4 Rebuilding a World Economy: The Post-war Era

The Second World War broke out a mere two decades after the end of the First World War. It was fought between the Axis powers (mainly Nazi Germany, Japan and Italy) and the Allies (Britain, France, the Soviet Union and the US). It was a war waged for six years on many fronts, in many places, over land, on sea, in the air.

Fig. 24 – German forces attack Russia, July 1941.
Hitler's attempt to invade Russia was a turning point in the war.

Once again death and destruction was enormous. At least 60 million people, or about 3 per cent of the world's 1939 population, are believed to have been killed, directly or indirectly, as a result of the war. Millions more were injured.

Unlike in earlier wars, most of these deaths took place outside the battlefields. Many more civilians than soldiers died from war-related causes. Vast parts of Europe and Asia were devastated, and several cities were destroyed by aerial bombardment or relentless artillery attacks. The war caused an immense amount of economic devastation and social disruption. Reconstruction promised to be long and difficult.

Two crucial influences shaped post-war reconstruction. The first was the US's emergence as the dominant economic, political and military power in the Western world. The second was the dominance of the Soviet Union. It had made huge sacrifices to defeat Nazi Germany, and transformed itself from a backward agricultural country into a world power during the very years when the capitalist world was trapped in the Great Depression.

Fig. 25 – Stalingrad in Soviet Russia devastated by the war.

4.1 Post-war Settlement and the Bretton Woods Institutions

Economists and politicians drew two key lessons from inter-war economic experiences. First, an industrial society based on mass production cannot be sustained without mass consumption. But to ensure mass consumption, there was a need for high and stable incomes. Incomes could not be stable if employment was unstable. Thus stable incomes also required steady, full employment.

But markets alone could not guarantee full employment. Therefore governments would have to step in to minimise fluctuations of price, output and employment. Economic stability could be ensured only through the intervention of the government.

The second lesson related to a country's economic links with the outside world. The goal of full employment could only be achieved if governments had power to control flows of goods, capital and labour.

Thus in brief, the main aim of the post-war international economic system was to preserve economic stability and full employment in the industrial world. Its framework was agreed upon at the United Nations Monetary and Financial Conference held in July 1944 at Bretton Woods in New Hampshire, USA.

The Bretton Woods conference established the International Monetary Fund (IMF) to deal with external surpluses and deficits of its member nations. The International Bank for Reconstruction and Development (popularly known as the World Bank) was set up to finance post-war reconstruction. The IMF and the World Bank are referred to as the Bretton Woods institutions or sometimes the Bretton Woods twins. The post-war international economic system is also often described as the Bretton Woods system.

The IMF and the World Bank commenced financial operations in 1947. Decision-making in these institutions is controlled by the Western industrial powers. The US has an effective right of veto over key IMF and World Bank decisions.

The international monetary system is the system linking national currencies and monetary system. The Bretton Woods system was based on fixed exchange rates. In this system, national currencies, for example the Indian rupee, were pegged to the dollar at a fixed exchange rate. The dollar itself was anchored to gold at a fixed price of $35 per ounce of gold.

Fig. 26 – Mount Washington Hotel situated in Bretton Woods, US.
This is the place where the famous conference was held.

Discuss

Briefly summarise the two lessons learnt by economists and politicians from the inter-war economic experience?

4.2 The Early Post-war Years

The Bretton Woods system inaugurated an era of unprecedented growth of trade and incomes for the Western industrial nations and Japan. World trade grew annually at over 8 per cent between 1950 and 1970 and incomes at nearly 5 per cent. The growth was also mostly stable, without large fluctuations. For much of this period the unemployment rate, for example, averaged less than 5 per cent in most industrial countries.

These decades also saw the worldwide spread of technology and enterprise. Developing countries were in a hurry to catch up with the advanced industrial countries. Therefore, they invested vast amounts of capital, importing industrial plant and equipment featuring modern technology.

4.3 Decolonisation and Independence

When the Second World War ended, large parts of the world were still under European colonial rule. Over the next two decades most colonies in Asia and Africa emerged as free, independent nations. They were, however, overburdened by poverty and a lack of resources, and their economies and societies were handicapped by long periods of colonial rule.

The IMF and the World Bank were designed to meet the financial needs of the industrial countries. They were not equipped to cope with the challenge of poverty and lack of development in the former colonies. But as Europe and Japan rapidly rebuilt their economies, they grew less dependent on the IMF and the World Bank. Thus from the late 1950s the Bretton Woods institutions began to shift their attention more towards developing countries.

As colonies, many of the less developed regions of the world had been part of Western empires. Now, ironically, as newly independent countries facing urgent pressures to lift their populations out of poverty, they came under the guidance of international agencies dominated by the former colonial powers. Even after many years of decolonisation, the former colonial powers still controlled vital resources such as minerals and land in many of their former colonies.

Large corporations of other powerful countries, for example the US, also often managed to secure rights to exploit developing countries' natural resources very cheaply.

At the same time, most developing countries did not benefit from the fast growth the Western economies experienced in the 1950s and 1960s. Therefore they organised themselves as a group – the Group of 77 (or G-77) – to demand a new international economic order (NIEO). By the NIEO they meant a system that would give them real control over their natural resources, more development assistance, fairer prices for raw materials, and better access for their manufactured goods in developed countries' markets.

Box 4

What are MNCs?

Multinational corporations (MNCs) are large companies that operate in several countries at the same time. The first MNCs were established in the 1920s. Many more came up in the 1950s and 1960s as US businesses expanded worldwide and Western Europe and Japan also recovered to become powerful industrial economies. The worldwide spread of MNCs was a notable feature of the 1950s and 1960s. This was partly because high import **tariffs** imposed by different governments forced MNCs to locate their manufacturing operations and become 'domestic producers' in as many countries as possible.

New words

Tariff – Tax imposed on a country's imports from the rest of the world. Tariffs are levied at the point of entry, i.e., at the border or the airport.

4.4 End of Bretton Woods and the Beginning of 'Globalisation'

Despite years of stable and rapid growth, not all was well in this post-war world. From the 1960s the rising costs of its overseas involvements weakened the US's finances and competitive strength. The US dollar now no longer commanded confidence as the world's principal currency. It could not maintain its value in relation to gold. This eventually led to the collapse of the system of **fixed exchange rates** and the introduction of a system of **floating exchange rates**.

From the mid-1970s the international financial system also changed in important ways. Earlier, developing countries could turn to international institutions for loans and development assistance. But now they were forced to borrow from Western commercial banks and private lending institutions. This led to periodic debt crises in the developing world, and lower incomes and increased poverty, especially in Africa and Latin America.

The industrial world was also hit by unemployment that began rising from the mid-1970s and remained high until the early 1990s. From the late 1970s MNCs also began to shift production operations to low-wage Asian countries.

China had been cut off from the post-war world economy since its revolution in 1949. But new economic policies in China and the collapse of the Soviet Union and Soviet-style communism in Eastern Europe brought many countries back into the fold of the world economy.

Wages were relatively low in countries like China. Thus they became attractive destinations for investment by foreign MNCs competing to capture world markets. Have you noticed that most of the TVs, mobile phones, and toys we see in the shops seem to be made in China? This is because of the low-cost structure of the Chinese economy, most importantly its low wages.

The relocation of industry to low-wage countries stimulated world trade and capital flows. In the last two decades the world's economic geography has been transformed as countries such as India, China and Brazil have undergone rapid economic transformation.

New words

Exchange rates – They link national currencies for purposes of international trade. There are broadly two kinds of exchange rates: fixed exchange rate and floating exchange rate

Fixed exchange rates – When exchange rates are fixed and governments intervene to prevent movements in them

Flexible or floating exchange rates – These rates fluctuate depending on demand and supply of currencies in foreign exchange markets, in principle without interference by governments

Write in brief

1. Give two examples of different types of global exchanges which took place before the seventeenth century, choosing one example from Asia and one from the Americas.
2. Explain how the global transfer of disease in the pre-modern world helped in the colonisation of the Americas.
3. Write a note to explain the effects of the following:
   a) The British government's decision to abolish the Corn Laws.
   b) The coming of rinderpest to Africa.
   c) The death of men of working-age in Europe because of the World War.
   d) The Great Depression on the Indian economy.
   e) The decision of MNCs to relocate production to Asian countries.
4. Give two examples from history to show the impact of technology on food availability.
5. What is meant by the Bretton Woods Agreement?

Write in brief

Discuss

6. Imagine that you are an indentured Indian labourer in the Caribbean. Drawing from the details in this chapter, write a letter to your family describing your life and feelings.
7. Explain the three types of movements or flows within international economic exchange. Find one example of each type of flow which involved India and Indians, and write a short account of it.
8. Explain the causes of the Great Depression.
9. Explain what is referred to as the G-77 countries. In what ways can G-77 be seen as a reaction to the activities of the Bretton Woods twins?

Discuss

Project

Find out more about gold and diamond mining in South Africa in the nineteenth century. Who controlled the gold and diamond companies? Who were the miners and what were their lives like?

Project