The Wealth and Poverty of Nations: Why Some Are So Rich and Some So Poor (1998)

by David S. Landes

On the eve of the storm, the world economy was, to an extent never seen before, truly global. It was linked by new technologies that made it possible to ship products cheaply from one side of the globe to the other, to communicate virtually instantaneously over huge distances. But it was also, more importantly, linked together by the almost universal, if sometimes grudging, acceptance of a common economic ideology: the belief that free markets, with secure property rights, were the only way to achieve economic progress; and in articular that a nation hoping to make its way forward needed to welcome foreign trade and foreign investors with open arms. And this shared ideology did indeed lead to unprecedented transfers of Western capital and technology to emerging economies -- transfers facilitated by the fact that everyone knew that any country that strayed from the path would be punished by financial crisis, and would soon be obliged to accept the harsh austerity prescribed by teams of Western technocrats.

The year, of course, was 1913 -- the high-water mark of what economic historians sometimes call the First Global Economy -- and over the decades that followed all of its certainties were lost. By the beginning of the 1950s, long-distance world trade had shrunk to a shadow of its former self, as Third-world economies, pursuing the goal of industrialization through "import substitution," began producing many of their own manufactured goods; private international movements of capital had virtually disappeared in the face of debt defaults, expropriations, and administrative restrictions. And about a third of the world's population lived under regimes that had completely rejected the idea of private property, let alone free markets.

The worldwide rejection of the market that took place in the first half of this century was not a matter of mere accident, or of the mysterious dominance of some misguided ideology. Free-market capitalism had proved, in the eyes of most people who thought about it, to be unstable, unjust, and ineffective. The world between the wars had been wracked by financial crises -- crises in which those countries that broke the rules, going off the gold standard and restricting the free movement of money and goods, had done better than those that tried to maintain the Victorian virtues. Capitalism seemed to be marked by ever-growing inequality, with the rich getting richer while the poor got poorer; and it seemed to condemn less-developed nations to a permanent role as mere suppliers of raw materials to the established industrial powers. The turn away from the market, and toward the state, was based -- or so everyone thought -- on the hard lessons of experience.

It is therefore an astonishing reversal of fortune that, as we approach the century's end, nearly all the world has returned to more or less the same ideology of free markets and sound money that prevailed at its beginning. Understanding why the seemingly inexorable trend toward growing state power has become instead a seemingly inexorable withering of that power is perhaps the most important question of contemporary history. And so I was extremely curious to see what answer Daniel Yergin and Joseph Stanislaw would offer in their widely heralded new book The Commanding Heights: The Battle Between Government and the Marketplace That is Remaking the Modern World.

Alas, while I enjoyed the book, I came away feeling cheated. Indeed, one might go so far as to accuse Yergin and Stanislaw of playing a game of bait-and-switch. They promise to tell us "why" but they never even try to go beyond "what."

Consider, for example, the centerpiece of their book: the rise and fall of the British welfare state. The outlines of that story are well told: After depression and war, the British people demanded and got a state that provided a strong social safety net and job security, in part by nationalizing key industries -- the "commanding heights." Given our current cynicism about government, it is hard to imagine that this statist solution could have had any merits -- but the fact was that for a generation or so it worked pretty well. Perhaps economic growth was slower than it might have been, perhaps Britain's rank as a world power eroded, but given full employment and steadily rising living standards, Harold Macmillan's famous declaration that "you never had it so good" was the simple truth. Then it all began to fall apart: inflation, rising unemployment, disruptive labor disputes -- all preparing the ground for the radical free-market ideology of Margaret Thatcher and her guru, Keith Joseph. And Thatcherism, after a rocky start, did seem to deliver on enough of its promises that its essentials now seem secure despite the return of Labour to power.

So what do we learn from this account? Free-market capitalism was discredited by its failures, replaced with a mixed economy that was legitimized by its successes; then the mixed economy began to work badly, and was replaced by a return to free-market capitalism, which has been legitimized by its successes.... Clearly this leaves all the important questions unanswered. Why do free markets, which seemed to fail so drastically in the 1930s, seem to work pretty well nowadays? Why did the mixed economy, which seemed to work pretty well in the '50s and '60s, fan apart in the '70s and '80s? And, the big question, are we on some sort of pendulum -- will the state rise again?

What would it take to answer these questions? Recounting the history is not enough. On reading Yergin and Stanislaw I found myself entertaining two hypotheses. One was that changing technology has been the driving force. After all, the collapse of capitalism's first golden age coincided with the rise of mass production; the era of the mixed economy was also the era in which the automobile industry was at that economy's core, and that state-within-a-state General Motors its emblematic firm. Perhaps the shift from mass production to just-in-time, from heavy industry to high tech, has somehow changed the rules about what works and what doesn't. In that case, predicting whether and when the pendulum will swing back is a matter of technological forecasting.

Or perhaps the story is really about psychology and sociology, not technology. Europeans who try to make sense of Eurosclerosis often point out that the factors that supposedly explain the continent's high unemployment rates -- generous unemployment benefits, high minimum wages, regulations that make it expensive to hire new workers -- go back to the the 1950s, yet at the time were somehow consistent with full employment. To explain the shift, they sometimes invoke a "generational" theory: The welfare state worked for its first generation because those who had grown up in the Depression, who feared unemployment and were grateful for the dignity of full employment, did not exploit the benefits to which they were entitled. Maybe there is a fundamental cycle: The failures of the market lead to an expanded state, which works as long as there is sufficient idealism to support it; but eventually cynicism prevails, and the market again appears an attractive alternative.

The point is that it makes a huge difference to our perspective which of these explanations -- if either -- is more nearly right. Yet Yergin and Stanislaw never give us anything that could help us decide. Instead they regale us with tales of the formative experiences of Margaret Thatcher and Deng Xiaoping -- interesting (the photo of young Margaret playing the piano is almost worth the price of the book), but off the point. Indeed, one might wonder why a book that is in large part a celebration of the triumph of the private sector over the state mainly seems to tell us about the lives and deeds of -- guess who? -- politicians.

One cannot make the same criticism of David Landes' The Wealth and Poverty of Nations: Why Some Are So Rich and Some So Poor. Landes is a distinguished economic historian whose classic Prometheus Unbound remains unrivaled in its explanation of just what was revolutionary about the Industrial Revolution. Where Yergin and Stanislaw concentrate on the last few decades, Landes has a thousand-year perspective, and concentrates mainly (and properly) on technology and institutions. Where Yergin and Stanislaw tell stories about rulers and how they came to their beliefs, Landes tells us about companies and industries, and how they gained or lost advantage. And much of what he has to say is fascinating and insightful.

Yet in the end I felt as cheated by Landes as I did by The Commanding Heights. Surely readers of a book that promises in its very title to explain why some nations are rich while others are poor deserve more than Landes' concluding paragraph: "The one lesson that emerges is the need to keep trying. No miracles. No perfection. No millenium. No apocalypse. We must cultivate a skeptical faith, avoid dogma, listen and watch well, try to clarify and define ends, the better to choose means." For this we needed to read 500 pages?

In the end, what both books left me with was a sense of the inadequacy of narrative history as a guide to action. No matter how many interesting stories you may tell about the past, they are just that -- stories -- unless they are brought to bear on some hypothesis about how the world works. History is useful because it is a laboratory, in which time and chance have performed experiments that can confirm or reject our ideas. But you can't learn anything from those experiments unless you are actually willing to state your ideas clearly in the first place.

So I ask myself: What do Yergin and Stanislaw and Landes actually believe? And the answer, which seems to me to be damning, is that I am not sure. I think Yergin and Stanislaw approve of the move to the market, but I have had to pick that up by osmosis -- or as a colleague of mine puts it, the economic moral is conveyed by innuendo, rather than stated in any way that could be refuted. And for all the erudition in Landes' book, I am at a loss to tell you what economic policies he might prescribe for any particular country.

So I am still waiting for a book that helps me understand what really happened in this utterly perplexing century, when the world moved decisively away from the market, then equally decisively back. The one thing I know is that whoever writes that book will have to be a person unafraid of offering theories as well as facts, and therefore of saying things that might turn out to be wrong.

Review by Paul Krugman as printed in the Washington Monthly 1998.