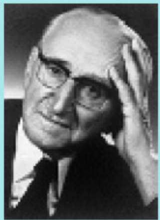
Ordnungspolitische Diskurse
Discourses in Social Market Economy



Bernhard Seliger

Theories of economic miracles

Diskurs 2010 – 01

Bernhard Seliger

Theories of economic miracles

Abstract

Studies into the *Wealth of Nations* have been the aim of economics since Adam Smith. However, the spectacular rise of some economies, beginning with industrializing England in the 18th century, has been of particular interest. England's rise has been as miraculous in the eyes of the observers as the rise of Germany and Japan from the ashes of World War II or the rise of South Korea from one of the poorest countries in the world to the league of OECD members in the second half of the twentieth century and later the rise of China. Nevertheless, to write about theories of "economic miracles" seems to be daring, since the architects of these "miracles", like fervently Ludwig Erhard, flatly denied anything miraculous in the development of their respective economies. Modestly, they spoke of the natural result of liberalization or, in another case, "getting the basics right". If this is the case, are there any ways to stellar economic performance to be emulated? Are there, more modestly, any lessons from the "economic miracles" of the past for the future development of other economies?

Keywords:

Economic Miracle, Growth Performance, Economic Order, Institutional Factors of Growth, Expectation Equilibrium

Seliger, Bernhard – PD Dr. habil.
Hanns-Seidel-Stiftung - Seoul Office
Room 501, Soo Young Bldg.,
64-1, Hannam 1 Dong, Yongsan-gu,
Seoul, Republic of Korea
bjseliger@yahoo.de

Bernhard Seliger

Theories of economic miracles

1. Introduction

This paper discusses the thought on "economic miracles" regarding several prominent cases, namely Germany, Japan and larger East Asia. A number of macroeconomic, political, politico-economic and institutional factors have been pointed out as responsible for their miraculous development. While the development cannot be disconnected from its historical and institutional background, in particular institutional factors determining the economic order (*Ordnungspolitik*) can be identified as important for the "economic miracles". In particular, the existence of an expectation-equilibrium allowing for stable economic policies over time has been so far relatively underexposed. Without allowing for a naïve blueprint towards an economic miracle, lessons for development processes can be drawn.

While the notion "economic miracle" denotes something spectacular, in fact it has been applied to quite a number of very diverse cases of economic development, diverse in time, extent, style, and geography. In fact, "miracles" seem to have happened fairly often, if the use of the term "economic miracle" is a reliable guide. Among others, the economic development of Europe, Asia, Korea, Japan, Germany, Taiwan, India, the Netherlands, Botswana, Estonia, Ireland, China, Argentine, Chile, Malaysia, Spain, Dubai, the United Kingdom and Vietnam has been described as miraculous at one point or another. Given the high priority of the underlying quest, namely that for rapid economic growth, the identification of so many miracles becomes more understandable. Studies into the *Wealth of Nations* have been the aim of economics since Adam Smith. However, the spectacular rise of some economies, beginning with industrializing England in the 18th century, has been of particular interest. England's rise has been as miraculous in the eyes of the observers as the rise of Germany and Japan of the ashes of World War II or the rise of South Korea from one of the poorest countries in the world to the league of OECD members in the second half of the twentieth century and later the rise of China. Miraculous in these cases were as well the new technologies, epitomized in the steam engine of the industrial revolution, the mechanization in the early and mid-20th

century and the microchip in the late 20th century, new forms of organization like the beginning industrial production in the 19th century or the assembly-line of car production in the 20th century, and the outcome, measured in terms of population dynamics and consumption per capita.

To write about theories of "economic miracles" seems to be daring, since the architects of these "miracles", like fervently Ludwig Erhard ("there are no miracles!"), flatly denied anything miraculous in the development of their respective economies. Modestly, they spoke of the natural result of liberalization or, in another case, "getting the basics right". If this is the case, are there any ways to stellar economic performance to be emulated? Are there, more modestly, any lessons from the "economic miracles" of the past for the future development of other economies? This paper discusses the thought on "economic miracles" regarding several prominent cases, namely Germany, Japan and larger East Asia. A number of macro-economic, political, politico-economic and institutional factors have been pointed out as responsible for their miraculous development. The second part looks back into the case of Germany's economic miracle, the third section discusses Japan and the East Asian growth experience. Section 4 discusses commonalities and differences of the cases. While development cannot be disconnected from its historical and institutional background, in particular institutional factors determining the economic order (*Ordnungspolitik*) can be identified as important for the "economic miracles". In particular, the existence of an expectation-equilibrium allowing for stable economic policies over time has been so far relatively underexposed.

The conclusion (5.) discusses the applicability of the lessons of "miracle" countries for economic policy making purposes. Without allowing for a naïve blueprint towards an economic miracle, lessons for development processes can be drawn.

2. The German "economic miracle" revisited – multiple causes, but no arbitrariness

In the 19th century, Germany had been a latecomer in industrialization, and this means also in growth performance. This changed around 1860, when Germany, like other European economies, achieved a strong push in growth rates which lasted until

the outbreak of World War I. Afterwards, the growth experience of European and North American countries began to differ strongly.

All countries suffered from the war years and the aftermath of the war. But for some countries the decline in growth rates was less strong (notably, the USA and Canada), and for some countries the end of the 1920s despite the Great Depression brought a renewed strong growth performance, e.g. for Sweden. Germany, on the other hand, remained on a path of moderate growth in terms of the growth trend. After World War II, this changed quite spectacularly when the economic reforms of 1948 and 1949 were implemented and Germany overtook most other European states in growth performance.[1]

The first phase of catch-up growth in the 19th century was triggered by technological developments, economic liberalization and integration of the German economic area and related population dynamics. Since the end of the 19th century, legal developments in Germany, in particular the decision by the German Imperial Court (Reichsgericht) of 1897 that cartels are legally binding, led to a centralization of economic power, in particular in key industries. The war economy of World War I and the subsequent phase of economic unrest in war-torn Germany reinforced cartels, like in the chemical industry (IG Farben) and the steel industry (Vereinigte Stahlwerke). At the same time, there was a secular trend to the centralization of political power. This began with the domination of Germany by the Prussian state after the realization of German unity in 1871, increased in the centralistic model of the first German republic, the Weimar Republic of 1919 to 1933 and peaked finally during the National Socialist phase during 1933 to 1945. This can be seen by comparing local autonomy and spending on different levels of government, both of which saw strong centralizing tendencies until the virtual abolishment of local autonomy by National Socialism. The totalitarian state after 1933 could not completely erase economic freedom, like its communist totalitarian counterpart in the Soviet Union did by nationalization, but was on the way to this goal and in the war economy after 1939 closely guided the industrial sector. A success of National Socialism probably would not have redressed, but rather reinforced nationalization tendencies.

---

[1] For historical data see Maddison (1991), pp. 206-219, and the figure in Landes (1999), p. 247.

This is the backdrop for the rise of the Freiburg School of Economics as the intellectual forerunner and the introduction of the Social Market Economy in Germany as economic policy model by Ludwig Erhard as economic minister and Alfred Müller-Armack as his state secretary.[2] Dubbed an „economic miracle“, Ludwig Erhard always stressed that the economic order implemented after 1948 was the reason for growth and that this was nothing miraculous. Erhard's reputation grew together with the German economy, a fact explaining his later election as the second German chancellor after Konrad Adenauer. Growth rates seem to have justified this decision, however, there have been forwarded competing explanations for the superior German growth performance of the time.

•	The miracle as a reconstruction boom
•	The miracle as return to pre-war growth path
•	The miracle and the American influence
•	The miracle and the role of personalities
•	The miracle as currency-based mercantilism
•	The miracle as a political ex-post rationalization
	versus
•	ordo-liberal explanations (institutions, their implementation, and the rise and decline of nations)

Table 1: Competing explanations for Germany's Economic Miracle

In the 1980s, economists and economic historians began to challenge the view that the German growth miracle was a consequence of economic policy decisions like the introduction of the new German Deutsche Mark. Rather, it was seen as the almost mechanical consequence of a reconstruction boom based on large-scale capital destruction in World War II (Reichel 2002). According to the neoclassical growth model of Solow long-run growth is determined by population dynamics and technical

[2] For a history of the introduction of the Social Market Economy see Van Hook (2004), for its development and decline see Giersch at al. 1992.

progress. The destruction of the capital stock leads to a declining capital/ labour ratio, far below the long-run equilibrium. At the same time, productivity of capital is strongly increasing, Higher productivity growth rates means higher per-capital income growth rates, asymptotically approaching the long-run growth path.[3]

A related argument sees the German growth performance of the post-World War II phase as a return to a long-run, pre-war growth path. The full utilization of capacity, rapid capital formation, structural change enforced by destruction and the immigration of millions of refugees helped to fuel growth rates. Both arguments, the post-war reconstruction boom due to the renewal of the capital stock as well as the return to a long-run growth part, can explain partly the post-war growth, but according to regressions run by Reichel (2002) on medium-term growth rates there is a large, unexplained residuum so that the concludes, “that there certainly was strong reconstruction growth after the Second World War, but there is also strong evidence for an additional growth-promoting effect that perfectly coincides with the economic reforms undertaken by Erhard” (pp. 436-437). In particular, the reconstruction boom should also apply to East Germany, which it did not. Despite forced savings by the new communist regime growth rates always lagged clearly behind those of West Germany.

Another argumentation line against the particular effects of the economic reforms of 1948 to introduce the “Social Market Economy” is that American aid, American influence and the Marshall plan were strongly contributing to German growth. The political economy side of this argument is that currency reform and price liberalization were impossible without decree by the occupying forces and that the credit for reform accordingly should not go to Erhard and his economic policy.

While formally right, it should be noted that sweeping price liberalization was not at all uncontested among occupying authorities and German politicians alike in the post-war period and that the allied forces of the three Western zones tried to minimize central structures in Germany by founding not a German central bank, but rather a “Bank of States” (Bank deutscher Länder) in the spring of 1948.[4] This approach failed and finally the BdL became a fully-fledged central bank, the Bundesbank. But this episode shows that American support for German liberalization was not as

[3] This theory is an important explanation for expectations of conditional convergence of developing countries.

[4] See Horstmann (1985).

unequivocal as presumed by the supporters of the theory that American influence can explain German growth performance after 1948. Certainly, while initially after 1945 the USA and in particular the United Kingdom with its new labour government favoured Social Democracy, later with the rise of cold war confrontation the interest in a clear market economic institutional system in Germany rose (Van Hook 2004, p. 5). However, price reforms after the currency reform of 1948 were initiated by Erhard without explicit agreement of the occupying authorities.

As a macro-economic argument, the influence of the USA is seen in the Marshall plan aid (European Recovery Program) and, more general, the tendency for worldwide Keynesian demand policies after World War II. This again misses an important part of the explanation, since Marshall plan aid was rather symbolic for Germany (compared to much more substantial aid to the neighbouring states) and Keynesian demand policies did certainly contribute to stabilize demand after the war, but should have had no particular influence on Germany, which still had to wait some time before it was fully re-integrated in the world economy.

Economic policy and economic history are not simply determined by mechanic historical „forces“, but also the result of personalities, creativity and alertness, or, as Ludwig von Mises put it, „*homo agens*“.

Erhard's personality and personal experience as well as that of his contemporaries is also important to understand his later economic policy. Born as the son of a textile trader and himself learning textile trade before World War I, he was later, after war and studies of economics and business management a lobbyist for SME and consumer industries as well as macro-economic analyst in the “Institut für Wirtschaftsbeobachtung der Deutschen Fertigindustrie” in 1928. Already in the 3rd Reich he spoke out against the primacy of heavy industry and later his strong emphasis on SME as the backbone of German industry was certainly influenced by this former occupation. Müller-Armack, his state secretary in the economic ministry, had a similar background in the SME-dominated textile sector, in the “*Forschungsstelle für Allgemeine und Textile Marktwirtschaft”* (Research institute for general and textile market economy). The personal background of the founders is certainly important to explain their later decisions, however it cannot really be seen as a substitute for the explanation of German growth performance after World War II

by ordo-liberalism and the Social Market Economy, but rather as a help to understand their development.[5]

Looking at West Germany's growth after 1948, the important and constant contribution of trade, unusual for such a large economy, led to the explanation of Germany's economic performance as the result of currency-based mercantilism. West Germany's "Deutsche Mark" entered the Bretton Woods system arguably undervalued (at 4.20 to the US-$ at September 18, 1948) and consequently faced a long phase of sustained competitiveness of its exporting industries. The Korean War crisis of 1950, when Ludwig Erhard decided despite strong pressure from opposition and trade unions against price controls, fostered the internal reputation of the Deutsche Mark as a stable currency. The London debt deal of 1953 and the settlement with Israel prevented another phase of currency instability like after World War I, when reparations and hyperinflation precluded sustained economic growth. While the German economy after 1948 was not miraculously liberalized in a big bang – for example, tariffs were still used as an instrument in crisis policy in the Korea crisis – external trade was a main factor to explain growth. However, this again (like the role of personalities) is not a competing explanation to that of the introduction of a new economic system as a basis for sustained growth, but rather an outcome of a policy favouring monetary stability – the primacy of monetary policy in the framework of Walter Eucken.

Finally, there has been the argument that the "economic miracle" is nothing else but an ex-post rationalization of favourable economic circumstances. Ludwig Erhard himself saw nothing miraculous in the economic miracle of the Social Market Economy. However, in particular after the Korean crisis and in the wake of the general election of 1953 the efforts to "sell" the economic success of the Social Market Economy increased. An important role was played by a group of industrialists, where notably heavy industry and mining was absent, called "Die Waage", which ran adds and cinema spots to convince people of the advantages of the Social Market Economy with the aid of modern marketing research and opinion polls. For the ruling Christian Democratic Union, to which chancellor Adenauer and economic minister Erhard belonged, as a modern, non-ideological party, the justification by economic

[5] This development also includes the aforementioned background of centralization in economy and politics, as well as a certain initial sympathy for National Socialism by some later opponents to its economic policies like Müller-Armack.

success was important (Spicka 2007). The notion “Social Market Economy” itself was deliberately designed to distinguish it from the “laissez faire economy”, without clearly indicating how, which is the reason Hayek called it a “weasel word”.

The above-mentioned theories deserve consideration and certainly they can explain partly German economic performance after 1948. However, they are either complementary – like explanations based on growth theory – or helpful in understanding economic policy making, but not contradicting the conclusion that Germany's economic policy decisions after 1948, based on ordo-liberal creed, played an important role in freeing the growth forces after the misallocation of resources through war and post-war administration. The ordo-liberal explanation in particular focuses on the role of stable money as a central and distinguishing feature of economic reform, the role of the liberalization of prices, and subsequently the role of competition policy, though here the link between the original blueprints of ordo-liberalism and actual economic policy were weakest. Additionally, the economic miracle as the role of the destruction of distributive coalitions by the war, as envisaged by Mancur Olson (1982), is an important explanation fitting into the ordo-liberal framework, though formulated in another context. All in all, the introduction of the Social Market Economy in Germany can be seen as a rare example of “theory-in-action”, a close relation of economic theory and policy making.

First of all, the primacy of monetary policy was based on the experience of hyperinflation in 1923 and the period of high inflation after 1945. Stability of money was a social and political issue – the rise of National Socialism in the 1920s had much to do with the loss or threat to income of the petty bourgeois – but also as a precondition for implementing the basic principle of a market economy, namely a functioning price system. It is no wonder that West Germany after 1949, though generally wary of nationalism after the war, experienced a particular form of it, namely “Deutsche Mark”-nationalism, a certain form of pride in the currency as well as an anxiety that currency stability might get lost. The comprehensive freeing of prices in 1948, after the currency reform, was the other pillar of the implementation of the basic principle of the market economy.

The influence of cartels, which allowed for freer domestic markets, was reduced considerably by the divestiture of leading cartels like IG Farben after World War II by the allied occupation forces. Later, Erhard fought long for a competition law, which

finally in 1957 was concluded. Though an independent cartel office should guarantee the strong position of competition, it never became quite as successful as the monetary authority, the Bundesbank. Erhard fought against exceptions from competition law nationally and in the new European Economic Community, but often in vain.

The destruction of distributive coalitions as described by Mancur Olson refers to the forcible end of asymmetric regulations in favour of certain business groups due to the war in Germany as well as in Japan, and, though to a more or lesser extent, in the other countries ravaged by the war. In peaceful time, asymmetric rent-seeking by interest groups leads to a sclerotization of economies due to decreased freedom and increased burdens by regulations and taxes in favour of certain special interests, namely those which are relatively more homogeneous and where the free-rider-problem can more easily be overcome.[6] The United Kingdom, where the war did not lead to a disruption of society and economic structures, suffered subsequently from the "English disease" in the 1970s, but also Germany and Japan, initially after World War II rapidly growing, saw declining growth rates and sclerosis. Though this theory has never been intended to describe a mechanical rise and decline of growth rates, it can explain the relative success of the Social Market Economy in its implementation phase, when adverse pressure groups were less well-organized and a window of opportunity for reform existed.

The introduction of the Social Market Economy is a rare case of "theory-in-action". The long-lasting economic policy discourse, since the early 1930s in Freiburg in the ordo-liberal school, later in the war years in various circles of economists and oppositional foreseeing the end of National Socialism, gave the Social Market Economy a strong theoretical foundation. The collaboration of two extraordinary economists with practical experience and of widely respected advisors was instrumental in implementing the concept against many odds – it is important, not to forget, that the Erhard reforms were indeed not very popular in the beginning. It also has to be mentioned that blueprint, as developed by the Freiburg school and related economists, and actual economic system, from the beginning were not identical, though over time differences dramatically increased. The window of opportunity to start again and differently after the war, the "Stunde Null" as *tabula rasa* was the

[6] See Olson's Logic of Collective Action (Olson 1965).

suitable time for a fundamental economic policy shift not possible under the pressure of interest groups in established economies.

The German Social Market Economy as an economic system derived from the ideas of ordo-liberalism proved to be remarkably robust; the alterations made in the German political process in the last six decades might have led to sclerotization in the Olsonian sense, but still the basic elements of the German economic system can withstand scrutiny. Indeed, after 1989 there was a renaissance of market economic thought throughout the world, and the German Social Market Economy became a model character again in many Central and Eastern European states. Ordo-liberalism, with its stress on the interdependence of order, proved to be a more comprehensive answer to the challenge of transformation than the neo-classical, more mechanical so-called “Washington Consensus” of policy reform, with the disregard for institutional change and its features.

The German economic growth performance after 1948 had many “fathers”, not only Erhard, the “father of the economic miracle”, like every successful model. But, while macroeconomic explanations are important to understand the growth dynamics after the war, they cannot explain the superior performance as well compared to European neighbouring market economies or to centrally-planned economies with a similar war experience. This is particularly true for the first ten years of the Social Market Economy, when the economic dynamic was markedly different. However, if Germany indeed had a superior performance, does that mean that growth is dependent on an ordo-liberal model? The next section shows that this is not necessarily the case.

3. The Japanese and East Asian Growth Experience - tigers, little tigers and paper tigers

East Asia's growth model has often been described as a distinctly non-market model of rapid growth and catching-up. This is as well true for Japan, the first nation experiencing high growth rates, as for the waves of “tiger economies”, “small tigers” and the second wave of former communist economies transforming, like Vietnam and especially China. However, it should be noted that not all economies grouped in this category had the same impressive growth performance. While Korea realized the worldwide highest growth rates from the 1960s through 1980s, the Philippines, once the second-richest economy in East Asia behind Japan, registered much less

impressive growth rates. Differences are especially marked for per-capita-GDP, since some countries like Japan and Korea underwent the same dramatic demographic transition than Western countries, with much high life expectancy and much lower birth rates changing the population pyramid, while in other countries per-capita-growth was “eaten up” by relatively higher birth rates.

The Japanese Economic Miracle denotes the rise of Japan from the ashes of World War II to become one of the most modern economies worldwide in the span of four decades. The “East Asian miracle”, popularized by a World Bank report accordingly named (World Bank 1993), is the subsequent rapid economic growth of “tiger states” (South Korea, Taiwan Hong Kong, Singapore) and “small tigers” (Malaysia, Indonesia, Philippines, Thailand). Though here an extensive discussion of their growth performance is not possible, it is important to see that the discussion about their growth performance has similar traits like that of the German Social Market Economy.[7]

[7] For a more extensive discussion see Seliger (2009) in the first volume of this series.

•	The miracle as an accumulation boom
•	The miracle as a result of superior bureaucratic planning
•	The miracle and the American influence
•	The miracle and the role of personalities
•	The miracle as currency-based mercantilism
•	The miracle as a political ex-post rationalization
	versus
•	ordo-liberal explanations (institutions, their implementation, and the rise and decline of nations)

Table 2: Competing explanations for East Asia's Economic Miracle

Japan was the first outlier in East Asian economic growth. Already in the 19th century Japan was most successful among Asian countries in adapting modern Western technology and administration during the Meiji Restauration. The rise of Japan to become the dominating power in East Asia was abruptly stopped with its defeat in World War II. Industry and basic infrastructure was widely destroyed, the territorial acquisitions after 1894 were separated from Japan and the United States governed the country through the Supreme Command of the Allied Powers (SCAP). Millions of ethnic Japanese settling formerly in the colonies had to be reintegrated. The powerful prewar industry conglomerates, the *zaibatsu*, were dissolved as part of the Japanese war machine. Inflation, unemployment and shortages threatened the stability of Japan. However, after SCAP backed the recovery of the economy and in particular with the onset of the Korean War Japan's economy began to grow at a rapid pace. Industrial production increased by 36,8 percent in 1951 alone. Overall, in the period of 1950 to 1973, the Japanese economy expanded by almost 10 percent a year. In the 1970s, it still grew by an average 5 percent a year and in the 1980s by 4 percent a year. Among the characteristics of the Japanese postwar economy were the strong influence of industrial planning by the state, in particular by the Ministry of International Trade and Industry (MITI), the re-emergence of dominant business

groups, *keiretsu*, with strong horizontal and vertical integration and house banks catering for the needs of industry, a labor market with enterprise unions closely interested in the fate of their companies, lifetime employment, and the rapid adaptation of technology. In the period from 1950 to 1973 the strong contribution of factor productivity to growth was particularly remarkable (Valdés 2003, p. 69, table 1).

Explanations for the Japanese economic miracle have always been competing: In the 1950s and 1960s Japan was seen as a successful model of modernization due to US-led economic and political reform, massive inflow of American aid and low defense spending due to the alliance with the US (Allen 1958, Forsberg 2000). Japanese economists challenged this view and referred to the modernization success in the 19th century and hence, the cultural roots of Japan's economic miracle (Hein 1996,). A key factor of growth was the export orientation of Japan's industry, which at the same time was protected by selective liberalization, allowing the free importation of inputs and intermediate goods, but closing the market for consumer goods of foreign countries. The low entry rate of the yen into the international monetary system, which until 1973 was a system of fixed exchange rates (Bretton woods) helped Japan to accumulate large trade surpluses. International economic integration into the GATT (1963), IMF and OECD (1964), where Japan soon became a major player, aided the internationalization of Japan's economy. In particular Chalmers Johnson (1982) stressed the role of the MITI and sparked a debate about Japan's success as a developmental state. Others were skeptical on the almost mythical power of foresight attributed to industrial policy of the MITI (Okimoto 1989). Mancur Olson (1982) saw the destruction of powerful distributional coalitions at the heart of the growth success of Japan in the post-war period, a record, which is consistent with the later decline of growth rates.

While the Japanese economic miracle had enormous impact on its East and Southeast Asian neighbors, as well through direct investment (the so-called flying geese model, Ozawa 2005) and as a model of development, in the 1980s the initial virtuous circle of accumulation, in which cheap credit by banks played an important role, became a vicious circle of debts for companies too big to fail and the prolonged existence of these so-called *zombie* companies, leading to two lost decades for Japanese growth in the 1990s and 2000s and greatly diminishing the appeal of the Japanese economic model.

The discussion of East Asia's miracle began in earnest, when the aforementioned World Bank report of 1993 was published. It tried to summarize as successful features of East Asia's different national economic policies the fact that most countries "got the basics right", i.e. created an environment where the growth of private investment and investment in human capital succeeded. This included a relatively low degree of inequality, high productivity growth in agriculture, relatively efficient (corruption-free) public administrations and market-enhancing instead of market-distorting interventions (like export goals plus a certain measure of protectionism for home markets instead of simply import substitution). It also included crucially macroeconomic stability, investment in human capital, in particular primary and secondary education, a functioning price system, a stable, though not necessarily market-oriented financial sector and selective instead of massive interventions, like selective credit allocation or export promotion. Market failure through asymmetric information in the financial sector and underdevelopment of the banking sector was, according to the report, overcome by special measures like long-term financial allocation by the state and the foundation of specialized public industrial banks (Japan, Korea, Taiwan, Indonesia). Overall, states were open for foreign technology, though FDI policy was not uniform.

This view was challenged by Krugman with this 1994 article "The Myth of Asia's Miracle", in which he put quantitative growth into the foreground and compared East Asia's growth performance to the rapid growth of the Soviet Union and its satellites since the 1950s through forced savings and expanded use of capital and, in particular, labour. This growth, Krugman predicted, would end. Though, certainly, expansion of inputs did play a role in East Asia's growth, it took a very different form than that of the socialist states, a factor not duly stressed by Krugman.[8] The idea of a miracle based on "perspiration instead of inspiration" was certainly catchy, however, critics asserted that it did not see the rapid assimilation of technologies, also those incorporated in the increased use of capital, for example in new machines, as for example Nelson and Pack (1999) argued.

In particular in the case of Korea and Taiwan, American influence and American aid have been stressed as factors explaining rapid catching-up. However, this is

[8] For example, the Soviet Union tried to expand labour input by harvest campaigns for high school and university students. East Asian countries, on the other hand, reduced the use of young labour by increasing enrollment in schools.

misleading on various accounts. Though US aid was important for Korea in the 1950s, its growth “miracle” began when aid was less important, in the 1960s, and aid declined subsequently in importance, while growth rates climbed. Also in terms of the economic system, American influence played certainly a role after World War II, it was quite limited by domestic political factors.

Personalities played an important role in various countries, like the legendary Lee Kuan Yew (prime minister from 1959 to 1990) in Singapore or Park Chung-Hee (president from 1962 to 1979) in Korea. Often ruling authoritarian regimes and disregarding human rights, they are remembered mostly for their dedication to growth and development. The idea of the “developmental dictatorship” originates in such personalities. However, first of all not all successful East Asian countries did have charismatic leaders, for example Japan, and second these persons might have been instrumental in implementing a certain economic order, but their activities are not to be judged independently from that order. Related to the role of personalities is the ex-post rationalization of miracles. This is certainly true to some extent in the memoirs of Lee (1999) in a time when the East Asian crisis of 1997 and 1998 required a reassertion. But it does not at all explain the indeed stellar growth performance of several East Asian countries. The idea of “tigers and small tigers” (or, in East Asia itself, dragons and small dragons) is another form of ex-post rationalization, though in particular some small tigers were rather paper tigers.

Like in the case of Germany's economic miracle, East Asia's miracle has been explained as currency-based as well as trade-based mercantilism. While this is mechanically true – growth in East Asian countries for a long time was more dependent on the external contribution of high trade surpluses than of domestic demand, compared for example with the United States, it does not explain why these states were so successful in developing a functioning export sector, while many other states failed to do so. Currency undervaluation, often cited for China, was not a problem in most other East Asian countries, where pegged exchange rates plus more or less high inflation differentials to the US-dollar meant a tendency for over-valuation, which only in the East Asian crisis was erased.

Certainly, it is much more difficult to put a number of very different country cases together as in this section compared to the section above. In some countries, growth was visibly hampered by authoritarian (non-development) states, like in Indonesia or

Burma, in other states growth declined with political unrest, like in Thailand and the Philippines. Economic policy differences were large: for example, Singapore and Hong Kong based their growth on the inflow of foreign investment, while Japan and Korea were long-time closed. Can their be a common denominator for the East Asian growth experience, and can that even be a shared denominator with the case of Germany? This will be discussed in the next section.

4. Commonalities and differences in economic miracles institutions, institutional competition and culture

On the surface, Germany and East Asia are totally opposed cases. It is true that Germany in the 1950s was much less open in some respects, e.g. in trade policy or the financial sector, than today taken for granted, and that in East Asia economic freedom was much larger than sometimes assumed by proponents of the explanation of growth as the result of powerful bureaucratic planning – even authoritarian states were much less controllable than centrally-planned economies. Moreover, they are cases represent cases of Olsonian destruction of distributive coalitions, in Germany, Japan and Korea through the war and post-war period, in other states through the rise of authoritarian governments. But this covers only one aspect of their growth experience. Economic policies with regards to a number of fields were quite distinct: some countries based their growth on a thriving SME sector, like Germany and Taiwan, some on large conglomerates like the Japanese *keiretsu* and the Korean *chaebol*. Competition policy played a much more important role in Germany than in most East Asian states. Trade policies were very different, with Germany integrated in a common market in Europe and Asian countries wary of trade integration until the last two decades.

Despite these differences, there is a commonality, not in the form of economic institutions, but in the fact that economic institutions seem to have allowed the long-term accumulation of private investment and human capital. Dubbed “constancy of economic policy” in Walter Eucken's seminal work on economic policy, one can also describe this as an accepted growth model based on a stable institutional (expectations)- equilibrium, leading to an overall fulfillment of expectations and allowing for long-term orientation of policies and private plans.

Among the most important elements of an economic system necessary to be analyzed are the formal and informal institutions.[9] Formal institutions are determined on the "market of institutions" of a country, which is a metaphor for the interaction of the market for politics with the markets for goods and services as well as factor markets. The market for politics includes on the supply side political entrepreneurs and the bureaucracy, supplying certain policies. The demand side includes (as sometimes overlapping groups) consumers, tax payers, workers and investors, which choose by voice in democracies (elections and demonstrations, political debate), as well as by exit options (like migration and capital flight). The exit option relates the market for politics with the markets for goods and services. Interest groups take a mediating position between supply and demand side, being characterized by asymmetrical information vis-à-vis both groups. Institutional alternatives become clear through exit and voice, i.e. institutional competition. The intensity of institutional competition is depending on international as well as national regimes, for example of trade. Globalization increased the intensity of institutional competition dramatically.

Informal institutions together with the formal institutions determine the economic system. They are central to understand the performance of formal institutions. They are not static, but their change is piecemeal and slow. This is an important reason for the different results of the same formal institutions in different regions. The effectiveness of informal institutions, which are not enforced by the state monopoly for power, is depending on the perception of market actors about their legitimacy. Therefore, another factor for economic change and stability of an economic system becomes important, namely the perceptions, the actors have about its functioning. Since market actors (as well as external observers) have no complete information, they formulate hypotheses about the functioning of the economic system, which determine their choice of goals and instruments. These hypotheses are again depending on cognitive schemata, which help the actors to reduce uncertainty in the face of incomplete information. When hypotheses are permanently frustrated, new hypotheses will be build. However, this does not automatically lead to a different acting: As long as the enforcement mechanism for informal institutions works, opportunistic behaviour can prevail.

---

[9] While the definition of both is not universal, mostly they are distinguished by their enforcement mechanism (state monopoly in the case of formal, private, decentralized enforcement by social norms, customs or other arrangements in the case of informal institutions).

However, this also means that relatively small changes in the perception of institutions can have large effects, if a critical mass for institutional change is reached, like in the transformation processes in formerly socialist states.

To understand the change of economic systems, first the relevant market for formal institutions has to be analyzed. This market is on the one side embedded into the context of international institutional competition, on the other side related to informal institutions in a functional relation. An equilibrium of expectations in an economy can be defined as the state, when *grosso modo* the expectations of actors about the functioning of institutions are not frustrated. These expectations again are depending on cognitive schemata of actors about these institutions.

These schemata, which are dependent on self-perception and the perception of others, are until now barely analyzed.

The equilibrium of expectations should not be confounded with a normatively optimal state of the economy. Stable expectations also can exist in face of dictatorship and economic decline, but permanent macroeconomic imbalances or crises will one day also lead to a crisis of the economic model.[10] The crisis of the model leads to transformation, which has again two aspects, namely the intended consequences initiated for example by the state to transform the economic system and the often more important unintended consequences[11]. The unintended consequences are for example depending on the relation of formal and informal institutions or on the perception of human actors of the changed institutions. Looking at the change of economic systems from such a point of view also allows to draw normative conclusions concerning the adaptive efficiency of an economic system.

Figure 1 includes the different aspects discussed above in a framework for the analysis of institutional analysis for the case of post-war West Germany.[12] For the international context, in particular the original limited sovereignty after World War II, later the increasing importance of European integration, for example in shaping competition policy, are important.

---

[10] Economic model not understood in the sense of a Weberian ideal type, but as the model, the actors have of an economy.

[11] Cf. Hayek (1969). The analysis of unintended consequences of human action is for Hayek the foremost aim of social science, cf. Hayek (1979), p. 41.

[12] The model framework has first been introduced in Seliger (2004).

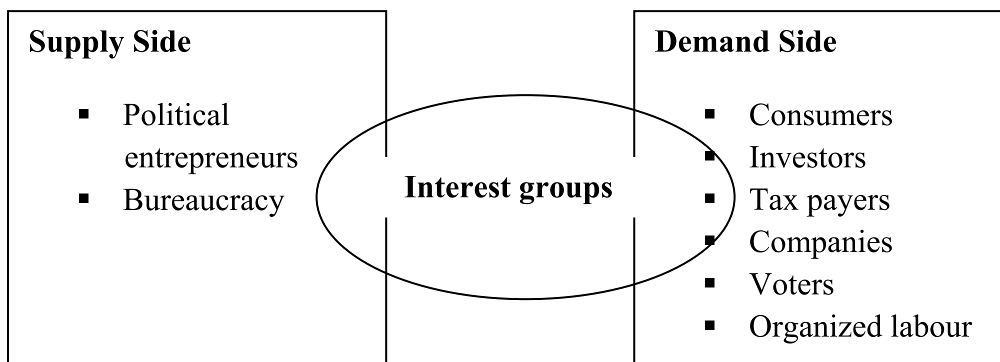
The market for politics is characterized, among others, by a large and successful modern conservative party, CDU/ CSU, as the main carrier of economic reform. Interest groups, though always existing, exerted limited influence in the immediate post-war situation and only slowly regained power to add asymmetric regulatory burdens to the economy. Among the informal institutions, a certain post-war concentration on economic success as a compensation for lost political aspirations after the war might be as important as the existing working ethics. Perceptions of Germany's economy then include the widely shared – domestic and abroad – idea of a “miracle” and a personalization in the “father of the economic miracle”, Ludwig Erhard. The cultural context includes the traumatic war experience, leading to consumerism and wariness of political exposure of Germany after the lost war, the traumatic inflation experience of 1923 and 1945-1947, leading to a strong preference for stability, monetary and otherwise, and standard of justice and fairness, leading to the acceptance of competition and markets, but only under the umbrella of a Social Market Economy.

International context: Institutional competition and institutional constraints

here: role of occupying forces, competition of economic models and competition for investment; European integration as a an increasingly important paradigm of foreign economic policy

---

Formal institutions: "market for institutions"



Informal Institutions

Perception of institutions (self perception; perception of others);

"the economic miracle"; "the father of the economic miracle, Ludwig Erhard"

Cultural context; cognitive models

Here especially: models of economic policy and the economy, standards of justice and fairness, traumatic war and inflation experience, "wir sind wieder wer" (we did it again) feeling in the 1950s

Figure 1: The institutional system of post-war Germany – a stylization

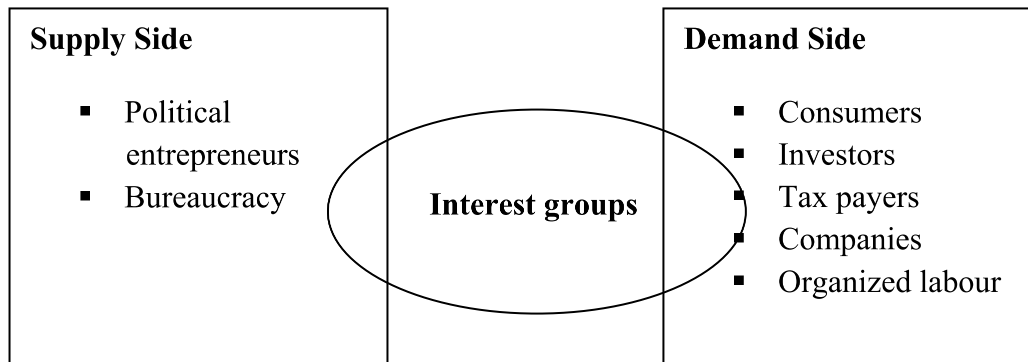
Also, for the case of East Asian catching-up, some commonalities can be included in a similar institutional model like in Figure 2. In the international context, peer pressure in East Asia has been an important factor for some states, in particular latecomers

like the “small tigers”. The role of American advisors was important in post-war Japan, in Taiwan and Korea. Competition of systems with communist neighbours was particularly strong again in Korea and Taiwan, but also played an important role in economic modernization in Southeast Asia. The formal institutions were often determined by authoritarian political systems, often with leaders of leading families, but with marked exceptions like Japan (formal democracy with a strong government party) or Hong Kong (colony with considerable internal autonomy). Voters were not really determining most of the East Asian political models, though they did play a role, as did labour unions in some countries. As for the informal institutions, those related to the dominant societal model, in many states a form of latter-days Confucianism, played an important role, with features like the seniority principle and a strong desire for formal education. The perception of “tiger states” had been accepted not only abroad, but also in the countries and thereby shaped behaviour, e.g. voting preferences or working ethics.

International context: Institutional competition and institutional constraints

here: peer pressure and American advisors; competition of economic systems with communist neighbours

Formal institutions: "market for institutions"



Informal Institutions

Perception of institutions (self perception; perception of others)

"tiger states" (or dragons), „*KORANDO*" (Koreans can do)[13]

Cultural context; cognitive models

Here especially: models of economic policy and the economy (developmental state), standards of justice and fairness, "Confucian" working and education ethics

Figure 2: The institutional system of East Asian development states – a stylization

[13] Korando is the name of one of the first Korean SUV. It is reportedly a contraction of "Koreans can do" and denotes the belief that Korean companies can be successful in all markets.

5. Conclusion – towards a theory of economic miracles?

The discussion of economic miracles above shows that the economic institutions leading to miraculous results were quite different. *Kairos*, the window of opportunity, played an important role, as did long-run informal institutions embedded in certain cultural and institutional backgrounds. At the same time, there seem to be factors precluding miracles, including macroeconomic instability caused by economic policy decisions as microeconomic factors like failed planning approaches. If this institutional model can help to identify features of successful economic systems leading to high growth rates, it begs the question, if a premeditated adaption of institutional systems is possible. The relevancy of this question is clear, but the answer is far from obvious. While indeed there have been cases of successful institutional imitation, they are often limited to similar circumstances in terms of cultural embeddedness, international context and pre-existing institutional system.[14]

The above-sketched institutional model of an expectations-equilibrium as the outcome of the interaction of the formal institutions, determined through the interaction of the market for politics with economic decisions, and informal institutions, and shaped by the international context as well as the cultural context, does not claim to be comprehensive to understand institutional systems, and even less, growth performance.

But it can show the importance of certain institutional factors for growth performance, which have to be included into the analysis of the relative success of economic systems. By that, it can add to the discussion of economic performance as the result of economic institutions in the sense of North (1990) and draw important lessons for development processes.

[14] For example, it has been noted that the Baltic states with a certain experience of market economies and democracies had a head start in transformation compared to other former Soviet states.

References

Allen, George C. (1958). *Japan's Economic Recovery*, Oxford: Oxford University Press.

Forsberg, Aaron (2000). *America and the Japanese Miracle,* Chapel Hill, NC: University of North Carolina Press, 2000.

Giersch, Herbert – Karl-Heinz Paqué - Holger Schmieding (1992). *The Fading Miracle: Four Decades of Market Economy in Germany*. Cambridge: Cambridge University Press.

Hayek, F.A.v. (1969). “Die Ergebnisse menschlichen Handelns, aber nicht menschlichen Entwurfs,” in: idem, *Freiburger Studien*, Tübingen: Mohr, pp. 97-107.

Hayek, F.A. (1979). *The Counter-Revolution of Science, Studies on the Abuse of Reason* (1952), 2nd ed., Indianapolis: Liberty Fund.

Hein, Laura (1996). “Free-Floating Anxieties on the Pacific: Japan and the West Revisited”, *Diplomatic History* (1996), vol. 20, no. 3, pp. 411-437.

Horstmann, Theo (1985). „Um das „schlechteste Bankensystem der Welt“. Die interallierten Auseinandersetzungen über amerikanische Pläne zur Reform des deutschen Bankwesens 1945/46,” *Bankhistorisches Archiv II*, pp. 3-27.

Johnson, Chalmers (1982). *MITI and the Japanese Miracle: The Growth of Industrial Policy*, 1925-1975. Stanford, CA: Stanford University Press.

Krugman, Paul (1994), “The Myth of Asia´s Miracle. A cautionary Fable,” *Foreign Affairs*, Vol. 73, no. 6, pp. 62-78.

Landes, David S. (1999). Wohlstand und Armut der Nationen,

Berlin: Siedler Verlag.

Lee, Kuan Yew (1999). *The Singapore Story: Memoirs of Lee Kuan Yew*, Singapore: Prentice Hall.

Maddison, Angus. (1991). *Dynamic Forces in Capitalist Development – A Long-Run Comparative View*, Oxford: Oxford University Press.

Nelson, Richard R. - Howard Pack (1999). “The Asian Miracle and Modern Growth Theory,” *The Economic Journal*, Vol. 109,

No. 457 (July), pp. 416-436.

North, Douglass C. (1990). In*stitutions, Institutional Change and Economic Performance*, Cambridge: Cambridge University Press.

Okimoto, Daniel I. (1989). *Between MITI and the Market: Japanese Industrial Policy for High Technology*, Stanford, CA: Stanford University Press.

Olson, Mancur (1982). *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities*, New Haven CT: Yale University Press.

Olson, Mancur (1965). *The Logic of Collective Action*, Cambridge, Mass.: Harvard University Press.

Ozawa, Terutoma (2005). *Institutions, Industrial Upgrading, and Economic Performance in Japan – The 'Flying-Geese Paradigm of Catch-up Growth*. Northampton, Massachusetts: Edward Elgar Publishing.

Reichel, Richard (2002). "Germany's Postwar Growth: Economic Miracle or Reconstruction Boom?," *Cato Journal*, Vol. 21, no. 3 (winter),

pp. 427-442.

Seliger, Bernhard (2009). "Die zweite Welle: ordnungspolitische Herausforderungen der ostasiatischen Wirtschaftsentwicklung," in: Seliger, Bernhard – Jüri Sepp – Ralph M. Wrobel (eds.), *Das Konzept der sozialen Marktwirtschaft und seine Anwendung, Deutschland im inernationalen Vergleich,* Wien: Peter Lang, pp. 259-288.

Seliger, Bernhard (2004). "Area Studies and Social Science – from uneasy coexistence to integration?," *Korean Review of International Area Studies*, Vol. 3, August 2004, pp. 3-43.

Spicka, Mark E. (2007). *Selling The Economic Miracle: Economic Reconstruction And Politics In West Germany, 1949-1957*, Oxford: Berghahn.

Valdés, Benigno (2003). "An Application of Convergence Theory to Japan's Post-WWII Economic "Miracle", *Journal of Economic Education*, vol. 34, no. 1, pp. 61-81.

Van Hook, James C. (2004). Rebuilding Germany. The creation of the Social Market Economy, 1945-1957, Cambridge: Cambridge University Press.

World Bank (ed.) (1993), *The East Asian Miracle – Economic Growth and Public Policy*, Oxford: Oxford University Press.

Ordnungspolitische Diskurse

Discourses in Social Market Economy

2007 – 1 Seliger, Bernhard; Wrobel, Ralph – Die Krise der Ordnungspolitik als Kommunikationskrise

2007 – 2 Sepp, Jüri - Estland – eine ordnungspolitische Erfolgsgeschichte?

2007 – 3 Eerma, Diana; Sepp, Jüri - Competition Policy's Role in Network Industries - Regula-tion and Deregulation in Estonia

2007 – 4 Claphman, Ronald - Welche Bedeutung haben nationale Wirtschaftsordnungen für die Zukunft der EU? Der Beitrag der sozialen Marktwirtschaft

2007 – 5 Strunz, Herbert – Staat, Wirtschaften und Governance

2007 – 6 Jang Tae-Seok - South Korea's Aid to North Korea's Transformation Process - Social Market Perspective

2007 – 7 Libman, Alexander - Big Business and Quality of Institutions in the Post-Soviet Space: Spatial Aspects

2007 – 8 Mulaj, Isa - Forgotten Status of Many: Kosovo's Economy under the UN and the EU Administration

2007 – 9 Dathe, Uwe - Wettbewerb ohne Wettbewerb? Über die Bedeutung von Reformen im Bildungswesen für die Akzeptanz der Wettbewerbsidee

2007 – 10 Noltze, Karl - Die ordnungspolitische Strategie des Landes Sachsen

2008 – 1 Seliger, Bernhard - Die zweite Welle – ordnungspolitische Herausforderungen der ostasiatischen Wirtschaftsentwicklung

2008 – 2 Gemper, Bodo Rheinische Wegbereiter der Sozialen Marktwirtschaft: Charakter zeigen im Aufbruch

2008 – 3 Decouard, Emmanuel - Das „Modèle rhénan“ aus französischer Sicht

2008 – 4 Backhaus, Jürgen - Gilt das Coase Theorem auch in den neuen Ländern?

2008 – 5 Ahrens, Joachim - Transition towards a Social Market Economy? Limits and Opportunities

2008 – 6 Wrobel, Ralph - Sonderwirtschaftszonen im internationalen Wettbewerb der Wirt-schaftssysteme: ordnungspolitisches Konstrukt oder Motor institutionellen Wandels?

2009 – 1	Wrobel, Ralph - The Double Challenge of Transformation and Integration: German Experiences and Consequences for Korea
2009 – 2	Eerma Diana; Sepp, Jüri - Estonia in Transition under the Restrictions of European Institutional Competition
2009 – 3	Backhaus, Jürgen - Realwirtschaft und Liquidität
2009 – 4	Connolly, Richard - Economic Structure and Social Order Type in Post-Communist Europe
2009 – 5	Dathe, Uwe – Wie wird man ein Liberaler? Die Genese der Idee des Leistungswettbewerbs bei Walter Eucken und Alexander Rüstow
2009 – 6	Fichert, Frank - Verkehrspolitik in der Sozialen Marktwirtschaft
2009 – 7	Kettner, Anja; Rebien, Martina – Job Safety first? Zur Veränderung der Konzessionsbereitschaft von arbeitslosen Bewerbern und Beschäftigten aus betrieblicher Perspektive
2009 – 8	Mulaj, Isa – Self-management Socialism Compared to Social Market Economy in Transition: Are there Convergent Paths?
2009 – 9	Kochskämper, Susanna - Herausforderungen für die nationale Gesundheitspolitik im Europäischen Integrationsprozess
2009 – 10	Schäfer, Wolf – Dienstleistungsökonomie in Europa: eine ordnungspolitische Analyse
2009 – 11	Sepp, Jüri – Europäische Wirtschaftssysteme durch das Prisma der Branchenstruktur und die Position der Transformationsländer
2009 – 12	Ahrens, Joachim – The politico-institutional foundation of economic transition in Central Asia: Lessons from China
2009 – 13	Pitsoulis, Athanassios; Siebel, Jens Peter – Zur politischen Ökonomie von Defiziten und Kapitalsteuerwettbewerb
2010 – 01	Seliger, Bernhard – Theories of economic miracles

Herausgeber:

PD Dr. habil. Bernhard Seliger – Seoul
Prof. Dr. Ralph M. Wrobel – Zwickau

www.Ordnungspolitisches-Portal.de