

# **Theories of economic miracles**

**Dr. habil Bernhard Seliger,**

**Universität Witten/ Herdecke**

**Hanns-Seidel-Stiftung Korea**

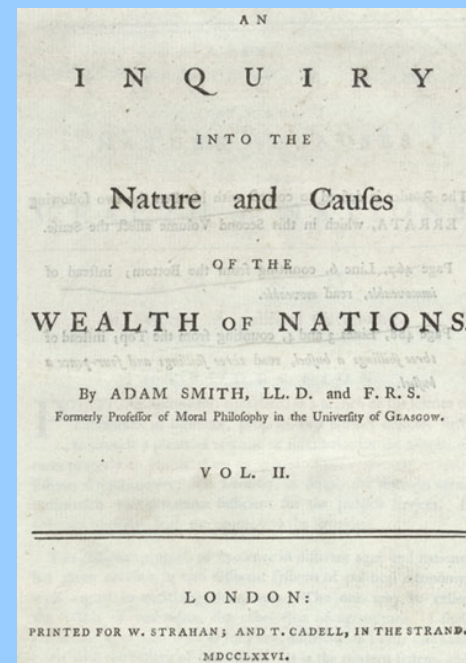
**2. Ordnungspolitischer Dialog, Westsächsische  
Hochschule Zwickau, 20.-21. November 2008**

## **Economic miracles seem to happen quite often...**

- Europe, Asia, Korea, Japan, Germany, Taiwan, India, Netherlands, Botswana, Estonia, Irland, China, Argentinien, Chile, Malaysia, Spain, Dubai, UK, Vietnam

# The question

- Do these cases have anything “miraculous” in common?



# Content

## I. The German economic miracle

- Overview
- Competing explanations
- The ordo-liberal view

## II. The East Asian miracle

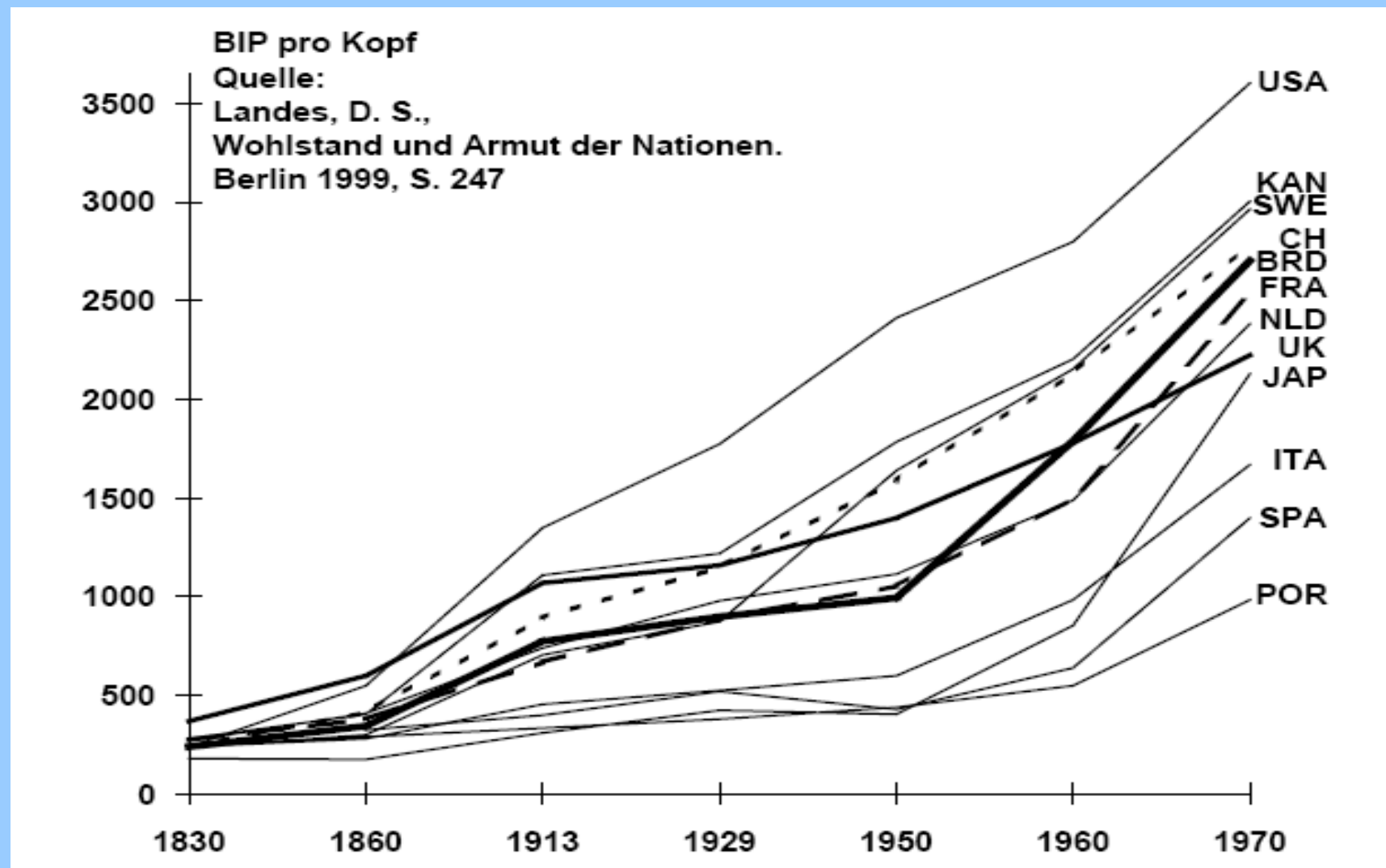
- Overview
- competing explanations

## III. Are there commonalities?

# The German Economic Miracle



impressive... but not unique



# **The experience of National Socialism (1933-1945)**

- Since 19th century concentration of economic power
- Cartels are legally binding (1897 Reichsgericht)
- IG Farben, Vereinigte Stahlwerke (chemical, steel industry)
- Concentration of political power (in Prussia, in Weimar Republic, peak during National Socialist phase)
- Centralization
- totalitarianism

# **Competing explanations for the German miracle**

- 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



# **The miracle as a reconstruction boom**









# **DIE ROTE ARMEE**

kommt als

## **HELPER**

Ihre Autos rollen und bringen uns

## **LEBENSMITTEL**

# **The miracle as a reconstruction boom**

- Neoclassical growth model (Solow)
- Destruction of capital stock leads to declining capital/labour ratio (below long-run equilibrium)
- Productivity of capital is increasing (higher productivity growth rates)
- Higher per-capita income, asymptotically approaching long-run growth path
- Conditional convergence (Sala-i-Martin 1996 for developing countries)

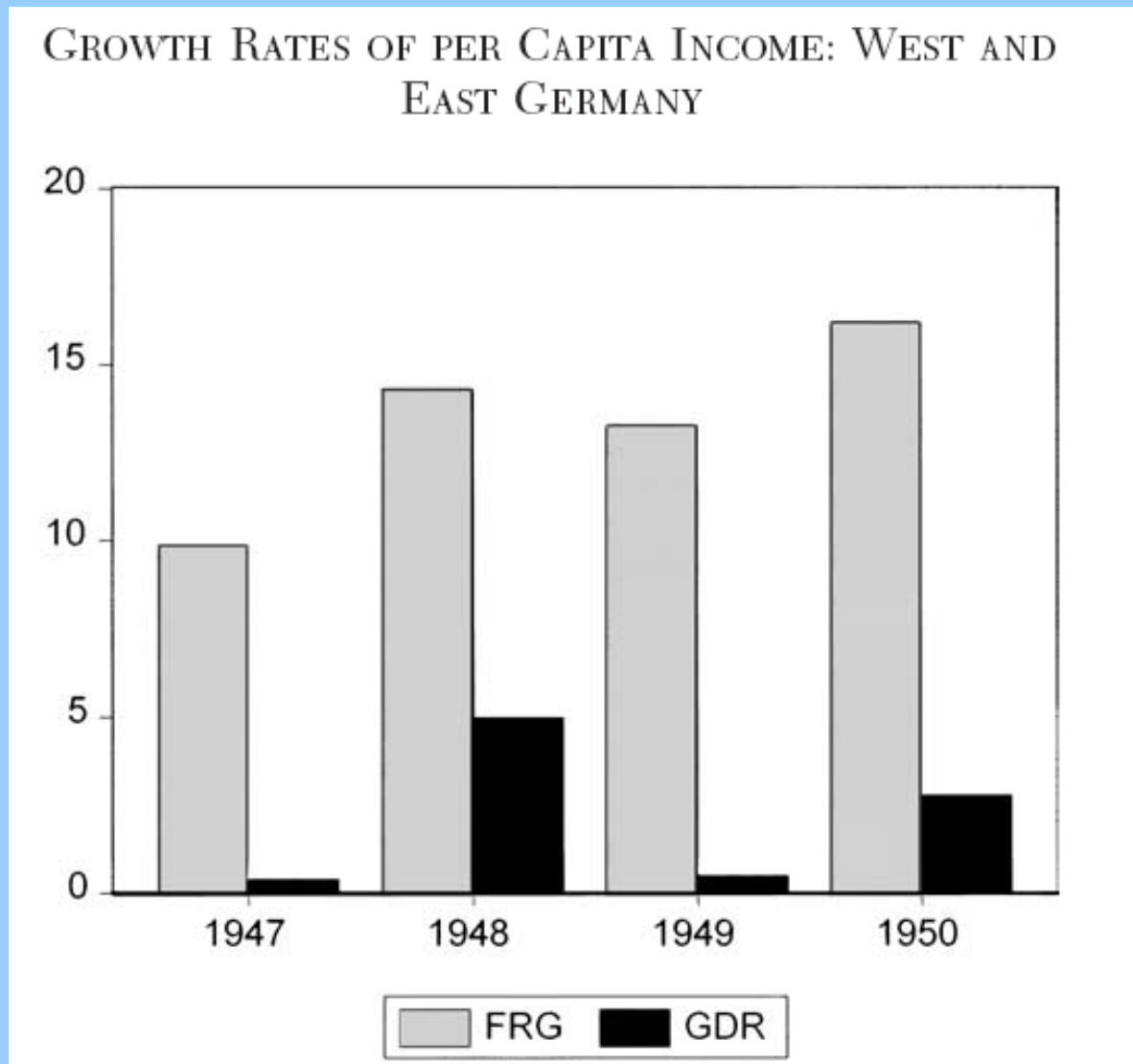
# When did the boom begin?

## GROWTH RATES OF PER CAPITA INCOME AND INDUSTRIAL PRODUCTION

Year	Per Capita Income (%)	Industrial Production (%)
1947	9.9	14.7
1948	14.3	53.8
1949	13.3	48.3
1950	16.2	25.7

SOURCE: Author's calculations based on *Wirtschaft und Statistik*, various issues.

# Why did East Germany grow so slowly?

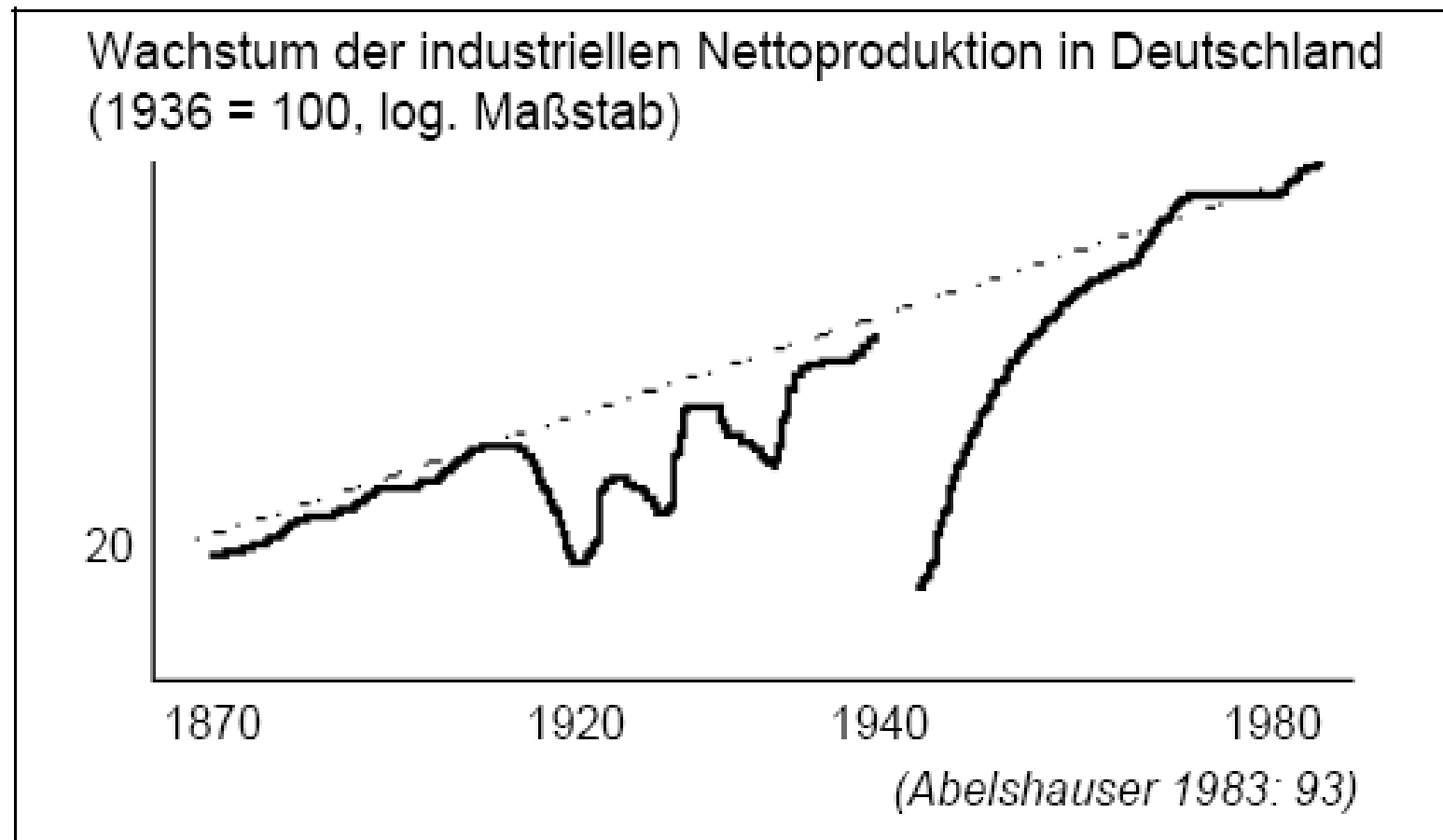




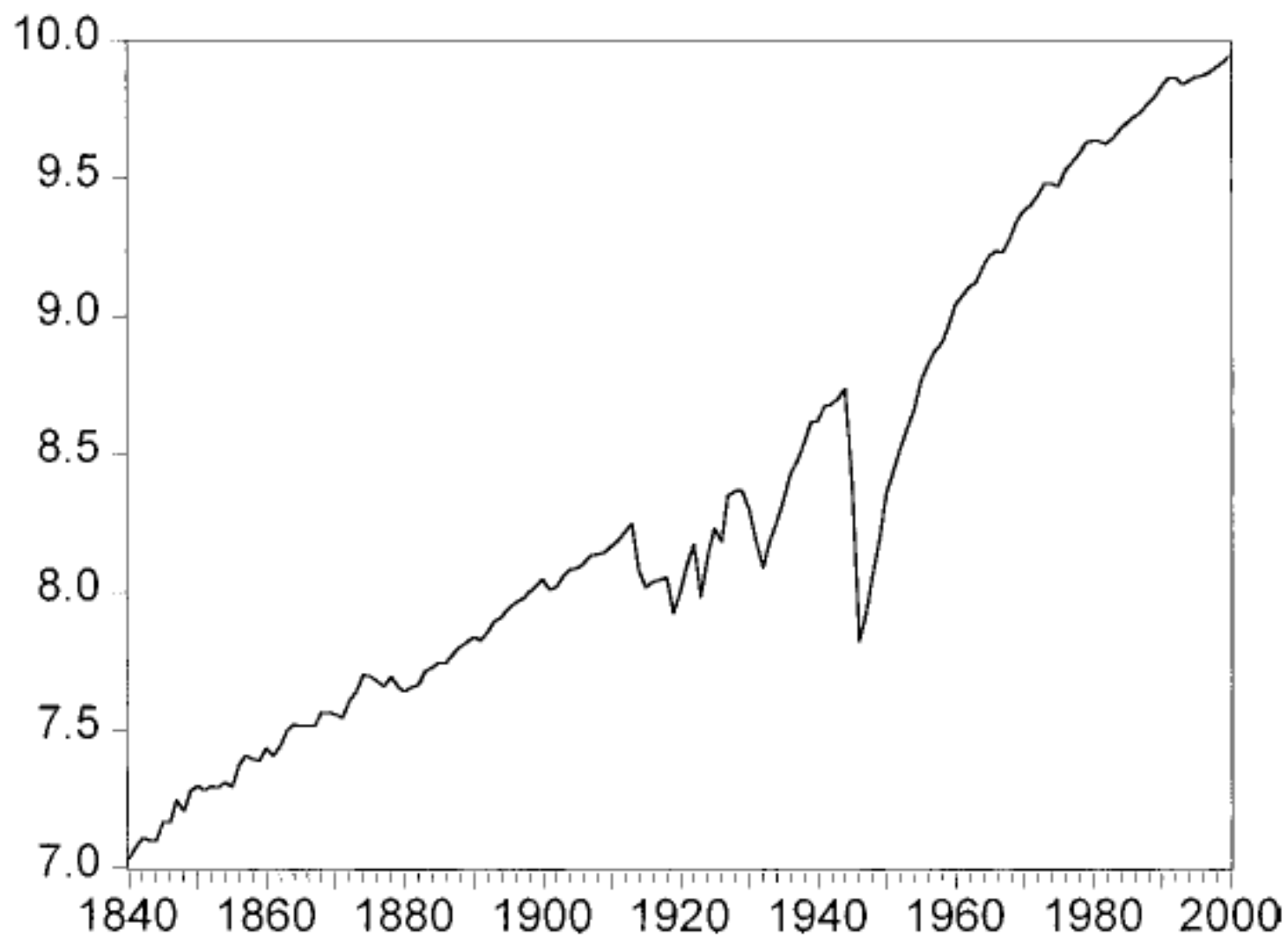
# **The miracle as return to pre-war growth path**

- Why did the per capita-income grow so fast?
- Return to pre-war growth path
- Full utilization of capacity
- Rapid capital formation
- Structural change
- Immigration of human capital (refugees)

# Industrial production in Germany



# GERMANY'S REAL PER CAPITA INCOME (CONSTANT LOGGED U.S.\$)



# The miracle and the American influence

- Political economy argument: currency reform and price liberalization impossible without decree by occupying authorities
- Spring 1948: Bank deutscher Laender (as attempt to weaken central structures in Germany)
- Growth (demand side) argument:
  - - the role of the Marshall plan (more symbolic than fundamental)
  - - Keynesian policies stimulate demand worldwide

# **The miracle and the role of personalities**

# „Wohlstand für Alle“ – Ludwig Erhard



# **The miracle and the role of personalities**

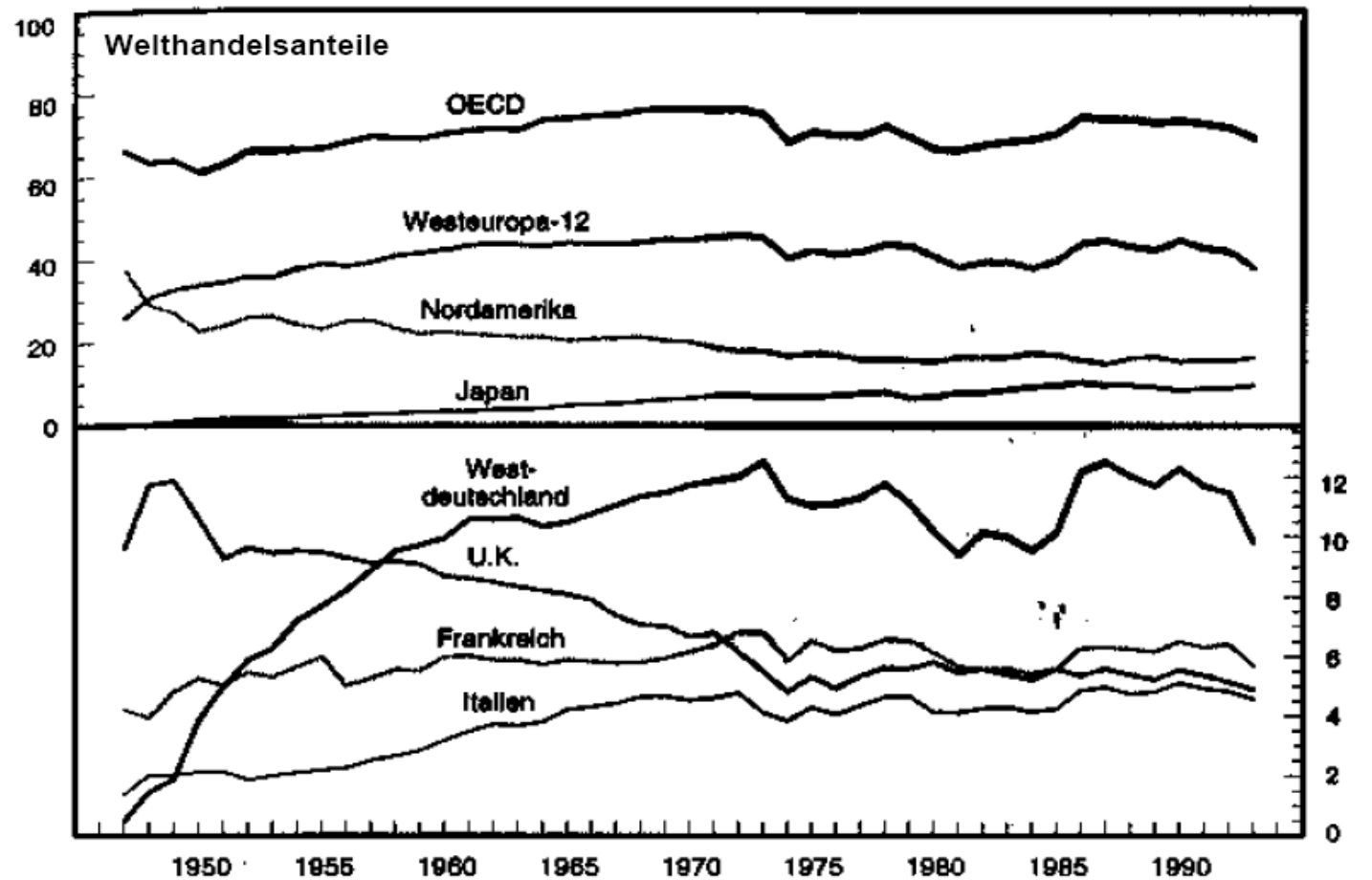
- Erhard born as son to textile trade in Nuremberg
- Lobbyist for SME and consumer industries
- Institut fuer Wirtschaftsbeobachtung der Deutschen Fertigindustrie (1928)
- In 3rd Reich against primacy of heavy industry since 1936
- Since 1941 in Berlin, contact to conservative (and classical liberal) opposition
- Müller-Armack textile sector

# **The miracle as currency-based mercantilism**

- Undervaluation in Bretton Woods system
- Domestic: hard currency (conflict in Korea war crisis was solved favoring reputation)
- Accumulation of foreign reserves (Germany changes from net debtor to net creditor); London debt deal; no reparations
- In crisis: import tariffs for certain goods increased



# Shares in world trade 1950-1995



Lindlar 1997: 247



# **The miracle as a political ex-post rationalization**

- Erhard: there is nothing miraculous in the miracle
- after Korea crisis „selling the miracle“
- CDU as modern, non-ideological party
- Institut für Demographie, Allensbach
- Die Waage (industrialists)
- Soziale Marktwirtschafts as a weasel word

# **Ordo-liberal factors in the economic miracle**

- The miracle and the role of monetary policy
- The miracle and the role of competition policy
- The miracle as a result of destruction of distributive coalitions
- The miracle as theory-in-action

# **The miracle and the role of monetary policy**





# The first day with the new Deutschmark – June 20, 1948





# **The miracle and the role of monetary policy**

- The experience of inflation in 1923 and after 1945
- Primacy of monetary policy
- (no functioning price system without stable prices)
- Deutschmark-Nationalism

# **The miracle and the role of competition policy**

- Freeing Germany from the influence of cartels
- Struggle for competition law (only 1957 in watered-down version)
- Erhard against exceptions (in particular, due to European integration), but in vain
- Independent cartel office remains weaker than central bank

# **The miracle as the result of the destruction of distributive coalitions**

- Mancur Olson
- Logic of Collective Action (1965)
- The rise and decline of nations (1982)
- Asymmetric rent-seeking
- Sclerotization of societies, economies
- English disease (1970s)
- German disease, Japanese disease (1990s)

# The miracle as theory-in-action

- Long-lasting economic policy discourse (since early 1930s in Freiburg)
- Strong convictions due to the war experience
- Two extraordinary economists with practical experience and widely respected advisors
- “Stunde Null” as *tabula rasa*, time for fundamental economic policy shift

# **The East Asian miracle – dragons and small dragons**

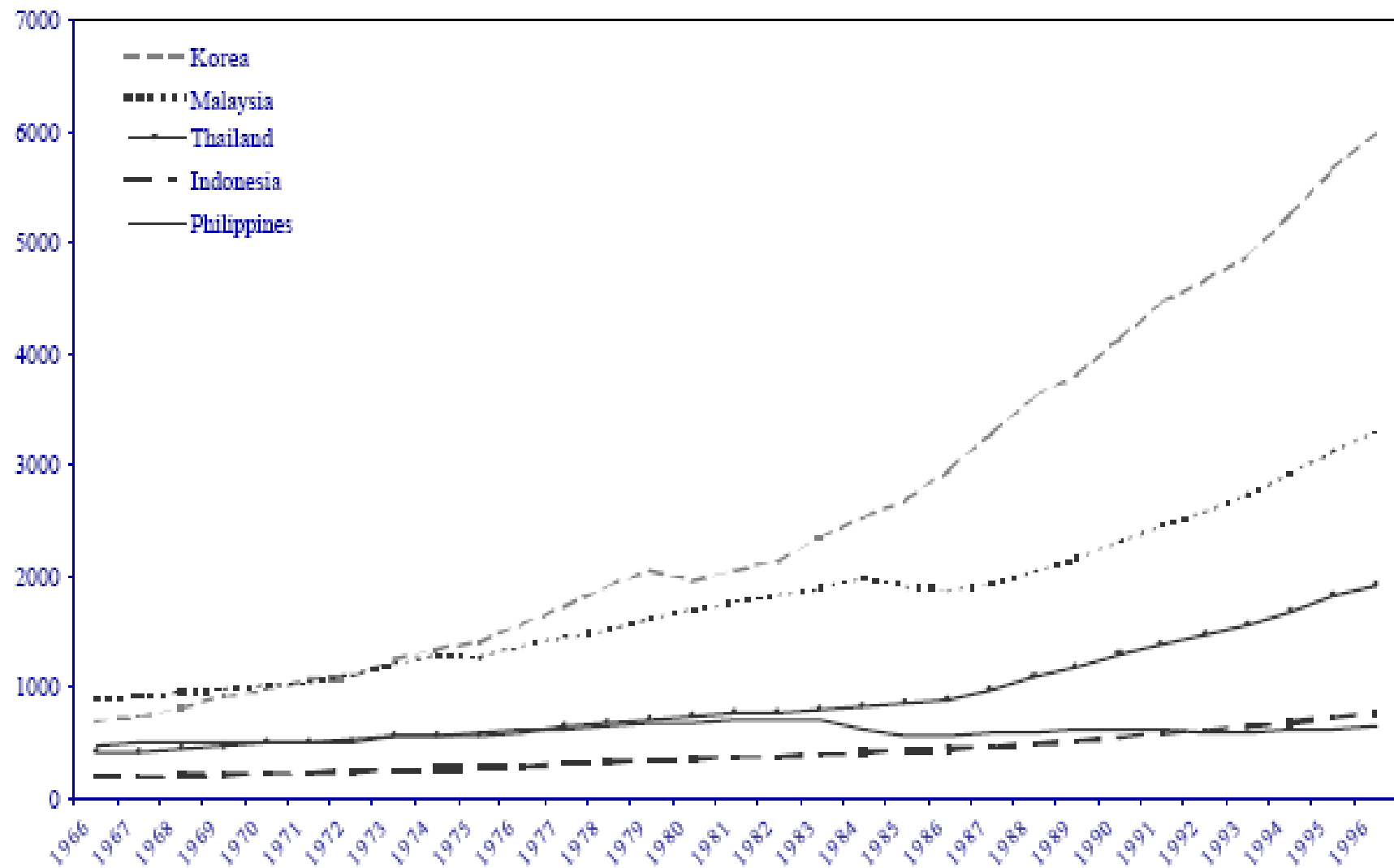
- East Asian dragons (亞洲四小龍): South Korea, Hong Kong, Singapore, Taiwan
- Small dragons: Malaysia, Thailand, Philippines, Indonesia
- Export orientation, selective liberalization, technology transfer from Japan (wild goose model), high savings rates, high degree of economic freedom
- Role of education (Confucianism), authoritarian governments



## East Asia



Figure 3: Evolution of GDP per Capita (Real US\$87), 1966-1996



Source: World Bank Development Indicators 1998, World Bank.

# **Competing explanation of the East Asian miracle (1)**

- Sound fundamentals and selective interventions (World Bank hypothesis)
- Mixture of market flexibility, regulation (e.g. in the labour market)
- Export orientation and “growth dictatorships” with neo-mercantilist practices
- Role of learning
- Explanations based on mixed economy approach and culture



# **Competing explanation of the East Asian miracle (2)**

- “Inspiration vs. perspiration” – the role of quantitative growth (Krugman hypothesis)
- Rapid assimilation of foreign technology (Nelson, Rodrick)
- Role of learning
- Explanations based on growth accounting and culture

Copyrighted Material

A WORLD BANK POLICY RESEARCH REPORT

The cover features a composite image. The upper portion shows terraced rice fields in a lush, green landscape with banana trees and palm trees. The lower portion shows a busy port city with numerous shipping containers, cranes, and large cargo ships docked at a pier. The title 'THE EAST ASIAN MIRACLE' is prominently displayed in the center in large, bold, dark blue capital letters. Below the title, the subtitle 'ECONOMIC GROWTH AND PUBLIC POLICY' is written in smaller, bold, white capital letters with a black outline. The entire cover is framed by a light blue border.

# THE EAST ASIAN MIRACLE

ECONOMIC GROWTH AND PUBLIC POLICY

Copyrighted Material

# **The World Bank hypothesis (1) – economic growth and public policy**

- „getting the basics right“: growth of private investment and human capital
- Low degree of inequality
- Productivity growth in agriculture
- Relatively efficient (corruption-free) public administration
- Market-enhancing interventions (like export goals)

# **The World Bank hypothesis (2) – sound fundamentals and selective intervention**

- Fundamentals: makro-economic stability, investment in human capital (schools), functioning price system, stable financial sector
- Selective interventions: industrial policy, selective credit allocation, export promotion
- Cost control of public investment (heavy industry in Korea, Malaysia)

# **The World Bank hypothesis (3) – overcoming market failure in the financial sector**

- asymmetric information and underdevelopment of the banking sector
- Allocation of long-term finance
- Specialized public industrial banks (Japan, Korea, Taiwan, Indonesia)
- Openness for foreign technology
- FDI policy not uniform

# Krugman hypothesis - Critique of the Asian growth model

- Krugman (1994): „*The Myth of Asia's Miracle*“ - quantitative growth automatically has to end
- Comparison with the high growth rates of the Soviet Union and the socialist states
- Partly convincing: no explanation of technological adaption, market-determined growth, limited role of the state, macro-economic stability
- What makes Asia so successful?

# Krugman on Singapore

## Perspiration vs. Inspiration?

- „Singapore grew through a **mobilization of resources** that would have done Stalin proud. [...] [A]ll of Singapore's growth can be explained by **increases in measured inputs**. There is **no sign at all of increased efficiency**.” “If there is a secret to Asian growth, it is simply deferred gratification, the willingness to sacrifice current satisfaction for future gain.”
- (Krugman 1994 , pp. 70-71)

# Growth and growth accounting

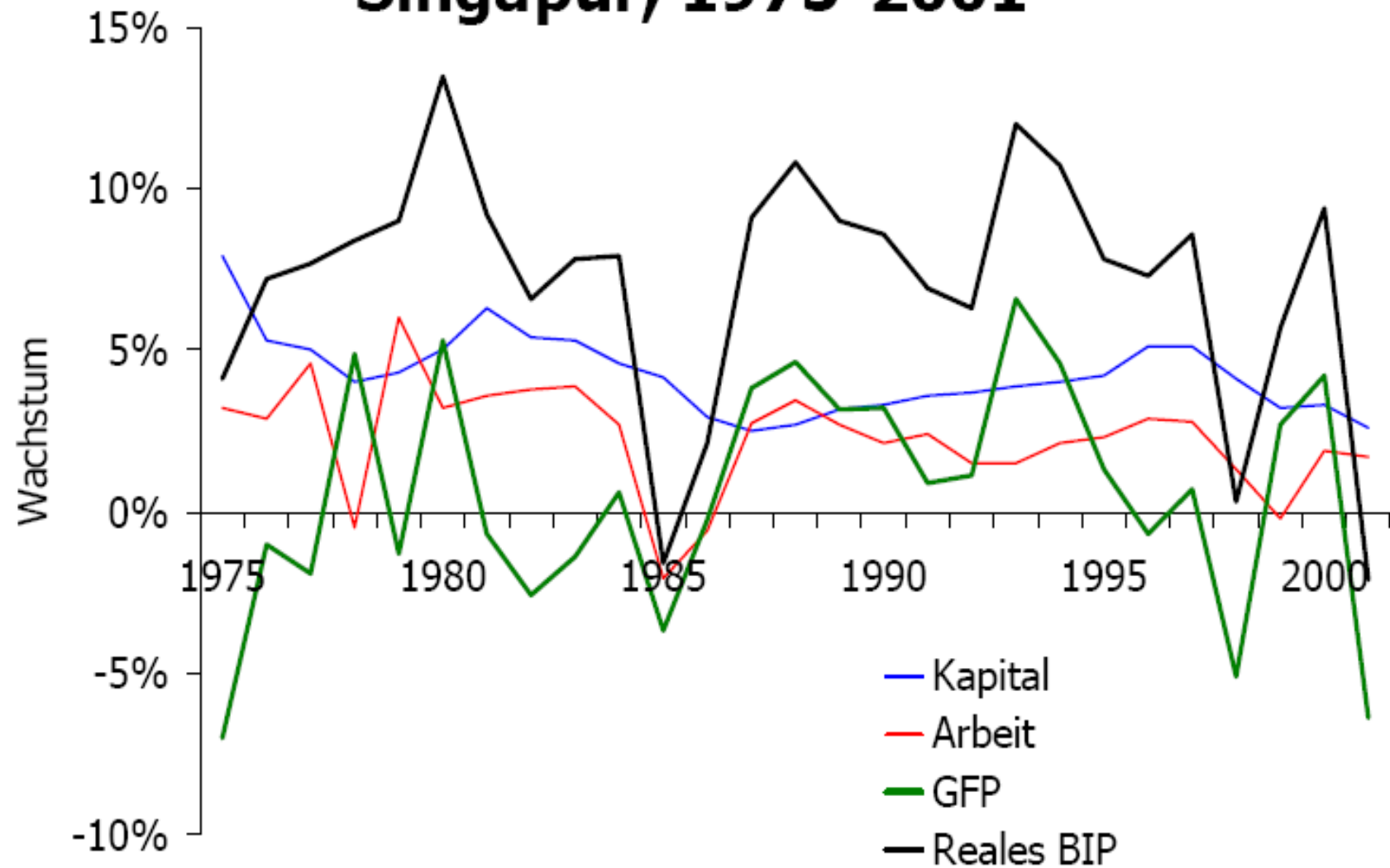
- Factors of production
- Total factor productivity (TFP)
- input-based growth is limited (neoclassical model; decreasing returns for inputs)
- Empirically especially in first phase of growth, until mid-1980s, capital accumulation as main reason for growth
- Young (1994): 1960-1993 South Korea 1,2%, Singapore 0,2 %



	BIP-Wachstum	Wachstumskomponenten		
		Kapital	Arbeit	GFP
<u>1950-73</u>				
Frankreich	5,0 %	1,6 %	0,3 %	3,1 %
Deutschland	6,0 %	2,2 %	0,5 %	3,3 %
Italien	5,0 %	1,6 %	0,2 %	3,2 %
Japan	9,2 %	3,1 %	2,5 %	3,6 %
Verein. Kgr.	3,0 %	1,6 %	0,2 %	1,2 %
<u>1966-90</u>				
Hongkong	7,3 %	3,0 %	2,0 %	2,3 %
Südkorea	10,3 %	4,1 %	4,5 %	1,7 %
Singapur	8,7 %	5,6 %	2,9 %	0,2 %
Taiwan	9,4 %	3,2 %	3,6 %	2,6 %

Daten: *N. Crafts 1997*, zitiert in *P. Wilson 1999*: 29.

# Komponenten des Realen BIP-Wachstums in Singapur, 1975-2001



Daten: Youna 1992; Soon, B. Sim 1999; SDoS

# Problems with the Krugman-hypothesis

- Neoclassical assumptions (perfect competition, knowledge, information)
- TFP cannot be measured easily (residuum)
- Empirical results unclear
- Causality unclear
- Capital accumulation and TFP cannot be divided

# **Accumulation hypothesis versus Assimilation hypothesis**

- Accumulation (Krugman, Young): input driven growth
- Assimilation (Nelson, Rodrick): sectoral change and assimilation of imported technology
- Learning (by doing, by using and copying, by interacting)

# **Are there commonalities (1)?**

- On the surface totally opposed cases
- But: in Germany in 1950s less economic freedom than sometimes assumed (e.g. financial sector regulation, convertibility)
- In East Asia more freedom than sometimes assumed (authoritarian state was much less controllable than centrally-planned economies)
- Both economic systems were mixed, but relatively to their environment free

# **Are there commonalities (2)?**

- Moreover, both cases represent cases of Olsonian power change and beginning (in Germany after the war, in East Asia through assumption of political power by authoritarian governments)
- Third, in both cases a stable institutional (expectations)- equilibrium was reached, leading to an overall fulfillment of expectations and allowing for rather stable, long-term oriented policies

# International context: Institutional competition and institutional constraints

*here: role of occupying forces, competition of economic models and competition for investment; low*

---

## **Formal institutions: „market for institutions“**

### Supply side

Political

entrepreneurs

interest groups

### demand side

consumers

investors

tax payers

companies

bureaucracy

## **Informal Institutions**

Perception of institutions (self perception; perception of others)

„the economic miracle“

---

## Cultural context; cognitive models

*Here especially: models of economic policy and the economy, standards of justice and fairness, traumatic war experience*

# International context: Institutional competition and institutional constraints

*here: peer pressure and American advisors; competition of economic systems*

---

## **Formal institutions: „market for institutions“**

### Supply side

Political

entrepreneurs

interest groups

### demand side

consumers

investors

tax payers

companies

bureaucracy

## **Informal Institutions**

Perception of institutions (self perception; perception of others)

„KORANDO“

---

## Cultural context; cognitive models

*Here especially: models of economic policy and the economy, standards of justice and fairness*



# Are there commonalities (3)?

- Preliminary results: there are different ways to an economic miracle (*kairos* plays an important part)
- There are factors precluding a miracle (as well macro-economic as especially micro-economic)
- **Successful economic order is a moving target!**
- Therefore, open question: is there a way for a “planful” adaptation of growth blueprints?
- Relevancy of this question is obvious, but the answer not

Thank you very  
much!