Volume III of *The Cambridge History of the Cold War* examines the evolution of the conflict from the Helsinki Conference of 1975 until the Soviet collapse in 1991. A team of leading scholars analyzes the economic, social, cultural, religious, technological, and geopolitical factors that ended the Cold War and discusses the personalities and policies of key leaders such as Brezhnev, Reagan, Gorbachev, Thatcher, Kohl, and Deng Xiaoping. The authors show how events throughout the world shaped the evolution of Soviet–American relations and they explore the legacies of the superpower confrontation in a comparative and transnational perspective. Individual chapters examine how the Cold War affected and was affected by environmental issues, economic trends, patterns of consumption, human rights, and non-governmental organizations. The volume represents the new international history at its best, emphasizing broad social, economic, demographic, and strategic developments while keeping politics and human agency in focus.

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vi
The world economy and the Cold War, 1970–1990

GIOVANNI ARRIGHI

The 1970s began with the collapse of the gold-dollar exchange standard and the defeat of the United States in Vietnam – two events that jointly precipitated a ten-year-long crisis of US hegemony. The 1980s, in contrast, ended with the terminal crisis of the Soviet system of centrally planned economies, US “victory” in the Cold War, and a resurgence of US wealth and power to seemingly unprecedented heights. The key turning point in this reversal of fortunes was the neoliberal (counter)revolution of the early 1980s orchestrated by President Ronald Reagan and Prime Minister Margaret Thatcher. The purpose of this chapter is to highlight the relationship between this turning point and the preceding crisis of US hegemony on the one side and the subsequent collapse of the USSR on the other.

The crisis of US hegemony and the onset of global turbulence

US hegemony in the Cold War era was based on institutional arrangements that originated in the widespread belief among US government officials during World War II that “a new world order was the only guarantee against chaos followed by revolution” and that “security for the world had to be based on American power exercised through international systems.”

Equally widespread was the belief that the lessons of the New Deal were relevant to the international sphere: “Just as the New Deal government increasingly took active responsibility for the welfare of the nation, US foreign-policy planners took increasing responsibility for the welfare of the

world.” To take responsibility, of course, “meant government intervention on a grand scale.”

In Franklin D. Roosevelt’s original vision, the New Deal would be “globalized” through the United Nations, and the USSR would be included among the poor nations of the world to be incorporated into the evolving Pax Americana, for the benefit and security of all. In the shoddier but more realistic political project that materialized under Harry S. Truman, in contrast, the containment of Soviet power became the main organizing principle of US hegemony, and US control over world money and military power became the primary means of that containment. This more realistic model was not so much a negation of the original notion of creating a global welfare state as its transformation into a project of creating a “warfare–welfare state” on a world scale, in competition with and in opposition to the Soviet system of Communist states.

Neither the economic boom of the 1950s and 1960s nor the subsequent long downturn can be understood except with reference to the successes and failures of this project. The boom was launched and sustained through the joint operation of both military and social Keynesianism on a world scale. Military Keynesianism – that is, massive expenditures on the rearmament of the United States and its allies and the deployment of a farflung network of quasi-permanent military bases – was undoubtedly the most dynamic and conspicuous element of the combination. But the US-sponsored spread of social Keynesianism – that is, the governmental pursuit of full employment and high mass consumption in the First World and of “development” in the Third World – was also an essential factor.

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The reconstruction and upgrading of the German and Japanese economies were integral aspects of the internationalization of the US warfare–welfare state. As Bruce Cumings notes, “George Kennan’s policy of containment was always limited and parsimonious, based on the idea that four or five industrial structures existed in the world: the Soviets had one and the United States had four, and things should be kept this way.” The upshot in East Asia was US sponsorship of Japanese reindustrialization. The Korean War became “Japan’s Marshall Plan . . . War procurement propelled Japan along its war-beating industrial path.” US promotion of the reconstruction and upgrading of the German industrial apparatus occurred through different but equally effective channels. Germany was, of course, among the main beneficiaries of the Marshall Plan and US military expenditures abroad. But the most important contribution was US sponsorship of West European economic union. As future secretary of state John Foster Dulles declared in 1948, “a healthy Europe” could not be “divided into small compartments.” It had to be organized into a market “big enough to justify modern methods of cheap production for mass consumption.” A reindustrialized Germany was an essential component of this new Europe.

The “catching-up” of latecomers with the technological and organizational achievements of the leading capitalist state – “uneven development,” in Robert Brenner’s characterization of the process – was thus consciously and actively encouraged by the leader itself, rather than merely the result of the latecomers’ actions, as it had been in the nineteenth century. This peculiarity accounts not just for the speed and extent of the post-World War II boom, but also for its transformation into the relative stagnation of the 1970s and 1980s. The capacity of Japan, Germany, and other West European countries to combine the high-productivity technologies pioneered by the United States with the large, low-wage, and elastic labor supplies employed in their comparatively backward rural and small business sectors pushed up their rate of investment and economic growth. Through the early 1960s, this tendency benefited the United States as well because the rapid economic expansion of Western Europe and Japan created profitable outlets for US multinationals


7 Quoted in McCormick, America’s Half Century, 79–80.
and banks, new export opportunities for domestically based US firms, and ideological resources for the US government in the Cold War. “Uneven development” was thus a positive-sum game that buttressed “a symbiosis, if a highly conflictual and unstable one, of leader and followers, of early and later developers, and of hegemon and hegemonized.”

By the mid-1960s, however, Germany and Japan had not just caught up with but had forged ahead of the United States in one industry after another — textiles, steel, automobiles, machine tools, consumer electronics. More important, the newer, lower-cost producers based in these and other follower countries began invading markets hitherto dominated by US producers. As a result of this influx of lower-priced goods into the United States and world markets, between 1965 and 1973 US manufacturers experienced a decline of over 40 percent in the rate of return on their capital stock. Their response to this intensification of competition included pricing products below full cost, repressing the growth of wage costs, and updating their plant and equipment. But, in Brenner’s view, the most effective US weapon in the incipient competitive struggle was the devaluation of the US dollar against the German mark (by a total of 50 percent between 1969 and 1973) and the Japanese yen (by a total of 28.2 percent between 1971 and 1973). Thanks to this massive devaluation, profitability, investment growth, and labor productivity in US manufacturing staged a comeback, restoring the US trade balance to a surplus, while the competitiveness of German and Japanese manufacturers was sharply curtailed. The global crisis of profitability was not overcome, but its burden was distributed more evenly among the main capitalist countries.

The intensification of intercapitalist competition that ensued from the US-sponsored reconstruction and upgrading of the West European and Japanese economies was not the only cause of the crisis of profitability. Equally important was US support for full-employment policies and the spread of high mass consumption both at home and throughout the First World. While consolidating the hegemony of liberal capitalism, this variant of social Keynesianism strengthened the capacity of workers to seek a greater share of the social product. This empowerment of labor culminated in what E. H. Phelps Brown aptly called the “pay explosion” of 1968–73. Coming in the wake of twenty years of rising real wages in the core regions of the global economy, the pay explosion supplemented the intensification

of intercapitalist competition in exercising a system-wide downward pressure on profitability.\textsuperscript{10}

Washington’s Cold War policies thus put a double squeeze on profits: through the intensification of intercapitalist competition, which US actions encouraged by creating conditions favorable to the upgrading and expansion of the Japanese and West European productive apparatuses; and through the social empowerment of labor, which Washington promoted through the pursuit of near full employment and high mass consumption throughout the Western world. This double squeeze was bound to produce a system-wide crisis of profitability, but was not in itself a sufficient reason for the crisis of US hegemony which became the dominant event of the 1970s. What turned the crisis of profitability into a broader hegemonic crisis was the failure of the US warfare–welfare state to attain its social and political objectives in the Third World.

Socially, the “Fair Deal” that Truman promised to the poor countries of the world in his 1949 inaugural address never materialized in an actual narrowing of the income gap that separated them from the wealthy countries of the West. As Third World countries stepped up their industrialization efforts (industrialization being the generally prescribed means to “development”), there was indeed industrial convergence with First World countries; but there was virtually no income convergence. Third World countries were thus bearing the costs without reaping the expected benefits of industrialization (see Table 1).\textsuperscript{11}

Far more conspicuous was the political failure of the US warfare–welfare state. Its epicenter was the war in Vietnam, where the United States was unable to prevail, despite the deployment of military hardware and firepower on a scale without precedent for a conflict of this kind. As a result, the United States lost much of its political credibility as global policeman, thereby emboldening the nationalist and social revolutionary forces that Cold War policies were meant to contain.

Along with much of the political credibility of its military apparatus, the United States also lost control of the world monetary system. The escalation of


Table 1. Third World GNP per capita as a percentage of the First World’s GNP per capita

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<tr>
<td>Sub-Saharan Africa (with South Africa)</td>
<td>4.7</td>
<td>3.9</td>
<td>3.1</td>
<td>2.7</td>
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<tr>
<td>Latin America</td>
<td>16.4</td>
<td>17.6</td>
<td>14.4</td>
<td>12.3</td>
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<tr>
<td>West Asia and North Africa</td>
<td>7.8</td>
<td>8.7</td>
<td>7.9</td>
<td>7.4</td>
</tr>
<tr>
<td>South Asia (without India)</td>
<td>1.7</td>
<td>1.3</td>
<td>1.4</td>
<td>1.4</td>
</tr>
<tr>
<td>East Asia (without China and Japan)</td>
<td>6.1</td>
<td>8.0</td>
<td>8.6</td>
<td>11.0</td>
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<tr>
<td>China</td>
<td>0.7</td>
<td>0.8</td>
<td>1.2</td>
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<td>India</td>
<td>1.3</td>
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<td>Third World</td>
<td>4.0</td>
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<td>4.1</td>
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<tr>
<td>Third World (without China)</td>
<td>5.7</td>
<td>6.1</td>
<td>5.5</td>
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<tr>
<td>Third World (without China and India)</td>
<td>8.1</td>
<td>8.8</td>
<td>7.7</td>
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<tr>
<td>North America</td>
<td>105.0</td>
<td>100.7</td>
<td>101.6</td>
<td>98.2</td>
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<tr>
<td>Western Europe</td>
<td>104.6</td>
<td>104.6</td>
<td>101.5</td>
<td>100.5</td>
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<tr>
<td>Southern Europe</td>
<td>58.2</td>
<td>60.0</td>
<td>57.6</td>
<td>58.6</td>
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<tr>
<td>Australia and New Zealand</td>
<td>83.5</td>
<td>74.7</td>
<td>73.3</td>
<td>66.4</td>
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<tr>
<td>Japan</td>
<td>126.4</td>
<td>134.4</td>
<td>140.8</td>
<td>149.8</td>
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<td>First World</td>
<td>100</td>
<td>100</td>
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<td>Eastern Europe</td>
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<td>11.1</td>
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<td>Former USSR with Russian Federation</td>
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<td>Russian Federation</td>
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<td>Former USSR without Russian Federation</td>
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<td>7.1</td>
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<tr>
<td>Eastern Europe and former USSR</td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>10.8</td>
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Note: GNP in constant 1995 US dollars. Countries included in the Third World: Africa (except Angola, Libya, Mozambique, Guinea, Guinea-Bissau, Mali, and Swaziland), Latin America (except Cuba), West Asia (except Saudi Arabia, Syria, Turkey), South Asia (except Afghanistan and Bhutan), and East Asia (except Burma, Cambodia, Laos, Vietnam, North Korea, and Japan).


Public expenditures to sustain the military effort in Vietnam and to overcome opposition to the war at home – through the Great Society program – strengthened inflationary pressures, deepened the fiscal crisis of the US state, and eventually led to the collapse of the US-centered Bretton Woods regime of fixed exchange rates. Crucial in this respect was the explosive growth of the eurodollar and other extraterritorial financial markets.

Established in the 1950s to hold dollar balances of Communist countries unwilling to risk depositing them in the United States, the eurodollar market grew primarily through the deposits of US multinationals and the offshore activities of New York banks. Having expanded steadily through the 1950s and
early 1960s, it started growing exponentially in the mid- and late 1960s – eurocurrency assets more than quadrupling between 1967 and 1970.\textsuperscript{12} Hard as it is to know exactly what lay behind this explosion, it is plausible to suppose that it was triggered by the crisis of profitability of those years. Declining rates of profit under the impact of intensifying competition and growing labor demands must have boosted the liquidity preference of US multinational corporations operating in Europe. Since conditions for the profitable reinvestment of cash flows were even less favorable in the United States than in Europe, it made good business sense for the multinationals to “park” their growing liquid assets in eurocurrency and other offshore money markets rather than repatriate them.

The explosive growth of eurocurrency markets provided currency speculators – including US banks and corporations – with a huge \textit{mass de manoeuvre} with which to bet against, and thereby undermine, the stability of the US-controlled system of fixed exchange rates. And once that system actually collapsed, fluctuations in exchange rates became a major determinant of variations in corporate cash-flow positions, sales, profits, and assets in different countries and currencies. In hedging against these variations, or in trying to profit from them, multinationals tended to increase the monetary resources deployed in financial speculation in extraterritorial money markets where freedom of action was greatest and specialized services were most readily available.\textsuperscript{13}

It follows that the massive devaluation of the US currency of the early 1970s was not just, or even primarily, the result of a conscious US policy aimed at shifting the burden of the crisis of profitability from US to foreign business. It was also and especially the unintended consequence of lax US monetary policies aimed at sustaining the military effort in Vietnam on the one side, and of the actions of US multinationals and financial speculators aimed at profiting from the fiscal crisis of the US warfare–welfare state on the other. Combined with the loss of credibility of US military power, the massive devaluation of the dollar in turn prompted Third World governments to adopt a more aggressive stance in negotiating the prices of their exports of industrial raw materials – oil in particular. Intensifying intercapitalist competition and the stepping up of low- and middle-income countries’ industrialization efforts


had already led to significant increases in raw-material prices before 1973. In 1973, however, the virtual acknowledgment of defeat by the US government in Vietnam, followed immediately by the shattering of the myth of Israeli invincibility during the Yom Kippur War, energized the Organization of Petroleum Exporting Countries (OPEC) into protecting its members more effectively from the depreciation of the dollar through a fourfold increase in the price of crude oil in a few months. Coming as it did at the tail end of the pay explosion, this so-called oil shock deepened the crisis of profitability and strengthened inflationary tendencies in core capitalist countries. At the same time, it generated an $80 billion surplus of dollars in the hands of oil-exporting countries (so-called petrodollars), a good part of which was parked or invested in the eurocurrency and other offshore money markets. The mass of privately controlled liquidity that could be mobilized for financial speculation and new credit creation outside publicly controlled channels thereby received a powerful additional stimulus.\textsuperscript{14}

The tremendous expansion in the supply of world money and credit, engendered by the combination of extremely lax US monetary policies and the explosive growth of privately controlled liquidity in offshore money markets, was not matched by demand conditions capable of preventing the devaluation of money capital. To be sure, there was plenty of demand for liquidity, not only on the part of multinational corporations – to hedge against or speculate on exchange-rate fluctuations – but also on the part of low- and middle-income countries to sustain their developmental efforts in an increasingly competitive and volatile environment. For the most part, however, this demand added more to inflationary pressures than it did to the expansion of solvent indebtedness:

Formerly, countries other than the United States had to keep their balance of payments in some sort of equilibrium. They had to “earn” the money they wished to spend abroad. Now . . . [c]ountries in deficit could borrow indefinitely from the magic liquidity machine . . . Not surprisingly, world inflation continued accelerating throughout the decade, and fears of collapse in the private banking system grew increasingly vivid. More and more debts were “rescheduled,” and a number of poor countries grew flagrantly insolvent.\textsuperscript{15}

In short, the interaction between the crisis of profitability and the crisis of hegemony, in combination with lax US monetary policies, resulted in increasing


\textsuperscript{15} David Calleo, \textit{The Imperious Economy} (Cambridge, MA: Harvard University Press, 1982), 137–38.
world monetary disorder, escalating inflation, and steady deterioration in the capacity of the US dollar to function as the world’s means of payment, reserve currency, and unit of account. From 1973 to 1978, the abandonment of the gold–dollar exchange standard appeared to have resulted in the establishment of a de facto pure dollar standard that enabled the United States to tap the resources of the rest of the world virtually without restriction, simply by issuing its own currency. By 1978, however, the threat of an imminent demise of the US dollar as world money had become quite real. When on October 6, 1979, the chairman of the US Federal Reserve, Paul Volcker, began taking forceful measures to restrict the supply of dollars and to bid up interest rates in world financial markets, he was responding to a crisis of confidence that threatened to deteriorate into a collapse of the dollar, perhaps leading to a financial crisis and pressure to remonetize gold, against which the United States had fought doggedly for over a decade. And when a few months later the flight of hot Arab money into gold in the wake of the Iranian crisis and the Soviet invasion of Afghanistan pushed the price of gold to a high of $875, Volcker took even harsher measures to stop the growth of the US and global money supply.

The neoliberal (counter)revolution and the end of the Cold War

Volcker’s switch from highly permissive to highly restrictive monetary policies in the last year of the administration of Jimmy Carter was the harbinger of the abandonment under Reagan of the ideology and practice of the New Deal, nationally and internationally. Drawing ideological inspiration from Thatcher’s slogan “There Is No Alternative” (TINA), the Reagan administration declared all variants of social Keynesianism obsolete and proceeded to liquidate them through a revival of early twentieth-century beliefs in the “magic” of allegedly self-regulating markets. The liquidation began with a

drastic contraction in money supply and an equally drastic increase in interest rates, followed by major reductions in corporate taxation and the elimination of controls on capital. The immediate result was a deep recession in the United States and in the world at large and a simultaneous escalation of interstate competition for capital worldwide.

TINA was thereby turned into a self-fulfilling prophecy. Whatever alternative to cutthroat competition for increasingly mobile capital might have existed before 1980, it became moot once the world’s largest and wealthiest economy led the world down the road of ever more extravagant concessions to capital. This was especially the case for Second and Third World countries which, as a result of the change in US policies, experienced a sharp contraction both in the demand for their natural resources and in the availability of credit and investment on favorable terms. It was in this context that the liquidation of the legacy of the welfare state in the United States and other First World countries was supplemented by a sudden switch of US policies toward the Third World. The focus shifted from the promotion of the “development project” launched in the late 1940s and early 1950s to the promulgation of the neoliberal agenda of the so-called Washington Consensus. Directly or through the International Monetary Fund and the World Bank, the US government withdrew its support from the “statist” and “inward-looking” strategies (such as import-substitution industrialization) that most theories of national development had advocated in the 1950s and 1960s and began instead to promote capital-friendly and outward-looking strategies, most notably macrostability, privatization, and the liberalization of foreign trade and capital movements.19

The change has been referred to as a “counterrevolution” in economic thought and political ideology.20 This characterization of the neoliberal turn contrasts with its promoters’ preference for the term “revolution.” In reality, as the expression “neoliberal (counter)revolution” is meant to convey, the phenomenon was counterrevolutionary in the intended consequences but revolutionary in the unintended ones. To focus for now on intended consequences,

the counterrevolutionary thrust of the neoliberal turn was evident not only on issues of economic development in the Third World, but also in its attempt to reverse the empowerment of labor that had occurred in First World countries in the 1950s and 1960s.

The slowdown of economic growth and escalating inflation of the 1970s had already eroded the capacity of workers in the United States and other core countries to resist encroachments upon their working and living conditions. But their leverage collapsed only with the Reagan administration’s liquidation of the New Deal. Beginning with the deep recession of 1979–82, pressure on profits emanating from workers’ demands in core countries subsided. As Thatcher’s adviser Alan Budd admitted in retrospect, “What was engineered in Marxist terms was a crisis of capitalism which re-created a reserve army of labor, and has allowed the capitalists to make high profits ever since.” The maneuver was especially successful in the United States, as Volcker’s successor at the helm of the US Federal Reserve, Alan Greenspan, pointed out when he attributed the higher profits and greater increases in productivity of US companies to Japan’s and Europe’s “relatively inflexible and, hence, more costly labor markets.” “Because our costs of dismissing workers are lower,” he explained, “the potential costs of hiring and the risks associated with expanding employment are less.”

The success of the neoliberal (counter)revolution in disempowering labor did contribute to the revival of US profitability in the 1990s, but it was not the key factor that pulled the US economy out of the deep recession of the early 1980s and propelled it towards renewed expansion in the 1990s. Far more decisive was what Brenner calls the “fortuitous” return of Keynesianism. Reagan’s “monumental programme of military spending and tax reduction for the rich . . . partly offset the ravages of monetarist tight credit and kept the economy ticking over.” This socially regressive Keynesianism brought back budget, trade, and current account deficits with a vengeance. In contrast to the 1970s, however, instead of precipitating a run on the dollar and increasing monetary disorder, even larger US deficits in the 1980s led to a sharp appreciation of the US currency and to the establishment of a long-lasting pure dollar standard.

This different outcome of Reaganite Keynesianism can be traced in part to the taming of labor. On the whole, however, it reflected the fact that the

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neoliberal turn promoted a major reorientation of the US economy to take full advantage of the ongoing financial expansion of capital at home and abroad. As previously noted, in the 1970s a growing competition between lax US monetary policies and mechanisms of private interbank money creation set an increasingly large group of countries free from balance-of-payments constraints, thereby undermining Washington’s seigniorage privileges while feeding offshore money markets with more liquidity than private capital could possibly invest safely and profitably. Unfolding in conjunction with the deepening crisis of US hegemony, this mutually destructive competition between US private and public money culminated in the devastating run on the dollar of 1979–80. Whatever the actual motivations and ostensible rationale of the sudden reversal in US monetary policies that followed the run, its true long-term significance—and the main reason why it eventually revived US fortunes beyond anyone’s expectations—is that it brought this mutually destructive competition to an abrupt end. Not only did the US government stop feeding the system with liquidity; more importantly, it started competing aggressively for capital worldwide—through record high interest rates, tax breaks, increasing freedom of action for capitalist producers and speculators, and, as the benefits of the new policies materialized, an appreciating dollar—prompting a massive rerouting of global capital flows toward the United States.

The extent of the rerouting can be gauged from the change in the current account of the US balance of payments. In the five-year period 1965–69, the account had a surplus of $12 billion, which constituted almost half (46 percent) of the total surplus of G7 countries. In 1970–74, the surplus contracted to $4.1 billion and to 21 percent of the total surplus of G7 countries. In 1975–79, the surplus turned into a deficit of $7.4 billion. After that, the deficit escalated to the previously unimaginable levels of $146.5 billion in 1980–84 and $660.6 billion in 1985–89 (see graph 1).24

This massive redirection of capital flows toward the United States had devastating effects on the Third and Second World countries that in the 1970s had been lured, to paraphrase David Calleo, the economic historian, into borrowing “indefinitely from the magic liquidity machine.” When the United States reversed its monetary policies and started to compete aggressively in world financial markets, the “flood” of capital of the 1970s turned into the “drought” of the 1980s. Suffice it to say that the success of the

24 Calculated from International Monetary Fund, International Financial Statistics Yearbook (Washington, DC: International Monetary Fund, various years). Leaving aside “errors and omissions,” current account surpluses are indicative of net outflows of capital, and current account deficits are indicative of net inflows.
United States in attracting capital turned the $46.8 billion outflow of capital from G7 countries of the 1970s (as measured by their consolidated current account surpluses for the period 1970–79) into an inflow of $347.4 billion in 1980–89. First signaled by the Mexican default of 1982, the drought created a propitious environment for the counterrevolution in development thought and practice that the neoliberal Washington Consensus began advocating at about the same time. Taking advantage of the financial straits of many low- and middle-income countries, the agencies of the consensus foisted on them measures of “structural adjustment” that did nothing to improve their position in the global hierarchy of wealth but greatly facilitated the redirection of capital flows toward sustaining the revival of US wealth and power.

The impact of the neoliberal (counter)revolution on the Third World was far from uniform. Some regions (most notably East Asia) succeeded in taking advantage of the increase in US demand for cheap industrial products that ensued from US trade liberalization and the escalating US trade deficit. As a result, their balance of payments improved, their need to compete with the United States in world financial markets lessened, and indeed East Asian countries became major lenders to the United States. Other regions (most notably Latin America and sub-Saharan Africa), in contrast, did not manage to compete successfully for a share of the North American demand. These regions tended to run into balance-of-payments difficulties, which put them in the hopeless position of having to compete directly with the United States in world financial markets. The overall result was that between 1980 and 1990 the income per capita of East Asia (including China and Southeast Asia but excluding Japan) relative to that of the First World increased by almost 40 percent, while that of sub-Saharan Africa and Latin America decreased by about 30 percent.  

I shall later discuss the conditions that enabled East Asian countries to turn the neoliberal (counter)revolution to their advantage. For now, however, it is important to emphasize that the change in the conjuncture of the global political economy precipitated by the neoliberal turn contributed decisively to the terminal crisis of the Soviet system of centrally planned economies. Standard accounts of the crisis focus on the internal dynamic of these economies, emphasizing their tendency to privilege quantity over quality in economic production and social provision. As long as massive inputs of labor and natural resources could be channeled toward the building of a heavy-industry economy, central planning generated rates of economic growth among the highest in the world. But once labor and natural resources became more fully utilized, and further growth more dependent on growing productivity, central planning became increasingly anachronistic. Worse still, attempts to spur productivity by stepping up investments in human capital further

27 The G7 is the group of seven major industrialized countries: Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States. The exact percentages are +38.5 for China, +38.7 for the rest of East Asia (excluding Japan), −30.6 for sub-Saharan Africa, and −30.1 for Latin America. Less extreme were the changes for West Asia and North Africa (−14.9) and for South Asia (+8.3). All percentages have been calculated from data provided in World Bank, World Development Indicators (Washington, DC: World Bank, 2001). For details on the countries included in each region, see Giovanni Arrighi, "Globalization and Uneven Development," in I. Rossi (ed.), Frontiers of Globalization Research: Theoretical and Methodological Approaches (New York: Springer, 2007), table 2, 191.

28 See Richard N. Cooper’s and Wilfried Loth’s chapters in volume II.
undermined the political legitimacy of a system that was more and more incapable of delivering on its promises of a quality of life superior to the Western one.29

Arguments of this kind are useful in highlighting factors that undoubtedly contributed to the terminal crisis of the Soviet system of centrally planned economies. They nonetheless obscure the fact that, despite its superpower status and the success of its modernization efforts, throughout the Cold War era the USSR occupied a position in the global hierarchy of wealth very similar to that of Latin American countries. Lack of data makes comparisons difficult for the period under consideration, but a fairly reliable source for an earlier period put the GNP per capita of the USSR at 25.2 percent of that of the wealthier countries of the West in 1938 and at 18.3 percent in 1948. These figures were almost exactly the same as those for Latin America (23.8 percent in 1938 and 16.2 percent in 1948) and for Hungary and Poland combined (26.7 percent in 1938 and 18.4 percent in 1948). Half a century later, on the eve of the collapse of the Soviet system, the situation had apparently not changed except for a further widening of the income gap vis-à-vis the wealthy countries of the West. Although there are no comparable figures for the USSR itself, the corresponding figure for Hungary and Poland combined in 1988 was 11.1 percent and for Latin America 10.6 percent.30

Assuming that the economic performance of the USSR between 1948 and 1988 was not very different from that of Poland and Hungary, the above


30 Figures for 1938 and 1948 have been calculated from data provided in W. S. Woytinsky and E. S. Woytinsky, World Population and Production: Trends and Outlook (New York: Twentieth Century Fund, 1953), and figures for 1988 from World Bank, World Development Report (Washington, DC: World Bank, 1990). The figures are percentages of the weighted average per capita income of Australia, Austria, Canada, France, (West) Germany, New Zealand, Switzerland, the United Kingdom, United States, and the Benelux and Scandinavian countries. The Latin American aggregate includes Argentina, Bolivia, Chile, Colombia, Dominican Republic, Ecuador, El Salvador, Jamaica, Mexico, Paraguay, Peru, and Venezuela. The figures are based on current exchange rates (FX) calculations. If they had been based on purchasing power parity (PPP) calculations, the percentages would have been higher. The choice of FX-based data is justified by their greater validity than PPP-based data as indicators of relative command over world economic resources. For a discussion of the criteria used in the choice of the aggregates and of the data, see Giovanni Arrighi, “World Income Inequalities and the Future of Socialism,” New Left Review, 1, 189 (1991), 39–65.
figures suggest that the economic position and trajectory of the Soviet system of centrally planned economies in the Cold War era was strikingly similar to those of a Third World region like Latin America. Despite their radically different political and economic regimes, not only did they occupy the same position in the global hierarchy of wealth, but they also lost about the same ground with respect to the upper echelons of the hierarchy. There was, of course, a fundamental difference in the status and power of the two regions in the Cold War era: Latin America was a politically subordinate and militarily insignificant domain of US hegemony, while the Soviet system of states had sufficient political and military power to limit and constrain the global reach of that hegemony. Over time, however, the capacity of the Soviet system to keep up politically and militarily with the US system was bound to be seriously restricted by the increasing income gap that separated the two systems.

The problem was not so much that, following Kennan’s advice, the United States had succeeded in retaining within its domains four of the world’s five main industrial core areas. As previously noted, in the Cold War era there had been considerable industrial convergence between lower- and higher-income countries. The problem was that industrial convergence with the high-income countries of the First World was not accompanied by income convergence, so that Second World countries, no less than Third World countries, had to bear the costs without reaping the expected benefits of industrialization. The nature of the predicament was nowhere more evident than in the armaments race on which much of the credibility of Soviet prestige and power had come to rest.

There is in this regard a close, if little noticed, parallel between the armaments race in the Cold War era and that between Britain and France in the nineteenth century. As William McNeill has pointed out, from the mid-1840s through the 1860s, most technological breakthroughs in the design of warships were pioneered by France. And, yet, each French breakthrough called forth naval appropriations in Britain that France could not match, so that it was “relatively easy for the Royal Navy to catch up technically and surpass numerically each time the French changed the basis of the competition.”

This pattern of the nineteenth-century armaments race shows that control over the world’s financial resources can provide a more decisive competitive advantage than leadership in technological innovation. This possibility was confirmed in the Cold War competition between the United States and the

USSR. The key technological innovation in this competition was the launching of the Soviet Sputnik in October 1957. Although the power and prestige of the USSR were greatly enhanced by the innovation, soon they were completely overshadowed by the achievements of the space program that the United States launched in 1961 with financial resources entirely beyond the reach of the USSR. What is more, in the decade following the launching of Sputnik, the installation of hundreds of long-range missiles empowered the United States and the USSR to destroy each other’s cities in a matter of minutes. The signing of a five-year Strategic Arms Limitation Treaty (SALT) in 1972 consolidated the balance of terror between the two superpowers, but did not halt the armsments race. It simply shifted it “to other kinds of weapons not mentioned in the treaty for the good reason that they did not yet exist.”

In the scientific discovery of new weapons systems – even more than in earlier forms of the armsments race – the superpower with greater command over global financial resources could turn the balance of terror to its own advantage by stepping up, or by threatening to step up, its research efforts to levels that the other superpower simply could not afford. This, of course, is what the Reagan administration did in the 1980s primarily, though not exclusively, through the Strategic Defense Initiative. It is not clear to what extent the need to rescue the US economy from the deep recession of 1979–82 through a powerful dose of military Keynesianism influenced the strategic considerations that led to this final escalation of the Cold War armsments race. But whatever the US rationale, Soviet miscalculations played a crucial role in determining the eventual outcome.

Two such miscalculations were especially crucial. One was the decision to join other middle-income countries in borrowing heavily from Western banks in the 1970s. The true extent of Soviet borrowing is not known, but we do know that East European countries assumed financial obligations that were among the heaviest in the world. A second and greater miscalculation was the invasion of Afghanistan. As previously noted, this event, in conjunction with the Iranian crisis, precipitated the run on the dollar that in 1980 led Volcker to tighten further the US money supply and take other measures that turned the flood of capital available to Second and Third World countries in the 1970s into the drought of the 1980s, and simultaneously produced a

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32 Ibid., 360, 368, 372–73; for the US–Soviet arms race, see William Burr and David Alan Rosenberg’s chapter in volume II.
33 For Reagan’s policies, see Beth A. Fischer’s chapter in this volume.
collapse in the price of gold, oil, and other raw materials, which had become the main source of foreign exchange for the USSR. These changes hurt the USSR as they did other middle-income countries that had gone into debt in the 1970s. But in the case of the Soviet Union, a deteriorating financial position was aggravated by the capacity of the United States to borrow massively from abroad, mostly from Japan, so as to escalate the armaments race well beyond what the USSR could afford. Combined with generous US support to Afghan resistance against Soviet occupation, the escalation forced the Soviet Union into an unwinnable double confrontation: in Afghanistan, where its high-tech military apparatus found itself in the same difficulties that had led to the defeat of the United States in Vietnam, and in the arms race, where the United States could mobilize financial resources wholly beyond the Kremlin’s capabilities.

This double confrontation did not in itself cause the collapse of the USSR. But it was certainly one of the most crucial elements in the combination of circumstances that did. Above all, it had unintended consequences that had a lasting impact on things to come.

The legacy of the neoliberal (counter)revolution

Who actually won the Cold War, if anyone did, remains a controversial issue. Assessments of the global power of the United States in the wake of the demise of its Soviet rival vary widely.

“Now is the unipolar moment,” a triumphalist commentator crows; “[t]here is but one first-rate power and no prospect in the immediate future of any power to rival it.” But a senior US foreign-policy official demurs: “We simply do not have the leverage, we don’t have the influence, the inclination to use military force. We don’t have the money to bring the kind of pressure that will produce positive results any time soon.”

These contrasting assessments of US power reflected the peculiar dynamic that had brought the Cold War to an end. The triumphalist assessment reflected the unanticipated ease with which US policies had thrown the Soviet colossus off balance and “won” the Cold War without firing a shot. The cautionary

36 For the collapse of the USSR, see Alex Pravda’s chapter in this volume.
assessment, in contrast, reflected the fact that the defeat of the Soviet Union had not eliminated the deeper causes of the crisis of US hegemony of the 1970s. To the extent that the Soviet collapse was caused by US power, it was due not to US military might but to a superior command over the world’s financial resources. And to the extent that it had military origins, it confirmed rather than reversed the verdict of the Vietnam War: it showed that, in Afghanistan no less than in Vietnam, the high-tech military apparatuses controlled by the Cold War superpowers, whatever their use in reproducing the balance of terror, were of little use in policing the Third World on the ground.

Worse still, the mobilization of the world’s financial resources to rescue the US economy from the deep recession of the early 1980s, and simultaneously to escalate the armaments race with the USSR, transformed the United States into the greatest debtor nation in world history, increasingly dependent on cheap East Asian credit, labor, and commodities for the reproduction of its wealth and power. This shift of the center of world-scale processes of capital accumulation from North America to East Asia may well turn out to be the most significant legacy of the Cold War. But whether it will or not, the shift provides key insights into the evolving relationship between the Cold War and the world economy.

The most immediate impact of the Cold War on the East Asian region was to reduce most of its states to a condition of vassalage vis-à-vis one or other of the two contending superpowers. Soon, however, the Korean War demonstrated the precariousness of this condition and induced the United States to establish in the region a trade and aid regime extremely favorable to its vassal states, especially Japan. This “magnanimous” early postwar regime set in motion a “snowballing” process of connected economic “miracles” which started in Japan in the 1950s and 1960s, rolled on in South Korea, Taiwan, Hong Kong, Singapore, and some ASEAN countries in the 1970s and 1980s, and eventually encompassed China and Vietnam as well.39

In spite of US “magnanimity,” the faultlines between the US and Soviet spheres of influence in the region started breaking down soon after they were established, first by the Chinese rebellion against Soviet domination in the late 1950s, and then by the US failure to split the Vietnamese nation along the Cold

In this respect, the Vietnam War was a crucial turning point. While the Korean War had resulted in the formation of a US-centric East Asian regime based on the exclusion of China from normal commercial and diplomatic intercourse with the non-Communist part of the region, defeat in Vietnam induced the United States to allow China to resume such contacts. The scope of the region’s economic integration and expansion was thereby broadened considerably, but only at the expense of US capacity to control its dynamic politically.

Japan’s spectacular economic ascent from the 1950s through the 1980s gradually transformed the previous relationship of Japanese political and economic vassalage vis-à-vis the United States into a relationship of mutual dependence: Japan remained dependent on US military protection, but the reproduction of US power came to depend on Japanese finance and industry. This transformation has been widely attributed to policies that made Japan the prototype of the “developmental state.” Equally important, however, were two other factors.

One was the strong growth in the United States and in the USSR of capital- and resource-intensive industries (such as the steel, aircraft, military, space, and petrochemical industries), which created profitable opportunities for specialization in labor-intensive industries and resource-saving activities. As economic historian Kaoru Sugihara has underscored, Japan seized these opportunities by developing interlinked industries and firms with different degrees of labor and capital intensity, but retained an overall bias toward the East Asian tradition of privileging the utilization of human over nonhuman resources. At the same time, a surge of nationalism under the Cold War regime generated fierce competition across the East Asian region between relatively low-wage industrializers and higher-income countries. “As soon as wages in one country rose even fractionally,” that country “had to seek a new industry which would produce a higher quality commodity,” thereby “creating an effect similar to the ‘flying geese pattern of economic development.”

40 For an analysis of the Sino-Soviet split, see Sergey Radchenko’s chapter in volume II.
42 The characterization of Japan as a “developmental state” was originally proposed by Chalmers Johnson, MITI and the Japanese Miracle: The Growth of Industrial Policy, 1925–1975 (Stanford, CA: Stanford University Press, 1982). The notion was later applied to other states in the East Asian region. See, for example, Deyo (ed.), The Political Economy of the New Asian Industrialism.
And the more low-wage countries joined the process, the longer the chain of “flying geese.”

The other factor that contributed decisively to the Japanese economic ascent and the diffusion of Japanese economic power throughout the East Asian region was the crisis of vertically integrated business organizations. As the number and variety of vertically integrated, multinational corporations increased worldwide, their mutual competition intensified, inducing them to subcontract to small businesses activities previously carried out within their own organizations. The tendency toward the bureaucratization of business through vertical integration, which had made the fortunes of US corporate business since the 1870s, thus began to be superseded by a tendency toward informal networking and the revitalization of small business.

This trend has been in evidence everywhere, but nowhere more so than in East Asia. Without the assistance of multiple layers of formally independent subcontractors, noted Japan’s External Trade Organization, “Japanese big business would flounder and sink.” Starting in the early 1970s, the scale and scope of this multilayered subcontracting system increased rapidly through a spillover into a growing number and variety of East Asian states. Although Japanese business was its leading agency, the spillover relied heavily on the business networks of the overseas Chinese diaspora, which were from the start the main intermediaries between Japanese and local businesses in Singapore, Hong Kong, Taiwan, and most Southeast Asian countries. The region-wide expansion of the Japanese multilayered subcontracting system was thus supported not only by US political patronage “from above,” but also by Chinese commercial and financial patronage “from below.”

Over time, however, patronage from above and below began to constrain rather than support the capacity of Japanese business to lead the process of regional economic integration and expansion. As long as the “magnanimous” postwar US trade and aid regime was in place, Japan’s dependence on US military protection was not a problem. But, by the 1980s, that regime had given way to US extortions, such as the massive revaluation of the yen imposed on Japan by the Plaza conference of 1985 and the so-called Voluntary Export Restraints imposed on Japanese imports into the United States, which considerably undermined Japan’s capacity to profit from US patronage. To make things worse for Japan, US corporations began restructuring themselves to compete more effectively with Japanese businesses in the exploitation of East Asia’s rich endowment of labor and entrepreneurial resources, not just through direct investment, but also through all kinds of subcontracting arrangements. The more intense this competition became, the more the overseas Chinese emerged as one of the most powerful capitalist networks in the region, in many ways overshadowing the networks of US and Japanese multinationals.

This development encouraged Deng Xiaoping to seek the assistance of the overseas Chinese in upgrading the Chinese economy and in pursuing national unification in accordance with the “One Nation, Two Systems” model. The result was the close political alliance between the Chinese Communist Party and overseas Chinese business. Together, they greatly facilitated the reincorporation of mainland China into regional and global markets and resurrected a state whose demographic size, abundance of entrepreneurial and labor resources, and growth potential surpassed by a good margin those of all other states operating in the region, the United States included. The progressive realization of that potential in the 1990s and 2000s would create for US hegemony a new challenge in key respects more complex and difficult to contain than the Soviet challenge of the Cold War era.