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## **The Marshall Plan: Searching for Creative Peace, Then and Now**

Spahn, Paul Bernd  
Goethe Universität Frankfurt

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# The Marshall Plan:

## Searching for ‘Creative Peace’, Then and Now

Paul Bernd Spahn

### Introduction

World War II had come to an end with disastrous economic and political consequences. Europe had suffered in particular: agricultural and industrial production had significantly fallen below pre-war levels, and so had exports; there were food shortages, deficient housing and scarcity of raw materials; existing capital equipment was either devastated, or obsolete and ill-adapted to peace production; people were hungry, poor, and demoralized; gold and dollar reserves had been depleted and access of European economies to world markets was lacking. At the political level there was humiliation and shame on one side, Germany, aching nationalism and political divisiveness on the other. Political antagonism between west and east would cleave the world into two hostile blocs for more than a generation. Civil and political liberties and democratic institutions were fragile and under assault from misery, lack of opportunities, and widespread pessimism. At that time, a soldier—a former chief of staff of the United States Army who had become secretary of state—George Catlett Marshall, rose to address young students of Harvard University with a truly visionary message:

”It is logical that the United States should do whatever it is able to do to assist in the return of normal economic health in the world, without which there can be no political stability and no assured peace. Our policy is directed not against any country or doctrine but against hunger, poverty, desperation and chaos. Its purpose should be the revival of a working economy in the world so as to permit the emergence of political and social conditions in which free institutions can exist.”

(George C. Marshall, Harvard University commencement ceremonies of June 5, 1947.)

Marshall’s sketch of ideas would form the bedrock of an American foreign policy initiative and foreign aid program that was truly unique in its approach and amazingly successful. Discarding the punitive philosophy of the Treaty of Versailles, Marshall stood for international cooperation and ‘creative peace’—as one observer has called it<sup>1</sup>—and this was initiated against political opposition at home where the polls showed little support for the Plan and where there were strong isolationist tendencies in Congress. The program was criticized to be a waste of money with little economic and political impact in Europe. It was neither expected to induce much economic restructuring and development under the conditions prevailing in Europe—where government interference and planning was rampant—nor deter those who favored communism from flirting with Moscow. On the contrary, concern was expressed that the plan would shelter uneconomic and unsustainable industrial structures of European economies, that it would uphold anti-market interventionist governments, and that it would run counter U.S. and European private business interests. Finally there was opposition to the Plan on the grounds that it would assist Europe’s colonial powers in maintaining their grip on African and Asian territories.

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<sup>1</sup> Porter letter to Kindleberger, January 16, 1947, RG 59, file: 501.BD Europe/1-1647, quoted in Hogan (1987, p.37).

True, Marshall did not stand-alone with his initiative at the time. The cooperative and multilateral spirit of his program had equally guided the conception of important institutional arrangements at the international level, notably the conception of the Bretton-Woods institutions — the International Monetary Fund, the World Bank and GATT —, but these institutions would unfold only later, and the Plan was thus crucial for political and economic developments in Europe. For the world economy, the initiative was indeed bold and unprecedented.

Marshall's original speech contains little details and specifications of the Plan, but it was to spawn the singular European Recovery Program (ERP) that was formally presented by president Harry Truman in a message to Congress only six months later. This Program was to endure for four years and designed to achieve three ambitious policy objectives: the expansion of European agricultural and industrial production; the restoration of sound currencies, budgets, and finances of individual European countries; and the stimulation of international trade among European countries and between Europe and the rest of the world.

### **"Creative Peace" Then**

The amounts expended under the Plan range between \$10 and \$13 billion, or roughly \$70 to \$90 billion in today's prices (Table 1).<sup>2</sup> Two implementing agencies were set up, one on the American side (the Economic Cooperation Administration, ECA), one in Europe (the Organization for European Economic Cooperation, OEEC, in Paris, which was to become the nucleus for today's Organization for Economic Cooperation and Development, OECD). This division of competencies reflected Marshall's intent to establish a truly transatlantic partnership, a "joint venture" between the United States and participating European countries, and a multilateral and shared responsibility for carrying the Program to success.

And success it was, indeed! By the end of 1951, during the four years of the plan, industrial production for all participating countries had increased by two thirds and agricultural production by one quarter. Aggregated GDP had grown by 25 per cent during that same period. The trade deficit of participating European states with regard to the dollar area had fallen from about \$8 billion in 1947 to nil during the first half of 1953,<sup>3</sup> and this despite deteriorating terms of trade.

Success can also be expressed in terms of specific quantitative objectives like steel production (60 million tons/year compared to a target of 55 million tons/year which had already been set at an ambitious 20 per cent above pre-war production) or oil-refining capacity (twice as high as the official target). Financial stability in Europe had been restored (also by other measures, of course, such as the German currency reform of 1948) and the "dollar gap" had been virtually closed. Intra-regional trade among OEEC-countries had substantially grown as it was fostered under the Plan, institutionally supported by a European Payments Union (EPU) established in 1950 that acted as a clearing and settlement system for payments among member states. During the duration of the Plan, government budgets recovered through stable wages, higher taxes, and the consolidation of debt burdens, and budget deficits could be reduced substantially.

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<sup>2</sup> U.S. Agency for International Development, November 16, 1971.

<sup>3</sup> OECD Observer, June 1967, pp. 10-11.

**Table 1: Funds Made Available to ECA for European Economic Recovery (a)**

(Millions of dollars)

Funds Available	April 3, 1948, to June 30, 1949	July 1, 1949, to June 30, 1950	July 1, 1950, to June 30, 1951	Total
Direct appropriations (b)	5,074.0	3,628.4	2,200.0	10,902.4
Borrowing authority (loans) (c)	972.3	150.0	62.5	1,184.8
Borrowing authority (investment guaranty program) (d)	150.0	50.0	--	200.0
Funds carried over from interim aid	14.5	6.7	--	21.2
Transfers from other agencies (e)	9.8	225.1	217.0	451.9
Funds made available (gross)	6,220.6	4,060.2	2,479.5	12,760.3
Less transfers to other agencies (f)	--	--	225.4	225.4
Funds made available (net)	6,220.6	4,060.2	2,254.1	12,534.9

- a. Compiled from figures made available by the budget division of ECA and from figures published in the Thirteenth Report of ECA, pp. 39 and 152; and Thirteenth Semiannual Report of the Export-Import Bank of Washington, D.C. For the Period July-December 1951. Appendix I, pp. 65-66.
- b. The Foreign Aid Appropriation Act of 1949 appropriated \$4 billion for 15 months, but authorized expenditure within 12 months. The Foreign Aid Appropriation Act of 1960 contained a supplemental appropriation of \$ 1,074 million for the quarter April 2 to June 30, 1949, and an appropriation of \$3,628.4 million for fiscal 1950. The General Appropriation Act of 1951 appropriated \$2,250 million for the European Recovery Program for the fiscal year 1951, but the General Appropriation Act of 1951, Sec. 1214, reduced the funds appropriated for the ECA by \$50 million, making the appropriation for fiscal 1951 \$2,200 million.
- c. The Economic Cooperation Act of 1948 authorized the ECA to issue notes for purchase by the Secretary of the Treasury not exceeding \$1 billion for the purpose of allocating funds to the Export-Import Bank for the extension of loans, but of this amount, \$27.7 million was reserved for investment guaranties. The Foreign Aid Appropriation Act of 1950 increased the amount of notes authorized to be issued for this purpose by \$150 million. The General Appropriation Act of 1951 authorized the Administrator to issue notes up to \$62.5 million for loans to Spain, bringing the authorized borrowing power for loans to \$1,184.8 million.
- d. The Economic Cooperation Act of 1948 was amended in April 1949 to provide additional borrowing authority of \$122.7 million for guaranties. The Economic Cooperation Act of 1950 increased this authority by \$50 million, making the total \$200 million for investment guaranties.
- e. Transfers from other agencies included: from Greek-Turkish Aid funds, \$9.8 million; from GARIOA funds (Germany), \$187.2million; from MDAP funds, \$254.9 million. The Foreign Aid Appropriation Act of 1950 and the General Appropriation Act of 1951 authorized the President to transfer the functions and funds of GARIOA to other agencies and departments. Twelve million dollars was transferred to ECA from GARIOA under Section 5(a) of the Economic Cooperation Act of 1950 and the remainder under the President's authority. The Mutual Defense Assistance Act of 1949 appropriated funds to the President, who was authorized to exercise his powers through any agency or officer of the United States. Transfers to ECA were made by Executive Order.
- f. Transfers to other agencies included: \$50 million to the Yugoslav relief program, \$75.4 million to the Far Eastern program, and \$100 million to India. The transfer to Yugoslavia was directed by the Yugoslav Emergency Relief Assistance Act of December 29, 1950. The transfer to the Far Eastern program was made by presidential order (presidential letters of March 23, April 13, May 29, and June 14, 1951). The transfer to India was made by presidential order (presidential letter of June 15, 1951).

Source: Brown, Jr., and Opie, 1953, p. 247 (from CRS Report for Congress, U.S. Information Agency Homepage).

True, there is much debate on whether the ensuing post-war "economic miracle" in Europe can be ascribed to the Plan and its off-springs (like the EPU) even partially, because—as the skeptics argue—the resources transferred constituted only less than 3 per cent of combined national incomes of OEEC-countries, because they were less than one fifth of gross investment, and because only 17 per cent of Marshall aid was spent on machinery and vehicles at home, the remaining part on commodity imports from the United States.<sup>4</sup> But the skeptics must also explain why Europe could maintain an investment level of about 20 per cent of GDP during that time—one third higher than before the war—despite the fact that national savings had actually been zero in 1948. There is evidence that countries that received more aid under the Plan also invested more (De Long and Eichengreen 1991). Moreover, the Marshall Plan had a high leverage effect through the mobilization of counterpart funds in national currencies because national governments had to match Marshall aid through their own taxpayers' money in order to account for program costs denominated in local currency. Also, the impact of the Program was enhanced through the possibility to target the funds on specific areas for reconstruction and development. And the yields on new investment were indeed extremely high the social rate return on investment being estimated as high as 50 per cent a year during that period.<sup>5</sup>

The main beneficiaries of the Plan were the United Kingdom (24 per cent) and France (20 per cent of total aid). The losers of the War, (West) Germany and Italy, received essentially half of these amounts with only 10 and 11 per cent of the total). In terms of per-capita transfers, the main beneficiaries were Iceland, the Netherlands, Austria, Greece and Norway—all smaller European countries. Among the bigger countries with populations exceeding 40 million, again the United Kingdom and France were at the top in terms of per-capita transfers received—with both securing approximately US \$ 420 each in today's prices. By contrast, West Germany and Italy received only about \$210 and \$190 per capita in 1997 US dollars (Table 2).

If per-capita transfers received by country are related to the per-capita average of the region (excluding the population figure for the Asian part of Turkey), the relativities can be seen from the Chart. Four groups can be distinguished. Portugal, Turkey and Sweden form a group with less than 30 per cent of aid in per capita terms; West Germany and Italy received 40 per cent, and a third less than the average in per capita terms. Belgium/Luxembourg, Denmark, the United Kingdom and France each obtained roughly 30 per cent more than the average per-capita. The smaller countries Norway, Greece, Austria and the Netherlands clearly stand out in terms of per-capita aid received, the latter three countries obtaining about twice as much as the average. There is only one country that comes close to the average per capita amount—Ireland. The wide dispersion of per capita aid is with a standard deviation of 66.7 percent is indeed striking.

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<sup>4</sup> De Long and Eichengreen (1991), p. 30. It should be noted however that such imports were not exclusively for consumption and that these commodities also set world quality standards for the emerging European production, a precondition for successful exports during the following years.

<sup>5</sup> *Ibidem.*

**Table 2: European Recovery Program Recipients**  
**April 3, 1948, to June 30, 1952**  
(Millions of dollars)

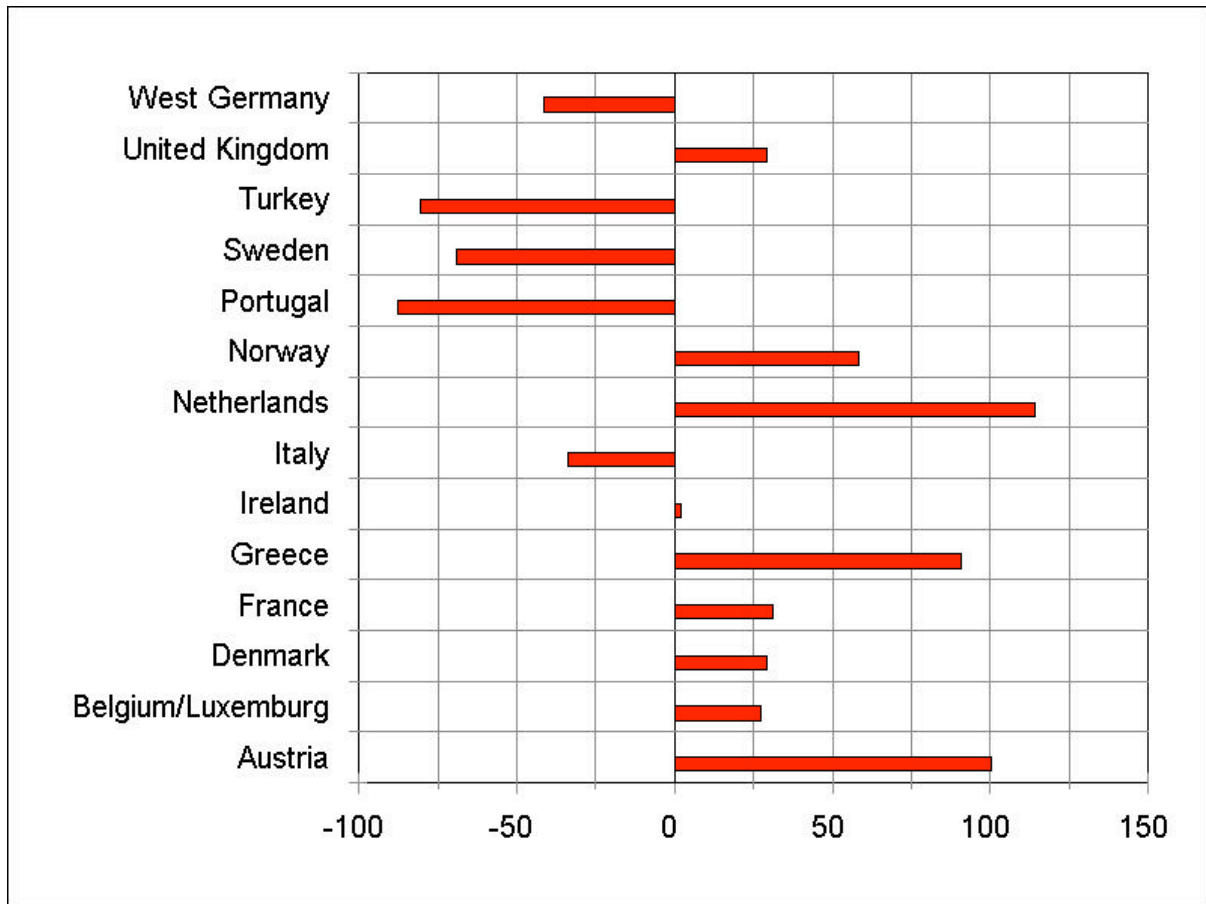
	Population		Current dollars		Constant 1997 dollars		Share of
	in 1000		Total	Per capita	Total	Per capita	total in percent
Austria	6,934	(June 1952)	677.8	97.75	4,486.9	647.09	5.1
Belgium/ Luxembourg	9,025	(Mid-1952)	559.3	61.97	3,702.5	410.25	4.2
Denmark	4,336	(mid-1951)	273.0	62.96	1,807.2	416.79	2.0
France	42,500	(March 1952)	2,713.6	63.85	17,963.6	422.67	20.4
Greece	7,600	(April 1951)	706.7	92.99	4,678.2	615.55	5.3
Iceland	145	(Mid-1951)	29.4	202.72	194.0	1,337.93	0.2
Ireland	2,959	(Mid-1951)	147.5	49.85	976.4	329.98	1.1
Italy	46,885	(September 1952)	1,508.8	32.18	9,988.0	213.03	11.3
Netherlands	10,377	(July 1952)	1,083.5	104.41	7,172.6	691.20	8.1
Norway	3,308	(March 1952)	255.3	77.18	1,690.0	510.88	1.9
Portugal	8,606	(Mid-1951)	51.2	5.95	338.9	39.38	0.4
Sweden	7,126	(June 1952)	107.3	15.06	710.3	99.68	0.8
Turkey	23,485	(December 1950) (a)	225.1	9.58	1,490.1	63.45	1.7
United Kingdom	50,650	(December 1951)	3,189.8	62.98	21,115.9	416.90	23.9
West Germany	48,708	(December 1952)	1,390.6	28.55	9,205.5	188.99	10.4
Regional	-	-	407.0		2,694.3		3.1
<b>Total</b>			<b>13,325.9</b>	<b>48.87</b>	<b>88,214.4</b>	<b>323.55</b>	<b>100.0</b>

a. European part only.

*Source: U.S. Agency for International Development, November 16, 1997 (from CRS Report for Congress, U.S. Information Agency Homepage). Population data from Statistisches Jahrbuch für die Bundesrepublik Deutschland (various issues); own calculations.*

There is wide agreement that the Plan alone would probably not have achieved much and that it was but one of several factors that added to economic growth and reconstruction in Europe. Existing human resources, sound infrastructure—albeit badly damaged—, regained access to new technologies and world markets, a robust legal framework and functioning bureaucracies as well as widespread political support in the region equally contributed to this "miracle". But although the direct effects of the Plan on growth in Europe may be questioned, a number of distinctive elements of the program were indeed important for post-war economic and political developments and the enhancement of well-being in Western Europe:

**Chart: European Recovery Program Recipients**  
**Per capita transfers received in percent of average per capita aid**



*Source: See Table 2.*

- First, it was the explicit recognition of a positive relationship between economic and political stability. This does not only emphasize the role of sound economic conditions for consolidating the role of government and the political system. It also embraces a dynamic component for attaining long-run stability and sustainability of European economies, because most of the aid was given in the form of grants and large amounts of indebtedness of the new partners in an emerging transatlantic partnership was thus avoided. The lessons of the Treaty of Versailles and its consequences had been learned.
- Second, it was the recognition of national sovereignty of OEEC countries—although under Allied control in the case of Germany—, and the institutions of the Plan fostered dialogue and cooperation, not submission or coercion. Initiatives had to be taken by recipient countries, implementation was a joint endeavor, and responsibilities were shared. Although the United States had a clear-cut foreign policy objective of their own—the containment of communism in the world—, the emphasis of the Plan was on partnership and mutual respect. Thus the European institutions created under the Plan, the OEEC and EPU, proved to be extremely effective instruments of U.S. diplomacy under difficult historical circumstances.

- Third, the national security objectives of the United States were carried on to Western Europe and the groundwork for NATO was laid<sup>6</sup> which would ultimately prove to be extremely effective in preserving peace in the Western Hemisphere. The Plan had extended financial assistance even to Central and Eastern European countries and the Soviet Union,<sup>7</sup> although the latter and its allies rejected this as an infringement on their national sovereignties and as jeopardizing the long-term aim of a "world revolution" and the establishment of communism at the global scale. By marrying foreign policy objectives, political stability and economic recovery, the Plan was indeed "creative" in its search for peace, and it is noteworthy that Marshall became the only professional soldier ever to be awarded the Nobel Prize for Peace.
- Fourth, the OEEC as a forum for mutual consultation and cooperation became the cradle of more comprehensive economic policy coordination among industrialized countries in the world—with progressive expansion of its membership. Some would draw the line even further and relate the Plan to the launching of the Coal and Steel Community in 1952, and eventually its longer-term successor—the European Union of today. These far-reaching implications may seem to be exaggerated for many,<sup>8</sup> because such developments were mainly driven by Europeans initiatives, but the initial trigger effects of the Plan should indeed not be underestimated in this context because it probably tipped the balance in a precarious political and economic situation where the newly emerging or reconstructing democracies in Europe—suspicious and unaccustomed to cooperation and partnership—were in search of a new feasible "*modus vivendi*" among themselves and with the rest of the world.
- Fifth, the Plan had a distinct leaning toward the free play of the market and toward the liberalization of international trade even where this seemed to jeopardize short-run American interests. Indeed, at the time, U.S. businessmen feared (and experienced) both mounting competition from European exporters at home, and the loss of formerly uncontested markets abroad. The emphasis on the market and on free trade—although by far not fully realized immediately—would create the conditions for a consumer-driven reallocation of resources and the enhancement of well being in European countries, and for a rapid conversion of their "war-production-machines" into internationally competitive economies. It also brought Western Europeans into the club of prospering countries that adopted a liberal, market-oriented philosophy, and they would become reliable partners in a reintegrating world economy.

However the Plan was not only important because it contributed to mobilize long-run dynamic gains from trade in an integrating world economy (from which both sides of the Atlantic would benefit); it was also decisive in guiding policy making in Western Europe where governments were indeed still predisposed toward interventionism and regulation. Without the Plan, the dismantling of wartime allocation controls and the elimination of re-

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<sup>6</sup> Compare U.S. House of Representatives, Committee on Appropriations, Foreign Aid Appropriation Bill for 1950, 1949, p.33.

<sup>7</sup> It may be debated though whether this offer was serious and whether it was not simply a strategic gesture whose acceptance by the Soviet Union would have embarrassed the U.S. government—playground for speculation by historians, but vain through the pace of events.

<sup>8</sup> It should be noted however that American politics was favorable to the idea of European integration at the time. For instance, John Foster Dulles told the National Publisher's Association in January 1948 that any plan for the future of Germany should be "in terms of the economic unity of Europe". And further "A Europe divided into small compartments" could not be "a healthy Europe" (from Hogan 1987, p. 37).



straints on competition and the free movement of resources are likely to have been slower and the transition process much more painful for Europeans.

- Sixth, at the more technical level, the Plan was creative in setting an unambiguous sunset date for support; this made it clear that the Plan was to be temporary "aid toward self-aid", and not to be relied upon indefinitely. This distinguishes it, for example, from the current regional transfer program within unified Germany which may be more massive in scale<sup>9</sup>, but certainly less effective because a policy of gap-filling has raised expectations of continuing bail-outs, it hinders own initiatives, and it slows down structural adjustment in Eastern Germany.
- Moreover, the idea of counterpart funds, whereby each country benefiting from Marshall aid was required to set aside a matching amount of its own currency, reinforced the impact of the program through a leverage effect, and it gave the United States an important policy lever in transmitting her own policy priorities—especially as these priorities changed later when an increasing proportion of the funds was being channeled toward defense under the peril of the Korean War. The policy regarding the counterpart funds was, however, very flexible. Whereas they were typically earmarked to very specific investment projects in utilities, transportation and communication facilities, for instance, Great Britain was allowed to channel a substantial part of counterpart funds into retiring debt. In France, the release of counterpart funds seems to have been made contingent on policies leading to a balanced budget (Auriol 1970, p. 162).
- From Marshall aid, a special fund was branched off to finance technical assistance and to bring to Europe experts from the United States. Although this program was small in terms of financial commitments, the effects of such assistance are generally thought to be rather important, and the program as such is considered to have been a success.
- And finally, the Plan was a tribute to raising the morale of European citizens and it turned widespread pessimism into purposeful actions. It also produced—at least in Germany—feelings of gratefulness—which was to be augmented during the blockade of Berlin—, and it contributed to the reconstitution of their national self-esteem after the devastating and humiliating experience of the Nazi regime.

All these elements combine into a singular American aid program for "creative peace" which will remain forever be linked to State Secretary Marshall's name.

### **The Quest for a "New Marshall Plan"**

It has often been argued, with regard to the Third World and—more recently—to transition economies, that a new Marshall Plan was needed to assist economic development and reconstruction in these countries. In order to assess whether a new version of the Plan would work under the present conditions prevailing in transition and developing countries, it must first be understood why the Plan was successful in the first place and what the conditions for its success had been.

Unquestionably, the ERP seed money fell on extremely fertile grounds in post-war Europe. European economies were operating in an institutional setting where private property rights had

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<sup>9</sup> Net transfers from West to East Germany constituted DM 160 billion in 1995, or 42 per cent of the recipient region's GDP—compared to about only 3 per cent of GDP for the OEEC countries during the years of the Marshall plan. For more details on regional transfers within Germany after unification see Paul Bernd Spahn and Wolfgang Föttinger (1997), Table 4, p. 234.

essentially been preserved—even under Hitler’s planned economy—, where there was a spirit of initiative, response, and entrepreneurship, and where there existed functioning administrations in the public sector. There were solid legal foundations that could be relied upon in order to foster and support economic activities. Moreover, American aid could mobilize a high degree of political commitment for the objectives of the plan because such commitments of the most recent past had been discredited—not only in Germany, but also in other European countries where collaboration with the Nazi regime had been noticeable. The emphasis of the Program was on productivity—rather than rent seeking—and the efficient use of dollars for international trade allowed an economic recovery that quickly became self-sustaining. Ironically, the destruction of production capacities during the war often proved to be an advantage for European entrepreneurs because it called for the redesign of production from scratch and because it inspired firms to discard old-fashioned production lines and to adopt most modern techniques. Moreover, economic restructuring and development were supported by a highly motivated, disciplined and skilled work force that had but one simple new ideology—economic accomplishment and success—after the hardship and, particularly in Germany, political disillusionment that had come with the end of the war. Poverty, social distress and fragile democratic institutions together with the lure of a hitherto unknown, but possibly attractive alternative ideology—communism—spurred the enthusiasm of those, including the Americans, that waged the battle against time in order to prevent Europe from falling prey to yet another historic blunder.

And finally, the Plan had to fill the void of a newly emerging world economic order where the main institutions conceived 1944 in Bretton Woods—the International Monetary Fund, the World Bank, and GATT—were still in their infancy and had barely begun to lay the groundwork for free trade, effective development policies, and a stable financial system for the world—with convertibility of currencies, fixed exchange rates, and freedom of capital movement.

The historic conditions prevailing in post-war Europe were thus unique and cannot simply be compared with the situation that prevails in the developing or transition economies of today. In a modern, integrating world economic order that prepares for the next century, the circumstances are quite different from those that existed fifty years ago.

- International cooperation has not only become the prevailing policy paradigm, there is also a great number of institutions for effective policy coordination and mutual support at the international level, the International Monetary Fund, and the World Bank, the World Trade Organization—let alone the United Nations and a host of regional development banks. Many of these institutions are in a position to mobilize funds for countries in distress, to support economic reconstruction and growth, and to work out development programs in conjunction with their member governments. Furthermore, they are committed to creating a stable and effective framework for international finance and to facilitating access to world capital markets, they monitor the common rules established for international trade, and they sustain world commodity markets and multilateral trade based on the principles of non-discrimination and transparency.
- For the industrialized world, the OECD constitutes an effective coordination agency, and the European Union has matured to an entity that shares responsibilities with the United States at an international level.
- Apart from these coordinating institutions, there is a clear trend toward regional economic integration and joint policy making among nation states—not only in the European Union, but also in other parts of the world (NAFTA, ASEAN, APEC, Mercosur). This implies a tendency toward multilateralism rather than bilateralism in addressing economic restructuring and development of retarded regions.

- Since the war, the world economy has become highly interdependent. Markets—in particular financial markets—are increasingly transgressing national boundaries while becoming more and more globalized and difficult to regulate or control. The scope for national economic policies is not only reduced by regional integration and international policy coordination, but also by the force of markets and competition at the world level. The free flow between countries of factors of production—capital and labor—has created a highly competitive environment with a multitude of new financial instruments and a massive expansion of financial activities. Moreover, global competition puts pressure on standardized labor contracts with severe consequences for the financing of the welfare state, which is predominantly based on payrolls, and it impinges on the ability of national governments to tax (Tanzi 1995).
- After the fall of the Berlin Wall, the market paradigm has gained distinction over interventionist philosophies, and the protectionist mood in many transition and developing countries has surrendered to more competitive attitudes worldwide. The defensive strategy of import substitution in foreign trade—that had retarded economic developments in many parts of the world—has finally yielded to a more aggressive export-orientation which benefits both, industrialized nations and developing countries alike—as the latter open up their economies to confront international competition. There are thus first traces of an all-embracing global consensus on the importance of market forces and of competition in the efficient use of resources—despite continuing cleavages on the question how to distribute the wealth of nations.
- The globalization of markets, the decentralization and diversification of production processes, the ubiquity and ready availability of information, ease of communication, and international competition, do not only imply the convergence of prices, but also of policies, perceptions, expectations, and visions. In particular, globalization is about to open up the service industry, which offers to developing countries an easier access to information, technology, and markets.

These new trends in the world economy have greatly enhanced the prospects for economic development in transition and emerging economies in conjunction with its financing. In 1996, liberalized private capital markets have mobilized five times as much international capital for the developing world than official government aid put together. But private capital flows are also more volatile than politically determined aid because they are highly sensitive to perceived market risks and to policy blunder. Therefore, private capital in developing, emerging and transition economies often matures fast, such flows can be rather volatile, and—importantly—they dodge are great number countries where growth potentials are sensed to be weaker. Nevertheless, they also bear testimony of the fact that finance does not seem to constitute a major bottleneck in these days. Moreover, even countries whose access to private capital markets is more difficult are not left apart. They can rely on multilateral international lending agencies and on a comprehensive network of bilateral arrangements with a great number of investment and development banks, as well as on continuing aid from industrialized nations.

All this renders a new financial aid program similar to the Marshall Plan less compelling now than in the post-war period. Furthermore—as demonstrated by Germany's regional transfer program to the Eastern *Länder*—financial aid can be counterproductive when it is given on a continuing basis. It tends to neutralize pressures for economic restructuring, it raises expectations for further bailouts, and "financial dependency" may easily become a "life-style"—even for nations. So it should be clear that a new Marshall Plan for transition and developing countries cannot be, and should not be, a long-term restructuring exercise, a point that is frequently overlooked by those that advocate for a new Plan.

It is therefore important to stress that the Marshall Plan was succinctly limited in time and this was an important element of its success. The question is now whether a targeted, time-limited ERP for Central and Eastern Europe could have made sense after the fall of the Berlin Wall. This question is more rhetoric than real, because historically such a program was not brought to bear, and by now its chances appear to have been missed. Hence, were today's politicians less visionary than State Secretary Marshall at his time?

Perhaps, some would say, but I plead that even Marshall may have hesitated to propose his program for transition countries in the historically unique situation after the collapse of communism. Why? As argued above, countries can nowadays rely on a well-functioning international capital market, and there are international bodies that specialize in the setting-up of economic development and restructuring schemes, and they combine it with specific, targeted and conditioned financial aid—not only the International Monetary Fund and the World Bank, but also the United States and the European Union as well as specific European agencies such as the London-based European Bank for Reconstruction and Development (EBRD). And there are many reasons to believe that it was wise to put those institutions in charge of dealing with the immense challenge after the historical break-down of communism rather than going for a blind re-make of the Marshall Plan of fifty years ago. The channeling of unconditional finance into the formerly communist countries would have indeed been dubious

- because their political and administrative institutions, the organization of production and distribution, and the legal framework for economic operations were (and still are, to some extent) inappropriate for a well-functioning market economy;
- because key economic sectors, such as finance and other highly specialized services, were deficient in these countries and typically had to be re-built from scratch;
- because private property had been limited, and collective property rights had thwarted investment initiatives and entrepreneurship; moreover, reforms to rewind this process had to be slow by nature, and they tended to be erratic;
- because entrepreneurship and specific skills of a modern service industry were (and still are) largely absent;
- because public enterprises were non-competitive in these formerly-closed economies, with poor technologies in most industries, hidden subsidies at all levels of production, and excessive social functions bestowed upon the enterprise sector;
- because administered pricing had eliminated or distorted economic incentives; this was also true for post-war Western Europe, but the length of time socialist countries had endured such regime as well as its proportions were more biting, and a harsh reversal of the policy threatened to entail social hardship and was therefore limited in scale; and finally
- because the level of public expenditures was unsustainable, and the tax system was distortive and misconstrued.

Consequently, a first period of restructuring had to be devoted to the establishment of a political and legal framework to support civil liberties and the play of a free market—liberalization and privatization—, to institutional reforms to sustain, *inter alia*, capital markets and other non-bank financial sectors, and to the restoring of macroeconomic stability. True, grantor governments and international donors have tried to encourage such restructuring through conditional grants and loans, but such transfers could hardly become as effectual as the Marshall Plan as long as these requirements had not been met. The first-round transfers to transition economies can thus be regarded as a vehicle to encourage basic reforms, which was typically expected to bear fruit only in the long run—different from the American approach of fifty years ago.

In a second phase of reform in transition economies the key challenges will be "to build, consolidate and strengthen the institutions, policies and practices which underpin a well-functioning market economy and the investment that supports growth. In responding to these challenges, good governance will be crucial. This must involve openness, transparency and credibility and the absence of bureaucratic interference and corruption. Such governance is vital to the emergence and maintenance of an effective competitive process. The private sector must also in this phase build the sound business practices, which will lead to long-term success. Good governance both encourages and is supported by the development of civil society." (EBRD 1997).

Again, this is a longer-lasting and painful process that cannot be expected to bear fruit rapidly—neither with, nor without grant money—, because the necessary reforms generally lag behind, and progress in enterprise restructuring and improving governance continues to be slow in many transition economies. Furthermore, it is exacerbated by severe income inequality, fragile institutions and uncertainty about legal rights and entitlements, the lack of understanding the rules of a market economy, weak initiatives in the private domain, and poor performance of the public sector—with corruption in the public administration.

Was the Marshall Plan then a historic incident with no further relevance for solving today's problems? Nothing could be more mistaken! In today's search for 'creative peace', one can still benefit from Marshall's basic philosophy, from the cooperative and multilateral spirit of his program, from his idea of partnership, shared responsibilities, collaboration among governments and institutions, mutual respect and full recognition of sovereignty and individual freedom. Such virtues are crucial in a globalizing world where information, attitudes, and moral values will have to be shared without spurring new ideological cleavages and combats. We still have to be 'creative' in the search for peace—as Marshall was at his time—although different conditions will commend different measures. But his basic message—cooperation, concertation, dialogue and respectful deliberation—rests all the same.

## **"Creative Peace" Today**

As follows from the preceding analysis, the conditions for financing reconstruction and development are very different from those that existed after World War II. There is now mounting agreement on a "world economic order" which is favorable to market processes and critical to state interventionism. Moreover, there are functioning international institutions such as the International Monetary Fund and the World Bank, and there are private capital markets that are prepared to bring savings to work on a global scale—even to the lesser-developed countries provided that their sovereign risks are manageable. So finance does not seem the main bottleneck in these days and financial aid as such will not be sufficient to solve the pending problems. What is required to allow the formerly socialist and the developing countries to participate in global welfare and its expansion can be typified by three *i*'s: institution-building, infrastructure, and integration.

### ***Institution-building***

Institution-building means democratization of the society in order to have citizens participate in public-decision making and to set up the necessary control mechanisms for checking errand behavior such as collusion and corruption; it also means the establishment of a robust financial sector with an independent Central Bank and the conduct of a stability-oriented monetary policy, as well as a healthy private banking sector that is subject to international competition and functions in a transparent way; and there is need for tax reform, for the improvement of the budget process and the realization of fiscal discipline through hard budget constraints. Institution-building implies fiscal decentralization and the enhancement of allocating public re-

sources; it entails a clear definition of property rights, including risks associated with the environment; it requires the overhaul of existing pension systems and the confinement of other financial risks of the public sector, the detachment of the government budget from public enterprises (privatization—in particular of state banks which provide access to soft financing); the strengthening of the domestic private financial sector and its control; it means the corroboration of the political and legal system and its institutions, as well as the improvement of the overall climate for investment and economic activities. Soft financing through foreign aid would probably only slow down this adjustment process—unless clearly based on a code of conditionality.

As for institution building in transition and developing countries, responsibility must remain with the citizens of these countries and their respective representatives in the first place. Assistance from abroad will always find its limits in a given national polity and the perceptions of the citizens and agents living therein. Foreign assistance has thus to be confined to technical advice—which may be supported by financial incentives. Today such expertise as well as corresponding funding mechanisms are predominantly vested in functioning international organizations—although bilateral aid may complement the complex mosaic of international political and economic relations.

In this context, the International Monetary Fund must continue to assume a key role in coordinating macroeconomic policies and in developing and implementing monetary and fiscal reforms. In the past, the IMF has often assisted structural transformation processes, notably in the former Soviet Union, and therefore some observers—including the Bretton-Woods Commission—advocate for a stricter separation of functions from those of the World Bank. The latter should primarily focus on microeconomic restructuring, while the International Monetary Fund should fulfill its tasks in the area of macroeconomic policy coordination. However, this separation is difficult given the fact that structural policies, institutional and political reform, and development processes are intrinsically connected to macroeconomic adjustment.

In order to assist institution building within emerging countries and to support private-sector capital flows in this part of the world, the IMF must concentrate on its role as a crisis manager in anticipation. This requires stronger surveillance through continuous and more candid dialogues with member countries and the closer monitoring of data. "The world community would gain by using the Fund as the principal forum for multilateral surveillance and coordination of national fiscal and monetary policies" (Singh 1995, p. 38). The Fund must develop a set of standards to guide member governments in publishing economic and financial data on their own and to keep markets better informed. This is to provide the discipline needed to ensure a systematic review of economic developments; it provides an opportunity for governments to deliver collective advice; and it permits markets to make informed decisions and perform its role more efficiently. Also financial market supervision and regulation would have to be strengthened both at the national and the international level.

### ***Infrastructure***

As to infrastructure development, the World Bank performs a key role in assisting structural adjustments to render markets more responsive to change and to enhance economic welfare. In recent times, this has been particularly important in the context of transforming the formerly socialist economies. Continuing widespread poverty in many countries, population growth and pressing environmental problems all pose major development challenges. Thus, the case for a major role for the World Bank is strong and even more acute. Together with regional development banks, it plays a key part in promoting sustainable social and economic development.

However, the Bank will have to narrow its focus on cofinancing public goods for which private resources are difficult to mobilize. This is not at odds with the present philosophy of the Bank, which tends to foster private sector developments and to mobilize resources for poverty reduc-

tion through markets. The end of the Cold War will permit the World Bank to avoid misallocation of resources through political concessions, and to insist, instead, on harsher conditionality and to concentrate on projects with a high social rate of return. The Bank is now in a better position to decline lending to governments that lack commitment in reducing poverty, that violate human rights or misallocate resources for military oppression and corruption. The Bank will have to place the emphasis on supporting primary education and health, and on the protection of the environment. Moreover, the Bank must assume a key role in coordinating international development projects among major donor countries and multilateral institutions. And the Bank should decentralize its operations wherever possible without losing the coherent framework of its general policy out of sight. This will enhance its effectiveness and foster democratic participation.

The global trend in the world economy also requires the World Bank and the International Monetary Fund to catalyze greater private sector involvement. This means, *inter alia*, that the work of the IFC and MIGA has to be integrated more strongly in their programs. Non-government institutions and new public-private arrangements will offer new chances to realize development projects with greater participation of beneficiaries and the private sector while assuring adequate risk-sharing between public and private lenders. A change in the Statutes of the Bank may also have to be considered which now restrict operations to those whose sovereign risks are fully guaranteed. In a world in which some countries have emerged from underdevelopment, others are freed from the yoke of totalitarianism, it seems to be perverse that the Bank has to refrain from business with these potentially more dynamic regions whenever these that ask for some risk-sharing, while it would have to concentrate on the poorer, albeit riskier, countries which assume a full bail-out guarantee of little value.

However, there will be a continuing need for poverty alleviation in a globalizing world. The main instrument for this purpose is the enhanced structural adjustment facility (ESAF) of the International Monetary Fund that provides conditioned assistance for growth-oriented adjustment programs in low-income countries. This facility was recently extended and enlarged, and a self-sustaining facility will be put in place. This constitutes a decisive improvement in the plight of poor countries. It is an irony, however, that the financing of IDA as the suborganization with the heaviest impact on alleviating poverty is constantly at risk and that major contributors, like the United States, fail to honor their commitments. Official development assistance of industrialized countries, multilateral and bilateral, is now less than 0.3 percent of GDP, at the lowest level since 1973, a trend that should be reversed.

Increasing demands on the Bretton Woods institutions resources will also require a strengthening of the financial basis for multilateral action in a globalizing world. While there are initiatives to develop new parallel financing arrangements by the Group of Ten and selected other countries with the aim of doubling the credit lines available under the General Agreement to Borrow (GAB) of the Fund, this measure is likely to be insufficient and not a substitute for an increase in quota. The fiftieth Annual Meeting of the International Monetary Fund and the World Bank of October 1995 has endorsed an emergency financing mechanism in order to enable the IMF to respond rapidly—with sizable front-loaded financing—to deal with potential Mexico-style crises. It also supported currency stabilization funds on a short-term basis for confidence building, and to expand the scope of emergency assistance in post-conflict situations. In 1997 the IMF quota have been increased again, but in view of the more recent turbulence in South-East-Asian financial markets, it is doubtful whether the scope for emergency funding is sufficiently large. In particular short-term events such as those observed in foreign currency and other asset markets that require temporary multilateral interventions that may put longer-term infrastructure developments in other parts of the world at risk.

## **Integration**

While institution-building and infrastructure development is mainly a responsibility of governments of transition and developing nations themselves, where foreign assistance can only be subsidiary, integration requires active participation of Western nations as well as the political will to cooperate with formerly socialist and developing countries. It is there where Marshall's spirit of partnership and mutual respect, of cooperation and concertation is imperative. Political and economic integration is the paramount device in the search for 'creative peace' under modern conditions. It offers a platform for solving international conflicts through deliberation and negotiation, and it has the potential to enhance welfare through the arbitration of opportunities that are mutually beneficial to consumers and producers. It also leads to the forming of a network of political, cultural, commercial and personal relations that will ultimately conduct to a better understanding among individuals and agencies, and thus consolidate peace.

At the political level, the Organization for Security and Cooperation in Europe, NATO's 'Partnership for Peace', the Group of Eight, the Council of Europe, and many other multilateral bodies and institutions now take a cooperative approach to a wide range of issues—which they try to achieve through preventive diplomacy, confidence and security building measures, arms control, economic policy concertation, the exchange of information and technical assistance, democratic and economic institution-building, election monitoring, and so forth. The extension of NATO is an important approach to political integration of the formerly socialist world, which can only be successful if combined with confidence and security building.

At the economic level, the expansion of trade with transition and developing countries is mandatory in order to help them overcome their balance-of-payment problems and to foster their reinsertion into the world economy. This requires, *inter alia*, a revision of the hitherto protectionist attitudes in some sectors of the economy such as agriculture where the comparative advantages are clearly on the side of countries like Poland, Romania, Bulgaria, and the Third World. A new round of WTO-negotiations will have to settle such problems, but this could be too slow a process for integrating Central and Eastern European countries into the world economy rapidly enough, and some immediate political action is required. The European Union and its agricultural policy play a key role in this context. Although there are first indications of a change in attitudes, much remains to be accomplished. Official statements such as "The World Trade Organization's rules, and the prospect of international WTO negotiations in 1999, mean that the Union must be in a position to defend its interests from a position of strength"<sup>10</sup> do not augur well in this respect.

Fostering trade with Central and Eastern European countries is just one element of a new type of creative peace policy. The decisive step will, of course, have to be the enlargement of the European Union and the acceptance of full membership, mutual respect and full recognition of sovereignty and individual freedom among nations in this part of the world. As in the days of Marshall, shared responsibilities and collaboration among governments and institutions are the ultimate test for partnership in a Europe that has finally come to overthrow the legacies of communism and of World War II.

## **Conclusions**

The Marshall Plan was a success at its time and it had significant portent beyond its immediate financial impact—which may be questioned. The Plan stressed the positive relationship between economic and political stability; it emphasized the free play of the market and the liber-

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<sup>10</sup> See "The Commission's Work Programme for 1998: The political priorities", in <http://europa.eu.int/comm/opoce/indexfr.htm> (December 1997).



alization of international trade; it fostered dialogue and cooperation; it married foreign policy objectives, political stability and economic recovery; it created a forum for mutual consultation and cooperation among industrialized countries; and it raised the morale of European citizens turning wide-spread pessimism into purposeful actions. These are its main outcomes that go well beyond finance.

In the light of such historical experience, the quest for a new Marshall Plan directed toward the formerly socialist and developing countries is understandable, but it neglects the fact that the world economy has dramatically changed during the last half of a century. Moreover, the specific conditions that initially prevailed in transition countries would have made such a program rather dubious. Unconditional funds to Central and Eastern European countries would have evaporated without notable results because political and administrative institutions were and are weak, the organization of production and distribution is inadequate, and the legal framework for economic operations is fragile. The lack, in these countries, of an institutional framework to support market forces and initiatives is likely to have rendered financial aid ineffective. Also good governance is needed (and often lacking) for a successful transition process. Good governance must involve openness, transparency and credibility as well as the absence of bureaucratic interference and corruption.

The most important prerequisites for successful transformation and development are institution building, infrastructure, and integration. Institution building implies the democratization of society in order to have citizens participate in public-decision making and to set up necessary control mechanisms. Infrastructure development is needed to assist structural adjustment, to render markets more responsive to change, and to enhance economic welfare. Political and economic integration of transition and developing countries is the paramount device in the search for 'creative peace' under modern conditions.

While institution-building and infrastructure development is mainly the responsibility of governments of transition and developing nations themselves, integration requires active participation of Western nations as well as the political will to cooperate with formerly socialist and developing countries. It is there where Marshall's spirit of partnership and mutual respect, of cooperation and concertation is still meaningful. Marshall's legacy is his vision, not so much a program that was appropriate for post-war Europe. 'Creative peace' today exacts politicians to draw on Marshall's imagination and to design new programs in his spirit if they want to pass the test of history—as Marshall did indeed.

Let me conclude with the words of President Bill Clinton in The Hague earlier this year:

"Now, the dawn of new democracies is lighting the way to a new Europe in a new century—a time in which America and Europe must complete the noble journey that Marshall's generation began, and this time with no one left behind." (President Bill Clinton, at a commemorative event for the 50<sup>th</sup> anniversary of the Marshall Plan, in the Hall of Knights, Binnenhof, The Hague, Netherlands, May 28, 1997.)

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