



Markets in the Post-Cold War Era: Controlled or Free?

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A Capitalist Revolution?

The fall of the Berlin Wall in November 1989 sent tremors rippling further than those of the most powerful earthquakes. Across the globe, ideologies of state control were shaken at their foundations. Even before November, “perestroika” had begun to move south. President Salinas of Mexico had adopted an economic reform program dubbed “Thatcherismo,” Carlos Menem was pursuing a decidedly un-Peronist battle against inflation in Argentina, and Fernando Collor de Mello of Brazil had explained that his red-tape slashing and bureaucracy-pruning campaign was “based on the fact that the state cannot remain with the power of interference that it has today in the Brazilian economy . . . The state is inefficient, the state is corrupt, the state is incompetent, and the state is gigantic.”^[1]

The rhetoric was less enthusiastic in the African less developed countries (LDCs), but nonetheless encouraging. The example of Botswana seemed to be sinking in: its open economy and relatively pluralistic political system had made it the fastest growing economy in black Africa.

In Eastern Europe, many democratic party spokesmen, former dissidents, and religious and human rights activists were revolutionary in their calls for a complete overthrow of the Communist economy and thoroughgoing reform efforts toward the legalization of private property, privatization of state-owned enterprises, openness to international trade and private foreign investment, and decontrol of state authority over pricing, production, and distribution decisions.

All in all, a capitalist revolution appears underway throughout much of the globe -- with the exception of a few recalcitrant holdovers such as China, Cuba, and North Korea. Though enthusiasm for the free market is only lukewarm among some regimes, the stubborn facts of socialism’s demise and the bankruptcy -- both moral and economic -- of statist ideology have taken their toll. Sensible leaders accept matter-of-factly the need to restructure radically their state-strangled economies.

Statist Holdovers

Of course, there are a few quarters where the lessons learned from the last forty years of development experience and from the collapse of the statist model in the last few years have not, apparently, registered. Academia seems to provide a fallout shelter immune from the tremors of the Communist crash. At a recent conference I was challenged

vehemently by several professors for asserting that the Sandinistas' political and economic model in Nicaragua had been carried out at grave human cost.

Moreover, many in the religious community who had apologized for Marxist ideologies of varying stripes remain unrepentant. Radical publications, such as *Sojourners*, tried to salvage the socialist dream by arguing that it was "undeniably true" that the socialist ideal in the Soviet Union and Eastern Europe had been "severely handicapped" by the two world wars and the Cold War. It warned the citizens of the East emerging from under the rubble not to rush headlong toward democratic capitalism, which was full of contradictions.^[2]

Voices from the environmental fringe also seem disturbed by the new enthusiasm for democracy and capitalism (despite the fact that the formerly Communist world was home to the worst environmental degradations). Prophets of an ecological apocalypse see the transnational problems of global warming, deforestation, and desertification as requiring new, powerful international institutions with authority to mandate the details of individuals' lives in the name of environmental protection. Green police governments must protect Mother Earth from what nasty humans, given too much latitude (and longitude), might do to her.

The fall of Communism, in other words, has not brought us the happy "end of history" where democratic-capitalism will inevitably triumph. There are many reasons for hope and enthusiasm that economies in our post-Cold War era will be free. The indictments leveled against state control in the last few years have been many and persuasive and real reforms are underway in a variety of contexts. The march of history does seem to be on the side of human freedom. But even if Communism, the most obvious expression of anti-capitalist animus, has for the most part withered away, more subtle, but virulent, threats to free markets have emerged. Four are discussed below.

The Green Religion

As noted above, one new nest of statist enthusiasm is the environmental movement. To be sure, some of the more responsible thinkers have recognized the clear evidence suggested by the Eastern European experience: namely, that "public control" led to far worse environmental degradation than seen in countries espousing free markets and private property. That controlled economies permitted worse environmental practices ought to have been expected: without property rights and a strict liability structure, stewards of the public domain are personally removed from the responsibility for enhancing the value of what they manage. In some accounts of the fall of Communism in the former Soviet Union (e.g., *Ecocide in the USSR* by Murray Feshbach and Alfred Friendly), the greens were closely aligned with the democratic movement, and even gave rise to it in certain quarters. Many of the "earthkeepers" seem to recognize that decentralized regimes and an economic and legal system connecting private property rights and responsibilities offer far greater promise for environmental protection than does centralized, bureaucratic regulation. But not all of them.

In a speech at a recent conference on the environment, former Secretary of the Interior Donald Hodel related an incident that had “opened his eyes” to the extremist elements in the environmental movement. He had been called to testify in front of a Congressional subcommittee on the Department’s performance in managing designated wilderness areas. He had already been informed that a number of unauthorized and unlawful entries into such areas had been made, but had confirmed that none of them had inflicted any lasting damage on the environment. Indeed, following revegetation, it was impossible to tell that there had been any entries. Confident that this information would reassure those concerned about such entries, Hodel was shocked at the reaction he witnessed from the environmentalists. To them it was immaterial that the entries had caused no damage; the point was that the “sacred” lands, the “holy of holies” had been “defiled” and desecrated by human entry.^[3]

The kind of spiritual commitment to “Mother Earth” revealed by this response characterizes a noteworthy segment of the environmental movement. The so-called “Gala Hypothesis” -- which basically imparts divinity to “Mother Earth” -- animates many environmentalists. Some scholars may be skeptical of the significance of a bunch of “tree-huggers” clinging to strange new quasi-religious beliefs, but the phenomenon should not be dismissed.

More than one analyst has noted the “myth-generating potency” of socialism.^[4] Simply put, a society is held together not just by practical needs or interests but “by beliefs that explain and justify its particular institutional arrangements.”^[5] Socialism’s mythic power has largely been broken (though some Western academics remain entranced by its apparently hypnotic quality); hence, the way has opened for new “myths” to justify statist control. Apart from what one may believe about religion, its persistence into the modern world would suggest that individuals, despite the pressures of secularization, continue to long for a sense of the transcendent. Socialism, in its time, provided that sense for some, substituting for religious belief. Neo-paganism, the New Age movement, and the pantheistic tendencies of much of the green movement all suggest that individuals are searching for a substitute for transcendence. Many are now finding it in the environmental movement. The green religion, much like the socialist one before it, provides justification for state-controlled economies and centralization. If socialism had to restrict individual economic liberty in order to create the workers’ paradise, environmentalism requires an expansion of government control to prevent humans from despoiling “the only planet we have” in order to protect life as we know it.

The apocalyptic character of environmental alarmism only increases its mythic potential and attraction. After all, if the ozone layer really is depleting, if the globe really is warming and the result really will be untold chaos, destruction, flooding, and famine, then perhaps the recommendations of the environmental fringe -- nationalization of businesses by the green bureaucracy, enforced sterilization for population control, and the establishment of extremely powerful transnational authorities to regulate polluting activities -- do not appear so radical. Consequently, the success of this extremist, quasi-religious segment of the environmental movement in attracting a significant following poses a substantial threat to the viability of free markets in the future.

Rising “Fair” Trade

A second sobering reality reining in our confidence in the “inevitability” of free markets is continued protectionism in the industrial countries. This threat is subtle in two ways. First, average tariff rates among the developed nations have generally declined, giving the impression of reduced protectionism. Second, talk about the need to address the problem of protectionism has gone on for so long -- witness the seemingly endless Uruguay Round of the General Agreement on Tariffs and Trade (GATT) -- that people’s ears are not as sensitive to it as they ought to be.

Protectionism remains a serious problem, despite the progress made in tariff reduction. Nontariff barriers and so-called voluntary export restraint agreements have proliferated. The United States has its own favorite protectionist practices -- such as “anti-dumping laws” and import quotas -- revealing that even the loudest defender of free trade ought not cast the first stone against other offenders such as Japan.^[6] The notorious MultiFibre Arrangement -- which applies stringent restrictions on exports of Third World textiles to the developed nations -- began as a “temporary” measure in 1962 and is still on the books. Then there is the European Economic Community’s coordinated agricultural policy that shuts out competition in various agricultural commodities. All of these arrangements make little economic sense. Australian and New Zealand farmers produce cheese substantially cheaper than do their French counterparts, but they cannot sell their less expensive goods to Western European consumers. Protectionist barriers are erected in response to political pressures on domestic governments by the protected industries and individuals.

If the Uruguay Round is unsuccessful in concluding some new agreements to deal with these kinds of blatant violations of the spirit of free trade, at least two sobering consequences are likely. World economic growth will suffer, perhaps leading to recessions that will give even further impetus to protectionism, fueling a vicious cycle. Underdeveloped countries will grow increasingly frustrated with the trade barriers they face and may abandon the market-oriented reforms they have started that emphasize -- drawing on the successful model of the East Asian newly industrializing countries (NICs) -- production for export. Neither of these possible outcomes is heartening for free market enthusiasts.

Reactions to Structural Adjustment

A third factor conducive to the persistence of controlled markets relates to the prospects for structural adjustment in many LDCs. Structural adjustment -- the attempt to transform state-centered economies into market-centered ones through monetary reform, lowering tariff barriers, rationalizing the exchange rate, decontrolling of domestic prices, privatization, and reducing government spending -- is never an easy or uncontroversial process. Its potential for success resides largely in a widely shared perception that the costs of adjustment are worth bearing, that the bitter medicine of austerity will prove a healing balm for critically ill economies and usher in a better future.

The historical and empirical evidence of the last forty-some years in development experience in the Third World provides an adequate basis for optimism. The divergent experiences of Latin America and East Asia, for example, suggest a few, easily accessible lessons about which development models work and which do not. At the risk of oversimplification, one can argue that LDCs that opened their economies to the rigors of international competition through outward-looking trade regimes; that allowed market mechanisms to guide investment, production, and pricing decisions; and that provided a legal structure securing property rights performed better, on a variety of economic indicators, than countries that hid behind protectionist barriers, strictly regulated foreign investment and domestic businesses (for example, through import-licensing bureaucracies and government marketing boards for agricultural goods), and created an atmosphere of unpredictability through nationalizations and expropriations. Simply put, these “lessons,” and others concerning the importance of fiscal prudence, restrained monetary policy, and a competitive exchange rate, are embodied in the best-designed structural adjustment programs. Consequently, countries that persevere in reforms of this nature should have some confidence about their efficacy.

Political realities, though, often force reform-implementing regimes to backtrack. In some instances, fragile democracies fear that adjustment programs will endanger their new political experiments by creating levels of social protest that encourage a military coup “to restore order.” We need not, however, be long delayed by this contention. Professor Karen Remmer has conducted perhaps the most thorough study of the possible connection between austerity and the breakdown of democratic regimes. After analyzing 114 stabilization attempts by regimes in nine Latin American countries, Returner concluded that democratic governments proved no more vulnerable to breakdown than authoritarian ones. Indeed, the breakdown rate for the latter was slightly higher. On the basis of this research, Remmer asserts that “the political risks of stabilization have been overdrawn.”^[7]

The more significant political problem is the maintenance of adjustment in the face of the real social dislocations -- and hence grumbling -- it produces. Typically, the “losers” under adjustment are politically vocal and well organized: they include unionized urban labor, previously protected domestic industries, and the bureaucrats who amassed personal fortunes by virtue of their control of various economic “goodies” under the mercantilist red-tape jungle that prevailed before the reforms. The “winners” under adjustment -- usually rural farmers who see food prices rise to market levels, small entrepreneurs in the informal economy who benefit from deregulation, and labor-intensive export sectors who thrive under new free trade practices -- are less politically powerful and more geographically dispersed. The reform-implementing government must consolidate a pro-reform coalition to back structural adjustment, and, while not impossible, this is a difficult undertaking.

Meanwhile, often well intentioned non-governmental organizations (NGOs) raise loud criticisms against adjustment measures, putting pressures on local governments and international actors (such as the World Bank and the IMF). These NGOs are located at

the “grassroots” and witness firsthand the painful initial consequences of adjustment -- higher food prices, rising unemployment in industry, and cutbacks in government social services. Lacking a broader macro-economic (and longer-term) perspective, these groups sometimes assert that the adjustment medicine is killing the patient.

A consortium of NGOs calling themselves the “NGO Working Group on the World Bank,” for example, issued a policy paper in late 1989 criticizing the Bank’s support of structural adjustment. It argued that the dismantling of state-owned enterprises in the developing countries should be slowed and that the Bank’s emphasis on export promotion should be diminished.^[8] These groups unfortunately have failed to distinguish between the suffering caused by the deep recessions created by populist excesses that made adjustment reforms necessary in the first place; the suffering arising from the dislocations of austerity itself; and the suffering rooted in the abandonment, delay, or distortion of adjustment programs. Their position paper is marred by disturbing arguments that appear to call for a return to the protectionist and populist policies that brought so many LDCs to their current ruinous state.

The need is great, therefore, for a loud reaffirmation by development practitioners of what the empirical record demonstrates: namely, that the costs of not adjusting are far worse than those of adjusting. Nonetheless, though important and necessary, such declarations are of little practical comfort to the individuals bearing the painful burdens of adjustment. Some creative policy responses to lighten those burdens (such as the Bolivian Emergency Social Fund), in ways that do not conflict with the aims of adjustment, are helpful.

To sum up, if adequate steps are taken by reform implementing regimes to alleviate some of the costs of adjustment, popular support for reform will be more likely. The developed countries can help further by reducing their protectionist barriers against LDC exports and generally pursuing market-oriented policies to encourage global economic growth. Structural adjustment reforms will be more likely to be sustained and successful in the context of a growing world economy that provides markets for LDC exports. When formerly statist, protectionist LDCs see it is in their best interests to persevere in market-oriented reforms, the chances are obviously greater that they will. But their enthusiasm for free markets is likely to wane if the sacrifices of adjustment do not lead to improved economic health because the developed world is shutting its doors to increased exports.

Moral Decay

The final factor checking an “inevitable” triumph of free markets may appear tangential, but it is central, it is, for lack of a better term, “moral decay” in the industrialized world and particularly in the United States.

The American Founding Fathers and latter-day philosophers of freedom have long recognized a connection between virtue and freedom. Even Thomas Jefferson, who was not so influenced by orthodox Christianity as, say, James Madison and George Washington, affirmed that “the practice of morality” was vital “for the well-being of

society.”^[9] A sense of “internal constraints” was necessary for life together in a free society if liberty were not to become license.

The free market functions only when it is embedded in a public legal order aimed at ensuring justice, open and equal access, and equality before the law. But beyond the formal structure, it is also necessary that the actors participating in the market system have some inclination toward charity and that they embrace ideals of integrity, honesty, and fairness. Some level of social trust and cooperation is necessary if market exchange is to flourish; likewise, some sense of future-orientation and self-restraint is necessary if capital is to be saved and reinvested.

Now, men are not angels (as *The Federalist* reminds us) and free markets work in spite of this. But markets work less well when men act like indulgent, materialistic, selfish devils: the result of such behavior is often rising levels of indebtedness, economic stagnation due to lack of investment, and growing disillusionment (especially among the impressionable young) about capitalism, which becomes exclusively identified with “greedy capitalists” like Ivan Boesky. Once again, we return to Peter Berger’s observation that capitalism is “singularly devoid of plausible myths”: it seems to lack the ability to enliven its own passionate defense. Moreover, it can quickly become the object of scorn when it is “disfigured” by the morally reprehensible actions of participants “cut loose” from ethical moorings. Problems that are really “moral-cultural” in nature come to be identified as economic in nature, and calls for greater regulation and state control follow.

Conclusion: Some Reasons for Optimism

The discussion above is not meant to discourage enthusiasts of democratic-capitalism, only to note that challenges to economic liberty remain even in a world where its principal antagonist has been defeated. Although we may wish it were otherwise, continued vigilance by the defenders of political and economic freedom is required in the post-Cold War period.

But, to close on a brighter note, several factors conducive to the sustenance and growth of free markets worldwide can be briefly mentioned. Clearly, the economic miracle of the East Asian “tigers” (Hong Kong, Singapore, Taiwan, and South Korea), and the impressive performances of a trio of newly industrialized countries -- Chile, Indonesia, Malaysia -- have had a far-reaching impact throughout the developing world. In 1989, Mexican Foreign Minister Fernando Solana stated:

For more than five years now, we have been shifting toward an export strategy and opening the economy to foreign capital . . . the success of the Pacific Basin countries has influenced our strategy.^[10]

Even LDCs previously committed to statist agendas cannot help but reconsider their approach in light of the successful East Asian model.^[11]

Moreover, the international development agencies are playing a more constructive role now than they had in the 1970s, when they contended that Third World governments had to be the primary actors in development. Massive government-to-government foreign aid transfers were implemented, with money often spent on huge, capital-intensive, prestige projects. Many World Bank officials seemed to believe bigger was necessarily better; they appeared skeptical of the potential for indigenous entrepreneurship; and they seemed to assume that industrialization could be achieved regardless of how badly the agricultural sector was squeezed. Now, the rhetoric is far more encouraging: there is intense interest in the phenomenon of the informal sector (though it took the publication of Hernando de Soto's landmark book, *The Other Path*, to jumpstart this discussion in the broader policy community); there is a new emphasis on labor-intensive, export-oriented production, a reaffirmation of the doctrine of comparative advantage, and a subsequent concern to free agricultural prices and marketing and otherwise take more seriously the conditions of farmers; and there is increasing stress on the importance of non state economic actors as more efficient channels of foreign aid funds. Though one would not want to overstate the case, the World Bank today does seem more committed to free market principles and liberal economics than it did a few decades ago.^[12]

The collapse of Communism also means an end to the Kremlin's funding of Communist satellite states, and it is not unreasonable to hope that this signals the death knell of such regimes. Fidel Castro continues to cling to power in Cuba, but with the economy imploding and nobody in Moscow to rescue him, a new Cuban revolution of some sort seems inevitable. One only hopes it will be more like the Velvet Revolution than the Romanian one, to spare Cubans further suffering after what they have already endured for over three decades.

Finally, the best hope for the future of free markets may be the flowering spirit of liberty around the globe, inclinations toward the centralization of political and economic power do remain in the post-Cold War world and can be seen in the Islamic regimes, the geriatric elite in the People's Republic of China, the military despots of Africa, and among small pro-Communist movements surviving in Eastern Europe and the former USSR. Nevertheless, in the last few historic years, the world has witnessed numerous brave acts of individuals fighting for freedom -- the students in Tiananmen Square, Solidarity workers in Poland, artists and intellectuals in Czechoslovakia, Lutheran human rights activists in what was East Germany. Their example both breathes new life into the "freedom dream" and reminds us that man does not live by bread alone. Citizens of the East who took their lives in their hands by rushing the streets fought for much more than the fancy washing machines, designer jeans, and VCRs enjoyed by their Western European neighbors. The Revolutions of 1989, though indisputably protest movements against political and economic repression, were fundamentally revolutions of the "spirit." As the idea of liberty -- that man was created to be free and that freedom is not only practical, in terms of facilitating economic prosperity, but normative, as the only condition befitting man's dignity -- gains more and more adherents worldwide, the institutions of liberty, democratic governance, and free markets will find fertile soil.

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1. Quoted in James Brooke, "Bad Times, Bold Plans for Brazil," *New York Times* (January 7, 1990), section In, p.4.
 2. See Gat Alperovitz, "Building a Living Democracy," *Sojourners* (July 1990), pp. 11-23.
 3. Donald Hodel, Address at the World Vision Washington Forum on "The Stewardship of Creation: The Effect of Environmental Change on the Poor," May 2, 1992, Washington, D.C.
 4. The phrase is Peter Berger's, from his remarkable work, *The Capitalist Revolution: Fifty Propositions About Prosperity, Equality & Liberty* (New York: Basic Books, 1986), p. 195.
 5. Berger, p. 194.
 6. See James Bovard, "Toxic Dumping," *The New Republic* (December 9, 1991), p. 18; and "Bush Protection," *The New Republic* (January 20, 1992), p. 9. In fairness, it should be noted that Japan's levels of protection are worse than the United States'.
 7. See Karen Returner, "The Politics of Economic Stabilization: IMF Standby Programs in Latin America, 1954-1984," *Comparative Politics* (October 1986), pp. 8-9. Remmer's findings would be even more persuasive if her study included stabilization attempts made after 1984. Since that time, austerity and liberal economic reforms have been sustained in Chile, and even produced economic growth that led to pressures for political liberalization. Bolivia's civilian government has managed to persevere in its reform program, though the political pressures have been significant, and President Jaime Paz Zamora has hinted at his willingness to employ "the Peruvian solution" if continued deadlocks between his executive branch and the legislature continue. Alberto Fujimori's "auto-coup" in Peru provides some fodder for those critical of economic reforms—to wit, that they cannot be successful unless implemented by an authoritarian regime. Fujimori's actions, however, cannot be easily explained by economic factors alone. He seems to have become extremely concerned about the political machinations of former President Alan Garcia, including Garcia's corrupt relations with much of the Peruvian judicial system and his alleged gathering of an armed political force. In this interpretation, the coup resulted more from Fujimori's desire to purge the judiciary of Garcia's influence and address the possible armed threat from Aprista extremists than from a belief that market-oriented reform could continue only if democratic processes were suspended.
 8. "Position Paper of the NGO Working Group on the World Bank," (December 1989).
 9. See Edward Boykin, ed., *The Wisdom of Thomas Jefferson* (New York: Doubleday, Deran & Co., 1941), p. 128.

10. Quoted in “Mexico’s Move to the Market,” *New Perspectives Quarterly* (Fall 1989), p. 42.

11. The policies of these newly industrializing countries were not “laissez faire” in a strict sense, but they did appreciate the central role of the free market.

12. Skeptics are correct to point out that the Bank’s free market rhetoric is ahead of the reality of its lending practices. Most aid is still channelled through governments, and the enforcement of conditionality (making continued aid contingent on the recipient’s adherence to market-friendly reforms) leaves much to be desired. Nonetheless, the Bank has opened conversations with the private and NGO sectors about the channelling of aid through such institutions and its recent major policy statements (e.g., the annual *World Development Report*) reveal a markedly more favorable disposition toward liberal economics than those of the 1970s.

Every great industrialized Western nation, not excluding the United States, owes a very great part—indeed, the major part—of its present technical knowledge and productivity to discoveries, inventions, and improvements imported from other nations. Notwithstanding the elegant elucidations by the classical economists, very few of us today appreciate all that the world and each nation owes to foreign trade, not only in services and products, but even more in knowledge, ideas, and ideals.

Government-to-government foreign aid promotes statism, centralized planning, socialism, dependence, pauperization, inefficiency, and waste. It prolongs the poverty it is designed to cure. Voluntary private investment in private enterprise, on the other hand, promotes capitalism, production, independence, and self-reliance. It is by attracting foreign private investment that the great industrial nations of the world were once helped. It is so that America itself was helped by British capital, in the nineteenth century, in building its railroads and exploiting its great national resources. It is so that the still “underdeveloped areas” of the world can most effectively be helped today to develop their own great potentialities and to raise the living standards of their masses.

—Henry Hazlitt,