Pressures</u>

1. By the late 1960s, it was evident that this unique balance could not continue. Labour productivity slowed in several countries. Why was this? Apart from the fact that labour productivity cannot rise indefinitely (the Law of Diminishing Marginal Returns), there was, understandably, a change in labourer's attitude towards work.

    a. In the years immediately after the war, many people could remember the Depression of the 1930s with its mass unemployment and insecurity - a painful antidote to complacency.

    b. In addition, there was the desperate need to rebuild war-shattered economies - one German engineer said, "When we came back from the Russian front, there was nothing to do but work."

2. By the late 1960s, this had changed and a new generation had become an adult, for whom the Depression and the economic desperation of the immediate post-war years were history and not part of personal experience.

    a. They had adjusted their expectations to the only experience of their age group, that of full employment and continuously rising prices.

3. Whatever the specific situation which triggered the worldwide wage explosion at the end of the 1960s - labour shortage, growing efforts by employers to hold down real wages or, as in France and Italy, the great student rebellions - there is no doubt that a major factor was the discovery by a generation of workers that the regular rises negotiated by their unions were, in fact, less than could be squeezed out of the system.

<u>The Late 1960s: U.S. Deficits and The Impending End of the Bretton Woods System</u>

1. To add to the growing problems, one of the backbones for the growth of the international economy came under tremendous pressure and eventually broke down. This was the BWS. It begs the question – If the BWS had been so good, why then did it break down in 1971?

2. The reason lay in the oversupply of US$ in the international financial system in the 1960s.

   a. This oversupply was due to previous US gifts and loans (such as the Marshall Plan and aid to Japan), to the system of US aid to developing countries (particularly in the 1960s with the US Peace Corps and the Alliance for Progress) and to the ongoing US expenditure on world-wide military commitments which involved the stationing of troops in many countries of the world – Great Britain, West Germany, France (until 1966), Belgium, Netherlands, Luxemburg, Norway, Denmark, Italy, South Korea, Japan, Philippines etc and etc – who were paid in US$. (Notice how the rest of the world benefited from this largesse in terms of economic prosperity and military security.) This whole picture was exacerbated in the late 1960s by the enormous spending on the Vietnam War - $2 billion per month.

3. By the 1960s, the amount of US$ holdings in the hands of foreigners exceeded the dollar value of the gold held by the US Treasury.

   a. The system could function only as long as the right to convert US$ into gold at $35 an ounce remained theoretical and was not exercised – at least, not on a large scale. If this right were to be exercised, the USA would not be able to meet its commitments – in other words, it would be bankrupt.

   b. It was then faced with three options: make an ounce of gold worth more than $35 (say $50) so, in effect, devaluing the US$ (but notice how foreigners who were holding US$ would object to this as their wealth would be reduced!); end dollar-gold convertibility; or move into surplus on its balance of payments by reducing its military commitments around the world (but then listen to the screaming of America's allies as their "security umbrella" was diminished!). It was a "no-win" situation.

c. In the end, President Nixon decided to devalue the US$ in August 1971 and ended dollar-gold convertibility.

d. The system of fixed exchange rates came to an end and this ushered in a period of exchange-rate volatility in the international financial system which, exacerbated by the "oil shock" of 1973-1974, had serious negative effects on international trade and prosperity.

# 4. Reasons for growth of the global economy

## 4.1 The Role of the USA in the Growth of the Global Economy

1. A key reason for the dramatic growth of the international economy is the role of the United States of America.
2. The fact that the "Golden Age" was the era of free trade, free capital movements and stable currencies can be attributed primarily to the economic dominance of the USA and of the US dollar, which functioned all the better as a stabiliser because it was linked to a specific quantity of gold, until the Bretton Woods System broke down in the late 1960s and early 1970s.
3. The economic supremacy of the USA *(Pax Americana)* can be illustrated by some figures: in 1950 the USA alone held 60% of all the capital stock of the advanced capitalist countries and produced over 60% of their output, and even at the peak of the "Golden Age", the corresponding figures were over 50% and just under 50% respectively.

### 4.1.1 The Cold War Providing the Impetus for U.S. Foreign Aid

1. The period after 1945 saw the outbreak of the Cold War which played a large part in shaping American policy. In the immediate aftermath of WWII, American policymakers already aimed at aggressive economic expansion in terms of exports. However, the fear of rising communism soon led them to take a longer-term view and to help their possible competitors to recover as rapidly as possible.

2. While it is probably an exaggeration to say that the Cold War was the major engine of the great global boom, the gigantic largesse of Marshall Aid/Marshall Plan US$13 billion certainly helped the recovery of Europe.

3. Similar US economic aid to Japan and Asia (totalling US$5.9 billion with Japan getting $2.4 billion) was evident – the USA built up Japan as the industrial base for the Korean War and, later, the Vietnam War. The USA funded the doubling of Japan's manufacturing output between 1949 and 1953, and it is no accident that 1966-70 were the peak years of Japanese growth – that staggering 14.6% per annum!

4. Thus, the role of the Cold War is not to be underestimated, even though the vast diversion of resources into military purposes was, in the long term, damaging. It can be argued in the shorter term, of course, that expenditure on guns and tanks and planes provided an expansionary stimulus to the civilian economy.

### 4.1.2 The USA Providing Its Allies with Access to the Open Market

1. Believing in “peace through prosperity”, American leaders sought to influence the countries of the world to adopt capitalism and participate in the market economy.

2. One aspect of the critical role the USA played in the recovery of the international economy and promotion of international trade and economic development would be its open market. To facilitate the recovery of its allies

from Europe and later Asia, the USA not only injected aid and expertise into their economies but also provided them with open access to the huge and relatively prosperous American market. Instead of Pax Britannica, it was now Pax Americana.

3. In the special case of Japan, it was almost like a "one-way street", where the USA provided the nuclear umbrella security and allowed Japanese manufactured products to gain access to the U.S. market freely, *while* accepting the protectionist closed-door policy of the recovering Japanese economy!

### 4.1.3 U.S. Leadership of the Bretton Woods System and Establishment of Key Financial Institutions

1. To ensure the free flow of trade and capital which were necessary for development, international cooperation was important. The USA thus took the lead to establish international economic institutions.

2. The Bretton Woods System was just what the world needed at the time and indeed much of the onset of the problems of the world economy in the 1970s can be traced back to the collapse of the Bretton Woods System in 1971.

3. The USA was also instrumental in setting up the international economic framework and supporting the creation of international institutions promoting trade and economic development, and arguably only the USA could have established/backed the creation of the Bretton Woods System which helped the world's trade and economic development tremendously in the period 1950-1971.

    a. **The World Bank** - mainly responsible for helping member states reconstruct after the war through the provision of low-interest long-term loans, focusing on developmental projects such as transport, housing and education. Such as structure was critical in generating growth in the developing world as it provided much-needed low-interest loans banks would otherwise not provide.

i. The Bank operated on a very limited scale during this period (1945 to ~1971), as it only had $570 million available for lending (contributed by the USA), which was insufficient to deal with the urgent need for reconstruction in Europe. As such, like the IMF, its role in facilitating economic reconstruction was dwarfed by the USA's Marshall Plan.

ii. The World Bank was **dwarfed by the Marshall Plan and private US investment.** It loaned out only US$500 million in its first four years. Moreover, while the international financial institutions did contribute to stabilising the global monetary order and increasing the overall trade volume, it must still be noted that they were created, dominated and sponsored by the USA.

iii. On their own (without the sponsorship of the US), these institutions would not have been able to contribute significantly to the growth of the global economy.

iv. As such, **the international financial institutions, in and of themselves, should not be considered a major factor contributing to the global economy**.

b. **The International Monetary Fund (IMF)** - responsible for providing short-term loans for members to tide over budgetary problems and also for maintaining stable exchange rates.

c. **General Agreement on Tariffs and Trade (GATT)** - a multilateral treaty organisation that promoted free trade, holding many rounds of discussions over the years to reduce trade barriers and promote free open trade, and notably in the 1970s, developing countries' products were given preferential access to markets of the developed world. GATT was later replaced by WTO in 1995.

i. GATT further encouraged economies to engage in free trade as a means of recovery through removal of tariffs on a wide range of goods.

ii. Through rounds of negotiations, GATT members had eliminated tariffs, quotas and other impediments to international commerce.

iii. Between 1947 and 1995, 8 rounds of trade negotiations under GATT set

iv. up a complex web of 60 agreements to govern world trade. $60bn worth of tariffs were removed.

v. While GATT saw a 73% reduction of all non-agricultural tariffs, most of this came from the USA. This made the US products cheaper to its allies, allowing them easier entry into the US markets.

4. The **system of fixed exchange rates** as adopted by the Bretton Woods System was instrumental in facilitating the growth of the global economy.

   a. The Bretton Woods System (BWS) was a system of **<u>fixed</u>** exchange rates. The external value of all currencies would be fixed in relation to the US$ (for example, the Pound Sterling was worth $4.03) and the value of the US$ was fixed in relation to gold at $35 an ounce.

   b. The US$ was convertible – this meant that, if you had $35, you could demand that the US Treasury give you one ounce of gold as promised.

   c. The great advantage of this system was its stability and predictability. You <u>knew</u> (within narrow limits) what the external value of any currency would be next week or even next year. This meant that exporters and importers could plan ahead with some degree of certainty and this, of course, facilitated international trade.

   d. A fixed rate places less premium on liquidity than a floating rate with its inherent pressure of unpredictability. Hence during the early years of recovery, much of the surplus capital, especially USA's, went into fixed capital formation and foreign direct investments. This encouraged capital formation and productivity growth in countries abroad, many of which could also plug into the benefits of more advanced American technological and managerial leadership.

e. Furthermore, the USA's expansionary economic policies would not only stimulate its own economy but through its imports also simulate production and income abroad.

f. Thus, there is **no doubt that there was a connection between the successful operation of the Bretton Woods system and the "long post-war boom" of 1945-1971**.

    i. In fact, when the Bretton Woods System came to an end in 1971, it ushered in a period of 'crises' in the international system.

## 4.2 The Role of Mixed Economies in the Growth of the Global Economy

1. Another major reason for the growth of the international economy in 1945-1971 would be due to the rise of mixed economies, largely underpinned by initiatives of governments to manage the economy, such as Japan, Singapore, France and Britain.

2. A mixed economy is one that comprises both private and government elements affecting the economy OR a mix of <u>both</u> capitalism and socialism.

    a. This model was found in a great variety of countries after 1945, albeit each practising the combination of capitalism and socialism to varying degrees, hence the difficulty in clearly defining mixed economies.

    b. The mixed economic model was appealing to the many new states with ***developing economies*** which had emerged during the process of decolonization across Asia and Africa after WWII. Ideally, a mixed economy provides them with a best of both worlds scenario – capitalist practices in the free market coupled with socialist government controls in certain sectors.

c. The model was also appealing to capitalist states with ***developed economies*** seeking to recover from the ravages of WWII and prevent a recurrence of the depression of the 1930s. Many adopted the Keynesian macroeconomic policies where governments had a crucial role in developing monetary and fiscal policies to stimulate growth. There would still be a large and important private sector but there would also be a significant public sector.

3. Helping the mixed economic models along was the amazing **political consensus** which prevailed in the capitalist states at the time. This political consensus was of the moderate Right and the moderate Left, with the extreme fascist / ultranationalist Right having been eliminated from the political scene by the Second World War, and the extreme communist Left by the Cold War.

    a. It was also based on an agreement (tacit or otherwise) between employers and labour unions to achieve growth by keeping labour demands within limits that did not eat into profits, and then making profits high enough to provide the investment without which the spectacular growth of labour productivity could not have taken place.

    b. It was a deal acceptable to all - Employers got predictability, which made forward planning easier. Workers got steadily rising wages and fringe benefits and a steadily widening Welfare State. Governments got political stability, weakening communist parties (Italy was an exception) and predictable conditions for the macroeconomic management which all states favoured.

## 4.3 The Role of Oil in the Growth of the Global Economy

1. Oil fuelled the growth of the global economy under the direction of the US-led capital-intensive and oil-dependent industrialisation, especially in the 1950s and 1960s.

2. In the 1950s, oil was the leading energy source. It was cheaper than coal, more convenient and of greater importance than other energy sources because of the rapidly expanding demand of goods that depended on it e.g., cars, airplanes, ships, plastics, synthetic rubber.

3. Oil prices were low in the immediate post-WWII period because of the abundance of oil, especially in the Middle East.[4] In the **1950s**, oil was **US$2 per barrel**.

4. Cheap and abundant oil lowered the costs of production and the prices of manufactured goods, amongst other benefits for the capitalist economies.

[4] Note that the Organization of the Petroleum Exporting Countries (OPEC) was formed in 1970 by Arab states, especially in the Middle East to strengthen the position of the governments of poorer oil suppliers vis-a-vis that of powerful multinational oil companies. OPEC would be partly responsible for the increase in oil prices that played a part in the 1973 Oil Crisis.

**IMPORTANT! Read this before moving on to the remaining sections of the notes!**

- The following sections will examine **post-war economic liberalisation** in Western Europe and Japan, as well as the role that **multinational corporations (MNCs) / transnational corporations (TNCs)** played in the growth of the global economy. It is imperative that we understand the remaining sections **within the larger context of attempting to analyse what contributed to the growth of the global economy and more specifically, the "Golden Age of Capitalism"**.
- Consider these questions thoughtfully when reading the remaining sections:
    - What role did the different actors (the USA, Western Europe, Japan) play in the post-war economic liberalisation of the region / country in question?
        - A related question: What role did domestic and external factors play in the post-war economic liberalisation of the respective countries being examined?
    - How did post-war economic liberalisation in the region / country in question contribute to the "Golden Age of Capitalism"?
    - To what extent was the USA primarily responsible for the post-war economic liberalisation in Western Europe and Japan?
    - Did domestic or external factors play a greater role in the post-war economic liberalisation of Western European countries and Japan?
    - What role did MNCs / TNCs play in post-war economic liberalisation?
    - Who and/or what contributed to the rise of MNCs / TNCs?
        - A related question: To what extent was the USA primarily responsible for the rise of MNCs / TNCs?

# 5. Post-War Economic Liberalisation: Economic Miracle in Western Europe

## 5.1 Role of the USA in Western Europe's Economic Miracle

1. Beyond the leadership role played by the USA in the creation of international institutions and systems, the American government had also undertaken unilateral action in the initial years to spur global economic recovery.
2. The Marshall Plan saw the United States giving $17 billion to European nations affected by World War II, with a large chunk of this money going to Germany.
3. However, the success of the Marshall Plan has been debated by economic historians.
    a. Some have estimated that aid from the Marshall Plan contributed less than 5% to Germany's national income during this time period.
    b. Other countries that received substantial Marshall Plan aid exhibited lower growth than Germany. Moreover, while West Germany was receiving aid, it was also making reparations and restitution payments well in excess of $1 billion.
4. Though the USA had a heavy hand to play in the immediate postwar years, **it was Western Europe and Japan, aided with initial support from the USA, that sustained what America started** by supporting its open door policy and trading extensively with the rest of the world, as well as investing heavily in other economies.

## 5.2 Role of Western Europe in the Region's Economic Miracle

1. While U.S. aid facilitated the quick recovery of Western European economies, domestic factors within Western European countries (e.g., the role of the state / government, high rates of literacy, industrial and social discipline) also played an important role.

a. If U.S. aid sparked the recovery of Western Europe's economies, these European nations sustained it with high levels of savings and investment.

   i. In the long term, Europe's wealth of human capital, high rates of literacy, and specialised institutions plausibly provided the skilled personnel and brain power needed to make the new technology work effectively.

2. Western Europe contributed to the **global economic growth** after recovering from the devastation of WWII by:

   **a. Sustaining the growth of their economies** after the U.S. kick-started it with aid;

   **b. Trading extensively with the U.S. and among Western European countries**, thereby increasing the foreign demands for their goods (exports);

   **c. Contributing extensively to the IMF and the World Bank**, thus making funds available to needy countries; and

   **d. Supporting the U.S. open door economic policy**, a critical step towards facilitating the liberalisation of global trade.

3. Governments in Western Europe were primarily moderate and anti-Russian conservatives who **worked towards common goals to achieve rapid economic growth**.

   a. The relatively high degree of inter-government cooperation among Western Europe countries contributed to the effectiveness of their economic performance.

      i. This reflects the **initiative and agency** of Western European countries, and helps to balance the notion that the U.S. was the main architect of the rise of the global economy.

b. An example of the role of Western European governments in promoting economic growth was seen in West Germany.

i. Erhard (German Chancellor) played a part in formulating a new currency (deutsche marks (DM)) issued by the Allies to replace the worthless remnant of the past.

ii. This plan would reduce the amount of currency available to the public by a staggering 93%, a decision that would reduce the little wealth that German individuals and companies held.

iii. In addition, large tax cuts were also instituted in an attempt to spur spending and investment. The corporate income tax rate, which had ranged from 35 percent to 65 percent, was made a flat 50 percent. For the median-income German in 1950, with an annual income of a little less than DM2,400, the marginal tax rate was 18 percent. That same person, had he earned the reichsmark equivalent in 1948, would have been in an 85 percent tax bracket.

iv. **Effects of reform**: In May of 1948, Germans missed approximately 9.5 hours of work a week versus post-reform, where price controls were lifted, and **hours missed went down to 4.2 hours per week**. **By 1958, German industrial production was also four times that of 1948**.

4. The role of the **European Payments Union (EPU)**, formed in **September 1950**, allowed free multilateral trade within the Organisation for European Economic Co-operation (**OEEC**).

   a. In the two decades or so after the formation of the EPU, trade grew at **an average of 8%**, the **highest in history since the 1860s**.

   b. The EPU was so successful that the free controverbility of currencies[5] was restored and full multilateral trade was seen by around 1958.

5. Western Europe committed itself to proliferating trade activity, crucially encouraging trade amongst themselves with the 1950 European Coal and Steel Community (ECSC) and the 1957 European Economic Community, which facilitated labour flows, technological transfer amongst each other and regional economic integration.
   a. The ECSC was to make possible real competition throughout a vast market, from which producers, workers and consumers would all gain.
   b. Between 1958 and 1960 alone, trade between the six member countries grew by 50 percent.
6. The 1960s was a decade of extraordinarily high and sustained rates of economic growth in Germany and throughout Western Europe.
   a. Burgeoning intra-European trade and strengthening trade links with the world would see Europe accounting for 40% of total world trade by 1970, up from just 25% in 1949.
7. Western Europe support from trade liberalisation boosted its economy, in turn benefitting global economic growth through increased economic activity.

[5] Currency convertibility is the ease with which a country's currency can be converted into gold or another currency.

# 6. Post-War Economic Liberalisation: Economic Miracle in Japan

## 6.1 Role of the USA in Japan's Economic Miracle

1. The USA gave Japan $12 billion from 1945 to 1952 in the form of direct transfers and other forms of aid e.g., equipment, technology, loans and machinery.

2. The USA pegged the yen at the competitive exchange rate of 360 (yen) to $1 in 1949.

3. The Security Treaty of 1951 laid the foundations for liberating Japan from the burden of paying for its own defence, and thus Japan was able to concentrate on generating economic growth under an American security umbrella.

    a. Japan's economic revival was being sponsored by the USA in order to assist with the stabilisation of Asia and to forestall the growth of communism Japan while strategically and politically being locked into the Western alliance system as a distinctly unequal partner.

4. The USA pumped in $2.2 billion of humanitarian and development aid over the course of 7 years and contributed tens of billions of dollars through procurement policies of its military forces based in Japan and the region.

5. The USA eased Japan's path into the world economy by sponsoring its entry into the General Agreement on Tariffs and Trade (GATT) organization in 1955.

    a. Noting also that Japan was denied access to the China market and that Southeast Asia was not sufficient to soak up Japan's exports, the Eisenhower administration in 1955 allowed Japanese goods such as textiles, access to the American domestic market.

6. With the lowering of trade barriers and entry of Japanese automobiles into the American domestic market, the USA suffered its first trade deficit with Japan in 1965.

7. In 1965, the USA brokered the opening of diplomatic relations between Japan and South Korea which beforehand had proved impossible due to the lingering animosity between the two countries. This move, which was part to strengthen the Korean economy and reducing the reliance on the USA, opened a new market for Japanese goods and investment.

8. The USA also granted Japan the 'most favoured nation status' which granted her all trade advantages, such as low tariffs. In essence it was to promote free trade.

    a. It allowed Japanese goods to flood the American markets which boosted Japanese economy tremendously.

    b. In fact, Toyota was saved from imminent bankruptcy by American procurements.

## 6.2 Role of Japan in Its Economic Miracle

1. Over in Asia, sound governance, industrial strategies and an export-oriented industrialisation growth plan under the Ministry of Trade and Industry (MITI) of Japan allowed it to build strong economic fundamentals, crucially contributing 15% of the global GDP by the 1970s, up from a mere 3% in 1950.

    a. This enabled it to play the role of a major export market and source of funds in Asia.

2. In 1958 it extended a $15 million loan to India for its development, providing the same support for Singapore and Malaysia in 1966 with $17 million and $30 million loans respectively Japan also invested heavily in countries like Indonesia and Thailand, and acted as the largest export market for these countries.

   a. It was these efforts that characterised the "flying geese" phenomenon[6] in Asia.

### 6.2.1 The "Income Doubling" Plan

1. Ikeda's, Prime Minister of Japan from 1960 to 1964, "income doubling" plan was introduced in 1960.

2. It was a vital turning point in Japan's history by downplaying defence and instead emphasising economic growth, which led to the marked expansion of the Japanese economy.

3. The decade after the introduction of the "income doubling" plan in Japan was one of phenomenal growth, and it is plausible that the plan contributed to this.

   a. While Japan's annual growth rate averaged from 1955 to 1960 was 10%, the subsequent years saw this figure increase to 13%.

### 6.2.2 Direct Role of the Government in Economic Growth and Development

1. The Japan government, particularly the Ministry of Trade and Industry (MITI), charted a course for the economy and coordinated its industrial growth.

   a. Government and industrial firms engaged in long term planning and both made use of consensus decision-making.

   b. The MITI bureaucracy, with its ties to political and business leaders, also steered a steady course, thereby providing policy continuity.

2. The government guided industrial development not only by targeting specific industries for growth but also by designating declining industries to be scaled

[6] The paradigm postulated that **Asian** nations will catch up with the West as a part of a regional hierarchy where the production of commoditised goods would continuously move from the more advanced countries to the less advanced ones.

down or dismantled. It also targeted foreign markets on which the Japanese would concentrate their attack.

3. In sum, the Japanese government fostered a national consensus on the priority of economic growth and established industrial and trade policies.

    a. The Ministry of Finance (MOF) and Ministry of Trade and Industry (MITI) shared the creation and implementation of policies designed to systematically target and develop strategic industries and technologies within the context of a five-year plan.

    b. Industrialisation promoted a surge in its heavy industries and a substantial rise in steel production - by 1970 steel and iron were Japan's largest exports, with it accounting 14.7% of total exports

    c. Ikeda's focus on export-oriented industrialisation led the economy to grow at an average rate of 10.4% per annum in the 1960s, with 96% of its exports being manufactured goods.

    d. The government also worked to diffuse good practices such as quality control, a lifetime employment system, and encouraged companies to disseminate technology and patents.

    e. It also worked closely with the Ministry of Finance and the Bank of Japan to ensure that the public and private capitals were made widely available to the key industrial sectors.

4. In the case of Japan, it can be seen that the state played a direct role in planning the development of a capitalist economy.

        i. The protection of automobile and electronics industries through tariffs allowed it to develop tremendously.

    b. Foreign automobiles were restricted to an insignificant share of the market in the 1950s, and never exceeded 1% of the domestic market from 1945 - 1985.

   c. From 1950-1980, Japan spent $10 billion on licensing 30, 000 foreign technologies, and used it to modernise factories, manufacture cheap products and mass dumped them to capture market share and drive out rivals.

   d. By the late 1980s Japan had twice as many industrial robots in operation than the rest of the world combined.

5. Originally set at 360 yen to a dollar in 1949, the yen became increasingly undervalued as Japan's economy expanded over the next 22 years.

   a. The yen remained undervalued even after Nixon forced the yen's revaluation to 308 to a dollar in 1971.

### 6.2.3 Socio-Economic Reasons

1. Tokyo encouraged high savings by limiting government benefits as welfare, education and social security and keeping consumer prices high and credit limited.

2. Consumers thus had to save a huge percentage of their income. Tokyo then channeled these vast savings into cheap loans for strategic industries.

3. Japanese workers saved a remarkable 18% of their salaries.

   a. The banks then invested the surplus capital in industry and commerce.

   b. The Japanese were served well by historically conditioned cultural traits, such as acceptance of authority, paternalism, a desire for harmony, loyalty to superiors, discipline and a sense of duty and sincerity. Group consciousness prevailed over individualism.

   c. Without these traits, Japan's labour management system would hardly have been possible e.g., mutual harmony between the workers and management rather than confrontation.

      i. Japan's dearth of raw materials, for example, necessitated hard work to attain, conserve, and use them efficiently.

4. In 1986 the average employee in manufacturing and production industries worked 2,150 hours in Japan.

5. The average Japanese worker is entitled to fifteen days of paid vacation a year but actually took only seven days.

6. The conscientious working culture coupled with high savings and an attractive employment system all combined to contribute to Japan's economic

### 6.2.4 Concluding Thoughts

1. Japan and West Germany crucially perpetuated the ripple effects of initial American aid, supporting liberal economic institutions and practices, while spurring the economic growth of other countries once they had secured their own.

2. Nevertheless, it was **plausibly the efforts of the USA which ultimately enabled Japan to** recover from the ravages of war and **contribute meaningfully to the growth of the global economy**.

# 7. Post-War Economic Liberalisation: The Rise of Multinational Corporations (MNCs) / Transnational Corporations (TNCs)

1. Multinational (or transnational) corporations are companies with a management headquarters in one country (home country) and operations in many countries (host countries). As such, MNCs tend towards an expansionary growth pattern.

2. These "multinationals" were not a new phenomenon in the post-WWII period, but what was new was the sheer scale and diversity of their expansion.

a. For instance, American corporations of this kind raised the number of their foreign affiliates from about 7500 in 1950 to over 23,000 in 1966, e.g. General Motors, Ford, Hertz, MacDonald's, Coca-Cola, Xerox.

b. By 1980, they accounted for over three quarters of the USA's exports and almost half its imports.

c. However, it should be noted that these MNCs were found mostly in Western Europe and the western hemisphere.

## 7.1 Reasons for the rise of MNCs

### 7.1.1 Lower costs of production abroad

1. Companies place factories to produce components or undertake certain stages of the manufacturing process abroad because of the cheap labour, cheaper raw materials or lower costs of energy.
2. There may also be laxer legal restraints on the treatment of their labour or on environmental pollution abroad.
3. Sometimes, companies establish their mines or plantations or production facilities abroad simply because the natural resource bases are found there, e.g. fruits in Latin America, oil in the Middle East, cotton in Asia.

### 7.1.2 Larger Markets

1. Companies may also go abroad in search of additional markets.
2. One aspect of this was the attempt to bypass tariff barriers or other methods of restricting imports – for example, the founding of numerous motor car factories by Japanese companies within Europe was in part a response to the attempts by European governments to limit the direct import of Japanese cars so Japanese car firms built factories in Europe.
3. Frequently, the expansion of one firm into branches abroad provides a spur to its competitors to do likewise, in order not to lose ground in the race for market shares and scale economies.

## 7.2 Benefits of MNCs / TNCs

### 7.2.1 Technological Modernisation

1. **Technological modernisation** is an important contributing factor to economic recovery and subsequent growth.
    a. MNCs are often highly efficient and among the technological leaders and innovators. They are responsible for much of the increase in output and productivity in the global economy.
    b. They have also helped to introduce up-to-date, frequently American practices, know-how and capital into other industrialised countries.
    c. This has helped the 'convergence' of European economies and their catching up with the USA.

### 7.1.2 A New International Division of Labour

1. A **new international division of labour** resulted from this growth of multinationals. The German car firm Volkswagen, for example, set up car factories in Argentina, Brazil, Canada, Ecuador, Egypt, Mexico, Nigeria, Peru, South Africa and Yugoslavia.
2. New Third-World industries supplied not only the swelling local markets but, increasingly, the world market. They did this, not only by exporting local articles produced totally by local industry (such as textiles, most of which had "emigrated" from the old countries to the "developing" countries by the 1970s) but also by becoming part of the transnational process of manufacture.
3. This was technically feasible because of the revolution in transport and communication, which made it possible and financially viable to split the production of a single article between, say, Houston, Singapore and Bangkok, airfreighting the partly completed product between these centres and controlling the whole process centrally by modern information technology.

## 7.1.2 Foreign Direct Investments (FDI)

1. **Most significantly,** MNCs brought with them capital investments or **foreign direct investments (FDI)** that helped economies to grow.

    a. Foreign Direct Investment refers to investment by citizens/companies of one country in companies located elsewhere in such a manner that they control/manage them.

    b. The essence of FDI is that foreigners control the operations of the firms. However, FDI can be wholly owned or partially owned (also known as a joint venture).

    c. By 1973, MNCs had invested $200 billion around the world, but in this early phase, three-quarters of it were in advanced industrial countries, where conditions were more familiar.

    d. Half of this FDI came from the US, although European and Japanese corporations soon caught up. Besides American MNCs, other European and Japanese MNCs also emerged.

        i. Examples - German chemical giant Hoechst, for example, established or associated itself with 117 plants in 45 countries, other big MNCs include Allianz, Volkswagen, Daimler Benz. Among the first big Japanese MNCs were Toyota, Nissan, Toshiba, Fujifilm, Sony.

    e. FDI became the leading edge of international economic integration - By 1975, it was estimated that only 25% of FDI was made in the developing countries of the third world. However, FDI was nonetheless significant for such countries with MNCs from the USA, UK, Germany and Japan accounting for 3/4 of FDI in these countries. By 1989, the 100 largest global companies were employing 12 million people outside the borders of their home country.

f. Total FDI in 1970 was about US$20 billion and this increased to $50 billion in 1985 and $200 billion in 1990. However, in 1991, FDI began to decline as the Western industrialized countries slid into recession and the Japanese economy weakened.

***<u>The debate about FDIs – benefits and drawbacks</u>***

1. It should be noted that though MNCs are based largely in the developed economies, they not only benefitted the home country. Business logic would force an international oil firm, for example, to calculate its policy and strategy towards its home country in exactly the same way as towards Saudi Arabia or Venezuela - i.e. in terms of profit and loss.

2. So the mainstream view of foreign investment is that it is conducive to economic growth and development because of the advantages it provides. By bringing capital and new technology to a less developed country, foreign investment increases productivity, incomes and output. As long as this increase is not completely appropriated by the foreign investor, the developing country's economy will benefit.

3. There are direct and indirect benefits. Direct benefits include lower prices, better quality products etc. Indirect benefits include access to foreign expertise in production technology, management, administration and marketing and these, in turn, exert competitive pressure on local firms.

4. Foreign investment is also beneficial to less developed countries because of the creation of pecuniary economies or spillover effects. It can reduce costs, or create demand in other industries. For example, the production of computer chips in Singapore by Texas Instruments reduces the input costs of local computer manufacturers. Foreign-owned firms also stimulate the expansion of local industries which supply inputs, i.e. there is an increased demand for packaging materials which are supplied by Texas Instruments by other firms in Singapore because most of the output is shipped to its subsidiaries overseas.

5. In order to attract FDI, less developed countries may have to offer generous

financial incentives (i.e. tax holidays, exemption from import duties for inputs etc.).

6. However, the evaluation of the role of FDI in developing countries is a contentious issue. While mainstream economists argue that foreign investment is conducive to economic growth and development, radical economists view it as a means by which less developed countries are exploited and kept in a state of underdevelopment.

7. The empirical evidence of various aspects of foreign investment in less developed countries is ambiguous and there is no conclusion as to the evaluation of FDI. But there is little doubt that countries which opened their doors to foreign investment grew fastest.

**Case Study – FDI-driven industrial development in developing countries and the Growth of the Asian NIEs**

1. The rapid economic transformation of many developing countries in the world—particularly in Asia—after World War II is one of the most significant developments in the global economy.

2. From widespread poverty and bleak prospects for economic advancement, many of these countries developed into economic powerhouses. Japan is the Asian leader and best example of rapid economic growth.

    a. By the 1970s, it had emerged as a major industrial power and a world centre of manufacturing and exports. Another good example would be the Asian NIEs.

<u>The Growth of Asian NIEs</u>

1. The NIEs refer to a group of countries whose economies, in terms of world economic development, are in a transitional stage between the less

developed countries (LDCs) of the Third World and the advanced industrial countries (AICs) of the West.

2. The NIEs of Asia refer to as the four tigers of Asia.

3. After WWII, the Asian NIEs were amongst the poorest, less developed countries then. They were bereft of much of their social infrastructure, large parts of industry, transport and communications facilities.

4. During the 1950s, all the Asian NIEs were rebuilding their economies after the devastation of WWII. The era of rapid economic growth in the Asian NIEs began in the early 1960s for South Korea, Taiwan and Hong Kong and in 1965 for Singapore, where all recorded some of the highest growth rates in the world during 1965-1989.

5. The Newly Industrializing Economies (NIEs) of Asia (Hong Kong, Singapore, South Korea and Taiwan) became the fastest growing economies in the world and major participants in world trade, transforming themselves from less developed to developed countries within the relatively short space of 20 to 30 years.

6. The NIEs are often regarded as the only countries in the world, since Japan, to have progressed successfully from the status of less developed countries to developed country status.

Role of Foreign Capital in NIEs

1. From 1970 to 1980, Singapore and Hong Kong were amongst the ten largest recipients of foreign investment amongst all developing countries.

2. In the period 1980 - 1990, Singapore was the largest recipient of foreign investment amongst all developing countries.

    a. In Singapore, the dependence of foreign investment was very high (about 70% of manufactured exports were from foreign-owned firms).

3. Foreign investment brought not only capital, new technology, management skills, training of labour, but also export markets.

4. Foreign-owned firms usually have established markets in developed countries either for final products with established brand names or for intermediate goods.

    a. E.g., Apple Computer Company manufactures Apple computers in Singapore and sells them throughout the world. Texas Instruments produces computer chips in Singapore and ships them to its subsidiaries and to other firms throughout the world.

<u>Role of the Asian NIEs in International Trade</u>

1. Asian NIEs are some of the most outward-looking countries in the world and their export-oriented industrialization since the 1960s has given them an important place in the international trading system.

    a. For example, Hong Kong's total trade ratio (exports plus imports) as a percentage of GDP in 1985 was 205%, Singapore's trade ration was 270%, South Korea's trade ratio was 72%, while Taiwan's trade ratio was 99%. This contrasts with Japan's trade ratio of 29% and USA's 17%.

    b. In 1965, the Asian NIEs share of world trade was 1.5% and grew steadily to reach 9.2% in 1997.

    c. Hong Kong alone accounted for 3.2% of world trade in 1997, while the other Asian NIEs each accounted for about 2% of world trade and this is a remarkable achievement by any standards. India, a much larger country, accounted for only 0.3% of world trade in 1997.

2. In terms of total volume of trade in 1997 the Asian NIEs ranked as follows:

    a. Hong Kong—9$^{th}$ in the world

b. **South Korea—13$^{th}$ in the world in terms of largest exporter**

c. Singapore—14$^{th}$ in the world

d. **Taiwan—15$^{th}$ in the world**

*Note that in comparison: China was ranked around 6$^{th}$ at this time.*

3. The importance of the Asian NIEs in world trade is also reflected in the value of exports per head of population.

# 8. Preliminary Analysis on the Causal Relationships That Underpinned the Growth of the Global Economy

1. The analysis in this section is neither exhaustive nor comprehensive. Rather, we will need to use these ideas as a starting point for developing our own evidence-based and sophisticated analysis that properly addresses the complex reasons why the global economy grew in the way that it did from 1945 to around 1971.

2. It is critical that we pay attention to how the learning outcomes in the syllabus requires us to analyse the **causal relationships that underpinned the growth of the global economy**.

    a. This necessitates that we move beyond the listing of factors e.g., 'It was X that contributed by… Next, Y also contributed… Also, Z contributed by… In conclusion, X, Y, and Z contributed to the growth of the global economy.'

    b. A good History student would **analyse the causal relationships between X, Y and Z** to explain the growth of the global economy e.g., 'X contributed by… However, Y was more influential than X because it provided the necessary conditions for X to happen… Ultimately, it was Z that was plausibly most influential because it was needed for Y to have a long-term impact and it also sustained the growth of the global economy over the long run because…'

## 8.1 Analysing the Role of Bretton Woods Institutions

1. The Bretton Woods system aided the recovery of most countries, particularly those that were well placed to participate in the international trade of **manufactured goods** e.g., West Germany and Japan.

2. However, the Bretton Woods system's impact was largely confined to the advanced capitalist economies within the First World and lacked a larger impact

that extended to the Second (Socialist bloc) or to the Third World whose economies focused on the export of agricultural goods, raw materials, minerals and commodities - goods where prices continued to fluctuate according to demand and supply, as opposed to experiencing a generally upward trend.

3. Cooperation and trade liberalisation facilitated by the IMF, World Bank and GATT created opportunities for growth but these institutions' ability to do so depended on other factors.

    a. For example, it was the abundance of labour and latent demand in Germany, and the willingness and ability of the Japanese workforce to participate in the advancement of the country's economic goals, which accelerated the economic growth of these countries.

    b. It is thus plausible that while the Bretton Woods institutions support economic liberalisation to the extent that it made economic growth possible, **it was at least as important that conditions in countries, such as West Germany and Japan**, were conducive for making such growth possible. The **role and agency of these countries** were minimally as important an explanatory factor as the Bretton Woods institutions when one attempts to analyse the growth of the global economy from 1945 to around 1971.

        i. To argue that Bretton Woods institutions > the role of countries such as West Germany and Japan, one could point to how these institutions **provided the key structures** that these countries could leverage upon to contribute meaningfully to domestic and international economic growth.

        ii. To argue that the role of countries such as West Germany and Japan > the Bretton Woods institutions, one could argue that while the Bretton Woods institutions were plausibly more important for explaining the **post-war recovery of these economies**, it was ultimately the countries and their governments that had to **sustain the growth** in the **long term**.

4. The Bretton Woods system was **highly dependent on the willingness and ability of the USA** to contribute meaningfully to the growth of the global economy.

   a. For example, the breakdown of the Bretton Woods institutions had its roots in the USA's decision to end the convertibility of the US dollar to gold in August 1971 - something that had helped provide stability and fuel growth for the global economy up to that point.

   b. In view of this, one could argue that the role of the USA > the role of the Bretton Woods institutions in contributing to the growth of the global economy.

5. Perhaps one of the most important things to remember is this: **institutions / systems in and of themselves cannot generate significant impact**; their impact depends greatly on the actors (e.g., the USA, Western Europe, Japan, etc) and the conditions at the time (e.g., the Cold War providing the impetus for the USA to promote economic liberalisation through the Bretton Woods system).

## 8.2 Analysing the Role of the Cold War

1. The Cold War's impact on the global economy was plausibly most significant in the **immediate post-war years**.

2. The Cold War provided the **impetus for a key actor, the USA, to fuel the recovery and growth of capitalist economies** and it was the economic performance of these economies that, in turn, supported the growth of the global economy.

   a. The Cold War helps to contextualise the desire for the USA to build a network of capitalist economies that were friendly to its ideology and safeguard countries against the ills of communism. This contributed to U.S. attempts to aid economic reconstruction through Marshall Aid, and increase trade and cooperation among countries through the Bretton Woods system.

   b. Marshall Aid plausibly helped to kickstart the post-war economic reconstruction of West Germany and Japan, two countries that were key actors in the "Golden Age of Capitalism".

3. It is then perhaps of little coincidence that the advent of the "Golden Age of Capitalism" coincided with the USA's actions in the post-war period that sought to promote "peace through prosperity".

4. However, the Cold War also motivated the USA to spend substantially in order to support capitalist and democratic ideals. In the **long run**, this drained the U.S. economy and motivated the USA to pursue policies that undermined the growth of the global economy.

   a. The USA spent about US$320 billion to fund its involvement in Korea and US$686 billion in Vietnam. Also, it spent approximately US$13.1 trillion on its nuclear programme.

   b. The large amount of spending would eventually curtail the USA's ability and willingness to contribute positively to the growth of the global economy, resulting in U.S. policies that instead sought to protect U.S. hegemony and interests.

5. The Cold War had an adverse economic impact on some parts of the world such as Indochina, especially Vietnam, that was deeply affected by the war that raged there. Also, the Cold War plausibly contributed to **inflation in the 1960s**, by driving up the prices of rubber, tin, and copper.

6. While many countries may have benefited from the Cold War e.g., Japan and its economic growth accelerating in part due to the Korean War, it could also be argued that many countries were **cordoned into different Cold War spheres during the period, limiting the extent of economic liberalisation and cooperation internationally**, and many countries

received **unproductive military aid, rather than aid for reconstruction and economy recovery**.

## 8.3 Analysing the Role of Oil / Cheap Energy Sources

1. The availability of oil at low prices plausibly contributed to and sustained post-war economic growth.

2. However, cheap oil is perhaps better understood as an **immediate rather than root cause of post-war economic growth**. In other words, it enabled the growth of the economies but it was not the fundamental reason why these economies grew at the rate they did during the post-war period.

3. Even with the availability of cheap oil, the key actors had to decide how to use it and one could argue that it was **the decision of capitalist economies, led by the USA, whose focus on manufactured goods** saw them taking advantage of the oil prices to spur economic growth and sustain economic development.

## 8.4 Analysing the Role of Multinational / Transnational Corporations

1. MNCs / TNCs played a key role in supporting the growth during the "Golden Age of Capitalism" by allowing capitalist economies to capitalise on their respective comparative advantages, leading to an increase in trade.

    a. At the same time, host countries with such comparative advantages benefited from increased investments, the spread of technology, the creation of jobs and increased productivity.

2. However, in the early growth years, there were **not that many MNCs** and the **ones that did exist at that time were mostly American**; this meant that it was U.S. interests and economic growth that benefited more than the international economy.

3. In addition, MNCs / TNCs also engaged in practices that impeded the growth of economies such as refusing to transfer technology and its benefits to the host countries that they had set up in, and having a limited impact on creating jobs in the host country especially because MNCs / TNCs were highly mobile and could move out of countries before longer term benefits set in.

## 8.5 Analysing the Role of the USA (versus that of Western Europe and Japan)

1. An absolutely critical point to make about the role of the role of the USA is that it is **imperative to avoid establishing a monocausal link between the role of the USA and the growth of the global economy** e.g.., it was the USA and its policies *alone* that fuelled the "Golden Age of Capitalism".

2. There is good reason to highlight that the USA played an essential role in starting and sustaining the phenomenal growth of the post-war years that came to be labelled as the "Golden Age of Capitalism".

    a. Policies such as Marshall Aid, and U.S. leadership of the Bretton Woods system contributed to the reconstruction of economies such as those of West Germany and Japan, while also benefiting other capitalist countries who contributed to the growth of the global economy.

3. An important counterbalance to the notion that the USA was *the* most important actor is that the other key actors also needed to play their part in ensuring that the aid provided to their countries and the benefits accrued from the increased trade among nations helped to fuel economic growth domestically and internationally.

    a. Sections **5.2** and **6.2** of the notes highlighted the respective roles of Western European countries and Japan in the growth of the region / country. The information there would help to provide evidence that prevents us from crowning the USA as the sole and undisputed actor who single handedly fuelled the growth of the global economy from 1945 to around 1971.