

THE SHORT AMERICAN CENTURY

A Postmortem



Edited by

ANDREW J. BACEVICH

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From the American Century to Globalization

Jeffry A. Frieden



Today's troubled economic conditions have led many to engage in nostalgic reminiscence about the decades after World War II, when the international economy seemed stable and predictable. The dollar was the world's key currency; trade and investment grew continually, and currency values were practically unchanging. But the international economic order that prevailed from the late 1940s to the mid-1970s was a very unusual creation, never before seen and very unlikely to be reproduced. Neither the United States nor the world is going back to the economic circumstances of that earlier era.

This essay describes the distinguishing features of the international economy during the Short American Century—and, in particular, during the thirty years after World War II. It then explains why the world economy took the form it did in this period, why it evolved as it did, and where we are headed now that the American Century has ended and a new one has begun.¹

Collapse of the Classical World Economy

The policy makers who constructed the American-led international economic order in the aftermath of World War II worked with the experiences of the decades before 1945 firmly in mind. Even before the war ended, American leaders, and others in the advanced indus-

trial world, had clear ideas about what they wanted to avoid and what they wanted to encourage, as they planned the postwar economic order. Their ideas came from the impressive successes and devastating failures of the international economy's previous hundred years.

One global experience that had a powerful impact on postwar planning was that of the integrated international economy that prevailed in the fifty years before 1914. In that first era of globalization, the movement of goods, capital, people, technologies, and information was freer than it had ever been. Indeed, on a couple of dimensions, the world economy was even more tightly tied together than it has been in our more recent age of globalization. The movement of people—especially of Europeans—was almost completely untrammelled. Some 50 million Europeans left the continent for other lands, largely in the New World, and in most cases they could immigrate almost without documents. Another 50 million Asians also migrated across borders, although their entry to countries like the United States and Australia was more restricted. Nonetheless, immigration was freer than it had been ever before, and freer than it has been ever since.

On a second important dimension, the world was more tightly integrated before 1914 than it is today: almost the entire world shared a common money—gold. At the height of the classical era, every economy of any significance (except China and Persia) was on the gold standard. This was, in some ways, tantamount to having a common currency: while there were separate national monies, they were all easily convertible into gold at a fixed rate. The gold standard made currency values extraordinarily stable and predictable—exchange rates for the major currencies did not change for over forty years, and the gold value of the pound sterling was constant in peacetime for two hundred years. This greatly facilitated trade, investment, finance, travel, and migration across borders, much as the euro has facilitated the greater integration of the economies of present-day Europe.

The world economy of the late nineteenth and early twentieth centuries was not only tightly integrated but also highly successful. The international economy grew more rapidly than it had at any previous time in recorded history—more in seventy-five years than in the previous 750. Many middle-income countries caught up with rich

countries; many poor countries caught up with middle-income countries. Although periodic panics and crises occurred, overall macro-economic conditions were quite stable, and world prices changed only gradually, and only very little. To be sure, this was an era of colonial imperialism, of periodic wars and arms races, and of much poverty and brutality. But compared to the economic conditions that came before, this was an extraordinarily successful economic order.

Yet the classical international economic order that had been so successful for generations collapsed in a matter of weeks in 1914. The onset of World War I disrupted international economic relations, which was no surprise. After the war ended, economic and political elites around the world set about trying to revive the prewar economic order—with no success. It turned out that the wartime collapse was no temporary aberration.

For two decades after the end of World War I, the world's political and economic leaders attempted to restore the integrated world economy that had characterized the classical age before 1914—and failed. Despite a bewildering array of conferences, negotiations, treaties, and international organizations, it seemed impossible to rebuild a globalized economy that most governments professed to want to see rebuilt. Not only that, but country after country turned away from the world economy, toward fascism, economic nationalism, and a myriad of anti-internationalist economic philosophies—many of which seemed linked to belligerent and expansionist militarism. The diplomatic lineup that emerged after 1939, in which liberal democracies confronted nationalistic dictatorships, seemed to spell the end of an era in which a consensus in favor of economic integration could be assumed.

As American policy makers began planning for the post-World War II world, they drew some important lessons from the international economic experience of the previous century. The first lesson was that the pre-1914 era had many features worth emulating. It was as close as the modern world had known to an age of generalized prosperity and peace; and whatever the classical system's flaws, it was better than the apparent alternatives. Yet these policy makers recognized that the world could not simply return to the precepts of an earlier era: as Dean Acheson said in 1939, "The economic and political system of the

Nineteenth Century has been for many years in the obvious process of decline. The system is deeply impaired."⁷²

The second lesson was that a more open international economy required purposive cooperation among its major participants. A commonly held view during the nineteenth century had been that the classical international economic order was self-regulating and self-equilibrating. But while individual markets might tend toward equilibrium, it seemed clear in retrospect that keeping the world economy open had required substantial, concerted efforts on the part of major governments. This was especially true in times of crisis—and there were periodic "panics" all through the nineteenth and early twentieth centuries. When they hit, the monetary and financial authorities of the major economic powers worked together to stabilize international financial conditions and minimize disruption to international trade and investment. It was precisely the failure of this cooperation after 1929 that had turned a localized recession into a global depression. To avoid any recurrence of this outcome and to rebuild an integrated economy, the governments of the principal economies had to work together.

The third lesson that guided plans for the post-World War II economic order was that for governments to sustain such cooperation they would need strong domestic political support. Mutual efforts to contain international economic problems usually involve national sacrifice, and domestic constituencies needed to be convinced that the costs of compromise and collaboration were worth the benefits. If constituents were unwilling to back the government's efforts to cooperate with its economic partners, cooperation would not be forthcoming—and without cooperation, efforts to rebuild an integrated world economy would fail.

With these three lessons in mind—domestic political support permitting the international cooperation necessary to sustain desirable economic integration—American and British planners went about attempting to construct a world economic order that fulfilled these requirements. And the first question to ask is why, after decades of failures, Anglo-American politicians were successful at reconstituting some semblance of an open international economy in the years after 1945.

Bretton Woods

The international economy that emerged after World War II had a number of striking features. The first was that its broad outlines were, unique among all international economic orders past or present, planned and implemented by government decree. The general contours of the world economy that emerged (at least in the capitalist world) after 1945 were designed while the war was still raging, largely by an American delegation headed by Harry Dexter White and a British delegation headed by John Maynard Keynes. The blueprint was adopted by forty-four Allied governments at an international conference that met at Bretton Woods, New Hampshire, in the summer of 1944. The fact that governments were central to drawing up the postwar international economic system was indicative of the central organizing principles of the new system, which combined a reliance upon free markets with the new tools of government macroeconomic management.

The second defining feature of the Bretton Woods system, as it came to be known, was a broad commitment to open markets at home and abroad. The system's architects were convinced that future economic growth required a restoration of normal patterns of international trade, investment, and payments out of the wreckage caused by two decades of depression and war. They designed a series of international institutions, all of which aimed to oversee the recovery of international economic exchange from its collapse in the 1930s.

The International Monetary Fund was empowered to oversee the reconstruction of the international monetary and financial system out of the ruins of the gold standard and its interwar successor. The Bretton Woods monetary system, as it evolved out of the designs of Keynes and White, was based on a U.S. dollar fixed to gold at thirty-five dollars an ounce, and other currencies whose values were fixed to the dollar but could be changed as policy makers felt necessary. This system of "fixed but adjustable" exchange rates provided what one prominent New York banker had referred to in 1936 as "a union of what was best in the old gold standard, corrected on the basis of experience to date, and of what seems practicable in some of the doctrines of 'managed currencies.'"³ It provided some of the predictability of the gold

standard but without the rigid constraints that had made gold unworkable in the 1930s.

Another Bretton Woods institution, the International Bank for Reconstruction and Development (World Bank), was meant to help restore international investment flows, especially to developing countries. A major obstacle to long-term investment was the inadequacy of the economic infrastructure in many poor societies, with private investors unable or unwilling to finance construction of this infrastructure. The Bank would borrow in the major capital markets, its debts guaranteed by its rich members, and then lend money at attractive rates to developing-country governments for the construction of projects such as power plants and port facilities. This would help smooth the way for private international investors to follow.

Yet another Bretton Woods institution concerned itself with opening world trade. After one false start, the major powers set up the General Agreement on Tariffs and Trade (GATT), a bargaining forum that facilitated the negotiation of reduction in obstacles to international trade. A series of bargaining "rounds" under GATT auspices reduced trade barriers substantially, roughly to where they had been at the height of the era of free trade in the nineteenth century.

In addition to its government origins and its emphasis on liberalizing international economic relations, the Bretton Woods system had a third, very important, characteristic. It was founded on the principle that modern political economies required substantial government intervention in the economy, in particular, active macroeconomic demand management and extensive social insurance policies. In most countries during the age of the pre-1914 open economy, there had been little government involvement in economic affairs: minimal active monetary policy, no fiscal policy to speak of, and barely any social insurance. But after 1918, with the spread of democracy, the rise of organized labor and labor-based political parties, and the development of modern industrial economies, virtually every advanced nation had adopted some form of the social-democratic welfare state. The Bretton Woods system accepted, indeed, attached importance to, this development. Its architects believed both in international economic integration and in the modern welfare state and assumed that the two could be compatible.

As this quick survey indicates, the Bretton Woods system was in almost every way a compromise. Economically, it attempted to find the middle ground between globalism and national economic management, between free markets and government intervention in the economy. Politically, it reflected the class compromises that grew out of the 1930s, among big business, big labor, and the middle classes. Ideologically, it brought together the Center Left and the Center Right against the extremes of fascism and communism.

The postwar economic order also reflected compromise in its gradualism and in the exceptions it allowed for politically controversial measures. In the commercial realm, for example, even as the GATT oversaw a general liberalization of international trade, it avoided confronting the most troublesome areas of world trade. GATT negotiations excluded farm products, for example, as farmers almost everywhere vehemently opposed liberalization. The GATT also exempted developing countries, strongly committed to protectionist methods to encourage industrial development at home. By the same token, the Bretton Woods monetary and financial order rested upon the expectation that governments would limit short-term capital movements in order to maintain a degree of policy independence. Indeed, over the course of the Bretton Woods period, every major participant in the monetary system imposed strict capital controls. This series of arrangements maintained the general commitment to international economic integration but permitted governments wide leeway in their pursuit of national social, political, and economic goals. And this series of compromises was no accident but, rather, a central precept of the system—the belief that the rigidity of the gold-standard classical order had led to its collapse.

Explaining the Postwar Order

What, then, explains the emergence of this international economic arrangement? Attempts to create something similar had failed miserably for twenty years after World War I. What had changed?

The easy answer is that America had changed. American recalcitrance had posed a major obstacle to international economic cooperation in

the interwar period. In contrast, the new world economic order built after 1945 was largely designed by Americans and implemented under the leadership of the U.S. government. But what exactly had changed America, and why? The change in American position was not inevitable; and, in fact, it came as a surprise to many informed observers.

After World War I, despite attempts by the Wilson administration to resurrect the international order, the United States had quickly backed away from playing a leadership role in world affairs. In the 1920 elections a Republican Party dominated by its “isolationist” wing swept into power. As a result, the United States did not ratify the Versailles Treaty, did not join the League of Nations, and refused to participate in most of the international economic consultations that were attempting to restore an open world economy. A penchant for unilateralist nationalism—commonly referred to as isolationism—prevailed until 1934, when New Deal Democrats began to dismantle it; yet the Great Depression and war made this reversal largely irrelevant. As World War II came to an end, Americans and Europeans who wanted to avoid another collapse into conflict feared that the United States might repeat its previous trajectory.

In fact, prospects for a major shift in American international economic policy did not appear encouraging. In 1946 the Republicans swept the House and Senate and were widely expected to win the White House in 1948. This was the same Republican Party that had been a stronghold of isolationism twenty years earlier, and it was led by Senator Robert Taft, a conservative anti-interventionist. Public opinion was still wary of American engagement abroad: in 1948, with the Cold War already in full swing, more than one-third of those polled by Gallup agreed that “since the war this country has gone too far in concerning itself with problems in other parts of the world.”⁴ While there was probably more sympathy for international involvement in 1945 than there had been in 1925, popular enthusiasm for a major American role was muted. This was especially true with respect to economic policy.

Yet U.S. foreign economic policy resumed the generally liberalizing trend that had started during the New Deal, with the United States working diligently to create an open international economic order.

Some suggest that this was due to the lessons of the Great Depression, especially the demonstration that very high trade barriers enacted by the United States in 1930 under the Smoot-Hawley Tariff had worsened economic conditions. However, there is very little evidence for this "learning" hypothesis. Almost all of the support for the Smoot-Hawley Tariff came from Republicans. And when, in 1934, Congress voted on the Reciprocal Trade Agreements Act to reverse this protectionism and begin the liberalizing trend, eighty-four of the eighty-six Republican legislators who had voted for the tariff voted *against* measures to reduce it. Only two Republican supporters of Smoot-Hawley seemed to have learned any particular lesson from its aftermath.⁵

There were two principal reasons for the American commitment to economic openness after 1945, one economic and the other political. On the economic front, the conditions that the U.S. economy confronted in the late 1940s differed fundamentally from those of the 1920s. After the second war, most of the country's potential competitors were in shambles, while the U.S. economy was booming. The world's thirst for American goods seemed endless, and no other country's industries seemed capable of contending with American industry for global markets. American manufacturers who had previously worried more about imports than about exploring markets abroad were now increasingly interested in exports and little troubled by foreign competitors. Indeed, a crucial group of Republican legislators that switched sides from protection to liberalization represented Northern districts in which exports had grown substantially in importance and the threat of imports had faded.⁶ Opposition to American involvement in the world economy weakened as America's role in the world economy grew increasingly predominant.

The second source of American interest in international economic integration related to the politics of American national security. Many Americans, and many American politicians, who had previously been hostile or indifferent to international economic affairs came to see them as an important part of the country's foreign relations. After 1947 the world divided into two camps, one capitalist and one Communist. American leadership of the Western camp was, at least at the outset, primarily military and diplomatic. Yet separating military from eco-

nomic matters posed difficulties. It hardly seemed reasonable for the United States to spend billions helping to rebuild the economies of Western Europe and Japan and at the same time to abandon these countries to their own economic devices. It made much more sense for the Western capitalist coalition to cooperate on economic matters as its members did on military and political ones. Indeed, inasmuch as American security was now closely tied to the strength and stability of its allies, the United States had a powerful incentive to promote their prosperity. Giving America's allies access to American markets and American capital seemed a natural concomitant to providing them with America's nuclear umbrella and diplomatic support.⁷

Both strategic and political factors, each blending ideological with more pragmatic considerations, came into play. There was an intellectual consistency to the argument that an inclusive pro-American, anti-Soviet alliance in the military and diplomatic spheres also needed to be inclusive in the economic sphere—that the United States could not build an integrated Western political bloc without also building an integrated economic bloc. Yet taking this approach also paid off in the domestic political realm. There were Americans who strongly supported economic integration but were not overly concerned about military affairs; and there were those who wanted a strong military alliance against the Soviet Union but were indifferent to economics—in very rough terms, Northeastern economic internationalists and Midwestern anti-Communists. Combining economic cooperation with military cooperation satisfied both groups.

The forging of this domestic consensus goes far toward explaining why the United States was willing and able to take the lead in constructing a new international economic order. And American leadership was crucial. The United States and its allies occupied West Germany, Italy, and Japan, all three essential to the creation of a new world economy, and it dominated the foreign relations of the other major Western powers. But while America's newfound eagerness for international economic cooperation was crucial, so too was European willingness to participate. Strong forces in many Western European countries were less than enthusiastic: Communists in Italy, France, and Belgium; nationalists in Germany. This resistance was swiftly overcome.

European collaboration stemmed in part from new geopolitical realities, as Western governments concerned about the Soviet Union gravitated toward the American orbit. But this was not all; domestic political conditions in Europe and Japan were particularly favorable. World War II and the Cold War had effectively lopped off the political extremes: the Far Right discredited by its fascist connections, the Far Left tainted by its association with the Soviet Union. As a consequence, neither the extreme right-wing nationalism of interwar business and agricultural groups nor the extreme left-wing redistributionism of interwar labor could get a hearing. What remained was a centrist consensus that brought together the (largely Social-Democratic) Center Left and the (largely Christian-Democratic) Center Right. The political forces comprising this coalition of the Center generally agreed on the desirability of both international economic openness and the welfare state; they shared a commitment to a gradualist middle ground that avoided extremism. The Bretton Woods system reflected this broad trend, a consensus on the desirability of a compromise that combined the market and the welfare state, both domestically and internationally.

The result proved extraordinarily successful, both economically and politically. By the 1960s, with the Bretton Woods system in full swing, the (capitalist) world economy was booming. World trade and investment took off and international finance revived. International monetary conditions were extremely stable. All this contributed to the Bretton Woods system's crowning achievement: the most rapid rates of economic growth in world history—rates that remain unsurpassed even today. Western Europe's output per person doubled between 1948 and 1964; Japan grew even more rapidly. By 1961, when the advanced industrial countries created their own club of rich nations, the Organization for Economic Cooperation and Development, its members—stretching from Japan through Western Europe to North America—were, for the first time, recognizably similar in their social, economic, and political organization and in their level of development.

From Bretton Woods to Globalization

The international economy of the Bretton Woods era appeared stable for nearly twenty-five years. But over the course of the 1970s the system ran into difficulties, and eventually it was fundamentally transformed. The result was a virtually global trend toward greater international economic integration.

By the late 1960s a divergence between monetary conditions in the United States and the rest of the industrial world was subjecting the Bretton Woods monetary order to considerable strain. American spending on the Vietnam War and on expanded social programs contributed to a higher rate of inflation in the United States than in Europe, which undermined confidence in the dollar. American austerity measures could have reduced inflation and restored confidence, but the U.S. government hesitated to sacrifice its domestic macroeconomic policy autonomy to maintain the gold-dollar link, even if this link was the centerpiece of the Bretton Woods monetary system. In the event, in August 1971, the United States broke the link and devalued the dollar, ending the Bretton Woods era of fixed but adjustable exchange rates.

Another source of tension in the Bretton Woods system grew, ironically, out of its success in rekindling international financial markets. With the restoration of macroeconomic stability and economic growth, financial institutions rediscovered foreign operations. By the early 1970s international financial markets were large and growing. The increased level of international financial flows helped undermine the fixed exchange rate regime by heightening speculative pressures on some currencies (including the U.S. dollar).

Once the Bretton Woods exchange rate arrangement ended, most major currencies began floating freely against one another. This loosened the previous monetary straitjacket, and a bout of inflationary pressures ensued. On top of this, in 1973, a cartel of oil-producing nations (the Organization of the Petroleum Exporting Countries, or OPEC) quadrupled the price of petroleum, putting further upward pressure on prices. A deep recession in the period 1973–1975 led to an

unaccustomed mixture of high unemployment and high inflation—"stagflation," as it was called. Another round of OPEC oil price increases in 1979-1980 further aggravated inflation.

Macroeconomic difficulties came to a head after 1979. To slow the rate of inflation, developed countries began to adopt more contractionary monetary policies, resulting in extremely high interest rates and several years of recession. While inflation eased in the advanced capitalist countries, unemployment remained very high. In this crisis atmosphere, developed countries gradually moved to recommit themselves to a market orientation and international economic openness. Governments exercised greater monetary restraint, deregulated many economic activities, and privatized previously public enterprises. The trend was epitomized by the policies of the British prime minister Margaret Thatcher and the American president Ronald Reagan, who made the case for less government involvement in their respective economies. Reagan did so, anomalously, while running up enormous budget deficits in the United States. Nonetheless, and despite such setbacks as a costly American banking crisis, by the mid-1980s the developed capitalist countries had made clear their renewed dedication to an integrated international economy.

More surprising were trends in the developing countries. After many decades of economic nationalism and protectionism, they emerged from the crises of the 1980s with a newfound orientation toward international markets. These crises, along with the accumulated problems of relatively closed markets in an increasingly open world economy, led almost every country in Latin America, Africa, and Asia to jettison the prior inward orientation in favor of much more economic openness to the rest of the world. Developed and developing capitalist countries continued to reduce barriers to trade and investment, leading to a characterization of the era as one of "globalization."

The most stunning development on the path to globalization was the collapse of the centrally planned economies. The economic problems of the late 1970s and early 1980s eventually drove these countries away from central planning and toward international markets. China and Vietnam moved first, in 1979, while maintaining Communist rule, both governments reoriented their economies toward exporting to

the capitalist world. After 1985 the Soviet Union embarked on an attempt at gradual reform, which was quickly overtaken by events as the country's social and political system unraveled. After the USSR collapsed in 1991, the entire Soviet bloc quickly abandoned central planning and moved toward capitalism at speeds varying from gradual to breakneck.

In a way, the very success of the Bretton Woods order caused its demise. Ever more inclusive patterns of economic integration undermined the gradualism and compromises that had characterized the postwar economic settlement. At the same time, the connection between military and economic interests became less clear as first détente and then the end of the Cold War made the solidarity of the Western bloc seem less relevant. In these circumstances, international markets took precedence over purely domestic considerations, and international economic considerations took precedence over national security concerns. Inasmuch as concern about the Soviet Union and its allies had been a major source of Western political and economic solidarity, the collapse of the Soviet Union and its bloc rendered this particular source obsolete. By the first years of the new century, the international economy had become something very different than it had been between the 1940s and the 1980s, the heyday of the American Century. But what sort of international economic order has arisen in the American Century's wake, and what can we expect of it?

The Contemporary International Economy

Today's globalized international economy is fundamentally different from that spearheaded by the United States in the aftermath of World War II. For one thing, virtually every nation—not just the United States and its closest allies—now engages in the world of international trade, finance, and investment. For another, the principles of compromise and gradualism that characterized the Bretton Woods order have given way to a more unqualified belief in the desirability of removing barriers to international economic exchange, and to a generalized skepticism about heavy-handed government intervention in national economies.

As a result, the international economy of the early twenty-first century is a global, integrated market system. Capital moves far more freely around the world than the Bretton Woods negotiators ever anticipated, and far more countries have joined the World Trade Organization and have committed to limiting their trade barriers than was originally expected in the late 1940s. More than at any time since 1914—and perhaps more than at any time in human history—something approximating a generally open international economy exists.

This evolution toward an ever more tightly integrated world economy has taken place alongside the development of major regional economic blocs. The European Union (EU), which started as a modest league of six nations, now encompasses virtually all of Europe, from Ireland to Bulgaria and from Cyprus to Finland. From a simple customs union, the EU has become a true single market that has eliminated barriers to the movement of goods, capital, and people while harmonizing the regulation of investment, migration, product and production standards, professional licensing, and many other economic activities. A subset of seventeen EU members shares a common currency, the euro, and a common European Central Bank. Meanwhile, the United States, Canada, and Mexico formed a free trade area in 1994, as did Brazil, Argentina, Uruguay, and Paraguay. Similar regional economic arrangements have proliferated elsewhere.

The growth of these regional blocs has contributed to the expansion of economic authority beyond the traditional economic powers. While the United States remains the world's largest economy, it no longer stands alone in terms of economic influence. The United States today has become, in many ways, just another country—subject to the vagaries of international economic trends in a way that Henry Luce would have found bewildering back in 1941.

Many of the new features of the international economic order were illustrated with the economic crisis that began in 2007. The United States found itself in the midst of a debt crisis not unlike those that had typically afflicted developing countries. And even as the U.S. economy and world economies struggled to recover, Americans found themselves heavily reliant on foreigners for goods, capital, technology, and markets. Perhaps even more surprising, chief among the foreigners upon

whom America had come to rely was China, which was now a major creditor of the U.S. government and of Americans more generally.

The new economic configurations of the early twenty-first century clearly signaled the end of the American Century. The United States is today one among several major centers of economic power, with other countries gaining ground. In international monetary relations, the dollar's predominance can no longer be taken for granted. America's massive debt to foreigners—hardly a sign of American predominance—has emerged as one of the principal problems in global finance.

The world economy today is, in many ways, far more democratic than it was in the aftermath of World War II. No single country can determine the future course of international monetary, financial, and commercial relations, and none can dictate the characteristics of the international institutions governing those relations. Areas of the world that had stagnated for centuries are now experiencing an unprecedented pace of economic growth and development, lifting hundreds of millions of people out of poverty.

Today's world economy is very much a product of the plans devised during World War II, under American leadership, and implemented, largely with American blueprints, in the years after the war ended. The United States was very successful, during its few decades of global preeminence, in rebuilding an open world economy out of the unpropitious ruins of a failed international order. This success fundamentally changed the way the international economy worked, and these fundamental changes made obsolete many of the original organizing principles devised at Bretton Woods. Today the United States can no longer determine the future of the world economy. America succeeded in creating an economic order largely in its own image, but the subsequent evolution of the world economy helped bring the American Century to a premature end.