From the Great Depression to the Euro Crisis, 1929–2013: A Global Approach

● JORDI CATALAN
University of Barcelona

Introduction[1]

This article attempts to explain the causes of the main economic crises that have occurred since 1929. A crisis is defined as any episode in which the GDP per capita of an economy, in real terms at purchasing power parity, remains below the highest annual level previously reached. The GDP per capita estimates made by Angus Maddison are the main source of data. For recent years these estimates are linked to OECD figures.

Two research hypotheses are proposed: first, that excessive financial speculation plays a central role in major crises; and second, that the magnitude of crises increases when governments adopt misguided policies, which can turn a crisis into a major slump. Excessive speculation is generally the result of outbreaks of euphoria among economic agents, who rather than having rational expectations are driven by animal spirits and the contagion of optimism. Financial intermediaries often contribute to feeding the bubble by providing easy credit. As Keynes, Kindleberger, Minsky and other authors have noted, overly optimistic expectations can push stock market and real estate assets to short-term prices far above their long-term values and lead economic agents to assume risks and levels of debt that turn out to be unsustainable

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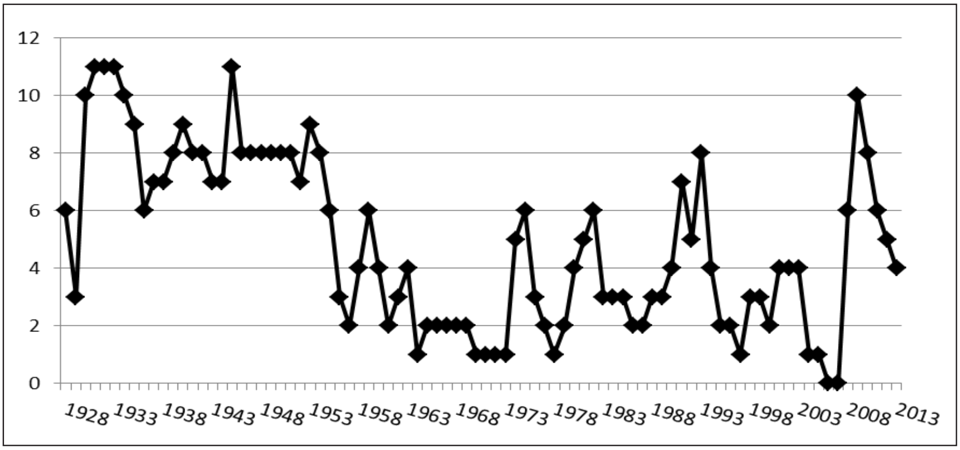
FIGURE 1 ▪ *Global crises, 1928-2013: number of economies in crisis (GDP per capita below previous peak) -sample 12 economies*



Source: By the author, from Maddison and OECD. See Note 3.

when the bubble bursts.[2] Immediately following the collapse of asset prices, debts grow, credit becomes scarce, and expectations are deflated. Real investment evaporates due to the combined effect of tightening of credit, waning animal spirits, and the spread of pessimism. Hence governments should implement policies aimed at managing demand, opting for expansionary policies when the main risk is a low level of output, and contractionary policies at the point in the cycle when markets are becoming overheated.

For this analysis, 12 economies representative of the global economy were selected in order to identify the most significant slumps at the global level. The economies chosen represent North America (the United States), Latin America (Argentina, Brazil and Mexico,), the industrial core of Europe (the United Kingdom, Germany and France), the European periphery (Sweden and Spain), and Asia (India, China and Japan). The first step in the analysis was to determine how many countries met the condition of "crisis" as defined above (GDP per capita below the previous peak) for each year from 1928 to 2012. This exercise provides a simple but powerful indicator of how global the crises have been. The result is represented graphically in Figure 1 below.[3]

2. Among the works by these authors, I consider the following particularly relevant: Keynes (1930 and 1936), Kindleberger (1973 and 1978), and Minsky (1975 and 1982).

3. The original GDP per capita figures for each country are expressed in 1990 international Geary-Khamis dollars, at purchasing power parity, and are taken from works by Maddison (1995 and 2006). Maddison's data have been linked to real growth rates for real GDP per capita (2005 prices) and population, provided by the OECD. The series obtained from the Maddison/OECD data have been used to create Figures 1–9, for which I am solely responsible.

Our global crisis indicator reaches its highest value during the 1930s, thus confirming that this was indeed the decade of the Great Depression. The worst point was the three-year period from 1931 to 1933, when 11 of the 12 sample economies were in crisis. The graph also suggests that the recovery which took place after 1933 was not sustained, and that it was only after 1945 that the downward trend in the extent of the crisis became unequivocal.

In contrast, the indicator shows a clear downward trend from the mid-1940s to the early 1970s. From 1970 to 1973 there was only one country in crisis. The results suggest that during the period defined as the Golden Age of European growth, crises at the global level practically ceased to occur.

From 1974 the trend changed again. Two shocks, around 1975 and 1982, can be identified. Half of the sample economies were in crisis at both of these times. Though shorter in duration and less global than the one in the 1930s, these crises broke the pattern of the golden age.

In the first half of the 1990s, we can observe another global slump that reached a peak in 1993, with eight of the 12 sample economies in crisis. Like the crises of the mid-1970s and early 1980s, this one was short-lived, but it involved a greater number of countries.

The new century began with a relatively mild warning that affected a third of the sample in 2001–02. There followed a number of years of apparent calm before the world sank into another slump in 2008. The downturn reached its nadir in 2009, when ten of the countries in the sample recorded a GDP per capita below its historical high. In 2013 a third of the sample economies were still in crisis. Given the intensity of the slump in 2009 and its relatively long duration, we consider it the most serious crisis to have hit the global economy since the 1940s.

In this article, we examine some of the slumps that have had the greatest global impact and use the methodology of comparative history to test the hypotheses stated above concerning the origins of crises and the role of economic policy. We analyse significant countries with similar starting conditions and different policies. In the next two sections, we focus on comparing the impact of the Great Depression of the 1930s in the centre and the periphery. Later, we compare the crises of stagflation. Finally, we analyse the crises of deregulation and the present situation, which many have dubbed a *Great Recession*, but which, given its duration and intensity, might better be described as another great depression.

The Great Depression of the 1930s in the centre

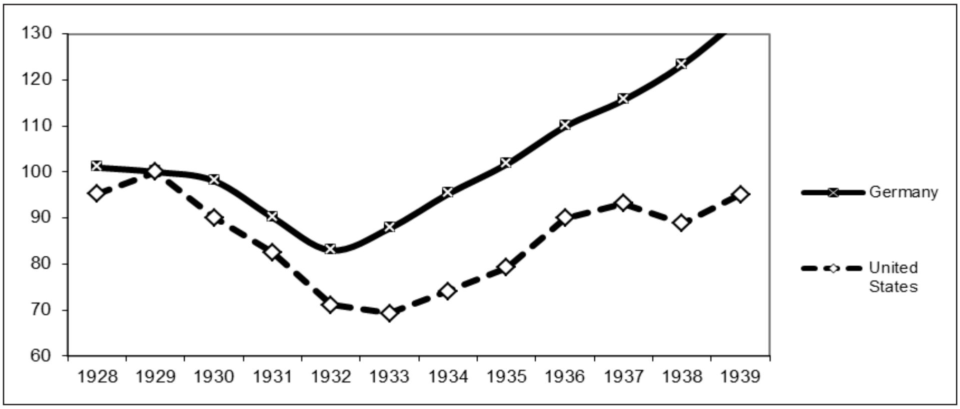
The first part of our analysis focuses on countries that had high levels of income per capita when the Great Depression hit.[4] First, we compare the experience of the United States and Germany, two countries that were similar in size and had comparable levels of GDP per capita, and both of which were epicentres of the Depression. We then compare what happened in the United Kingdom and France, which are similar in size and had comparable income levels, but which implemented diametrically opposed policies.

Up until 1931, the world was dominated by what has been called the Genoa consensu. The participants in the Genoa Conference, held in 1922, passed a series of resolutions, including one calling for the restoration of a system of currency convertibility based on fixed gold parities, and another that stressed the importance of pursuing balanced budgets. As a result, most countries returned to the gold standard in the second half of the 1920s and attempted to reduce their public deficits. These policies also held sway in the early 1930s, because it was believed that the gold convertibility of currencies and the free circulation of the metal would automatically correct any macroeconomic imbalances.

The crisis originated in the United States and was caused by excessive stock market speculation. The index of share prices on the New York Stock Exchange increased from 93 in May 1926 to 193 in May 1929: an annual growth rate of 27 per cent over the three-year period. Meanwhile, the growth rate of GDP per capita (i.e. the real economy) was only 1.5 per cent annually. The imbalance between the two rates was clearly unsustainable. In many cases shares were purchased on credit provided by brokers and banks, and when the cycle turned in October 1929 stock traders were unable to realise expected profits. Many were left insolvent and also dragged down those who had recklessly lent them money. Credit contracted, interest rates rose, and deflation spread from the stock market to the rest of the domestic economy. As deflation took hold and the cost of money rose, expectations were deflated, animal spirits were depressed, and investment contracted. The US slump spread to the rest of the world as a result of the drop in US imports and tightening of credit (which some countries had already been experiencing since the peak months of the stock market expansion).

4. The main works used to compare the way the Great Depression progressed in industrial countries, in addition to those cited in Note 2, are as follows: Friedman and Schwartz (1963), Sauvy and Hirsch (1984), James (1986 and 2009), Barkai (1990), Louat and Servat (1995), Temin (1989 and 1990), Overy (1994), Eichengreen (1995), Bernanke (2000), James (ed.) (2002), Henry (2003), Eichengreen and O'Rourke (2009), Margairaz (2009), and Parejo and Sudrià (2012).

FIGURE 2 ▪ *Indices of GDP per capita in 1990 GK $ (1929=100)*



Source: By the author, from Maddison. See Note 3.

The enactment of the Smoot-Hawley Tariff in June 1930 may have contributed to spreading the Depression to the rest of the world, but it is generally agreed that the action taken by the Federal Reserve in September 1931, which interrupted its expansionary monetary policy, made the situation worse in the United States. Herbert Hoover's policy of raising taxes the same year and his rejection of the proposal to create an unemployment benefit and compensate war veterans also gave fiscal policy an excessively contractionary bias. As a result, the US economy continued to contract in 1932 and 1933.

Germany experienced the cancellation of credit as a result of the Wall Street Crash, and the Reichsbank raised interest rates in an effort to halt to the flight of gold. Chancellor Heinrich Brüning also had to deal with the insolvency of first Austrian, and later leading German banks. But his preference for fiscal adjustment led to a worsening of the crisis. In 1931, he sharply reduced salaries in the civil service, cut unemployment benefits, increased taxes on tobacco and beer, and backed wage cuts in the private sector. As a result, by 1932, German GDP per capita had fallen by about 17 per cent from the 1929 level. With over 6 million unemployed, Brüning ended up being replaced by Franz von Papen, who began to make changes to government policy. But Papen could not prevent the electoral rise of the Nazis, which led to Adolf Hitler's accession to the chancellorship in January 1933.

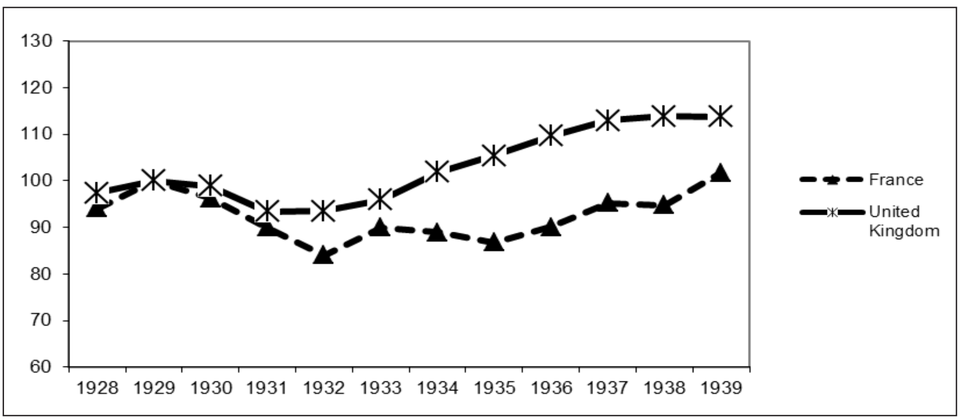
National Socialist governments gave priority to public works, focusing first on reforestation and expenditure on road infrastructure (*Autobahnen*) and railways. Public spending later grew as a result of the drive to rearm the country. Although Hitler did not officially declare his rejection of the gold standard, strong control of exchange rates (which included the adoption of multiple rates) led to de facto abandonment of the system. Furthermore, in

1933 the Chancellor announced that outstanding loans would not be repaid (with the exception of those provided through the Dawes and Young Plans), and the following year he declared a complete moratorium on foreign debt service. Strong fiscal expansion enabled Germany to emerge from the crisis from 1935 as the Third Reich's motorisation programme was openly transformed into an expansion of the war industry.

In the United States, Franklin Roosevelt's victory initially led to the implementation of an expansionary policy that broke with the Republican approach. In March of 1933, the same year he took office, Roosevelt abandoned the gold standard, allowing the dollar to depreciate. He facilitated farm credit and mortgage lending, created the Tennessee Valley Authority to boost construction of dams and power stations, allowed minimum wages to be established in industry, supported banks in exchange for their agreement to separate commercial and investment banking (Glass-Steagall Act), and ratified the Social Security Act, which introduced unemployment, disability and old-age benefits, as well as providing for the compensation of war veterans. This strongly expansionary policy paved the way for recovery from 1934, but Roosevelt still believed a balanced budget was important. In 1937, when GDP per capita was still below the 1929 level, the Democrat government sought to achieve a budget surplus, triggering another recession the following year. Consequently, America had still not fully recovered when the Second World War broke out.

The contrast between the policies implemented in the United Kingdom and France is even more significant. In 1931, the National Government formed by Ramsay MacDonald adopted the most radical measure possible for a country that had championed gold for over two centuries when it decided in August to allow the pound to depreciate. This measure was complemented by an ex-

FIGURE 3 ▪ *Indices of GDP per capita in 1990 GK $ (1929=100)*



Source: By the author, from Maddison. See Note 3.

pansionary monetary policy consisting of continuous interest rate cuts. Furthermore, the British Empire Economic Conference, held in Ottawa in 1932, marked another shift for a power that had traditionally advocated free trade. Protective tariffs were raised to discriminate in favour of trade between the dominions and colonies of the British Empire. As a result, in 1931, Britain became the first major industrial nation to start recovering. It was also the first major Western country to pull out of the Depression (after Sweden). By 1934, GDP per capita had recovered to the 1929 level, so the Great Depression only lasted four years in Britain.

At the opposite extreme we find the other great European empire of the time: France. During the 1930s, the country experienced major political instability and governments were short-lived. Even before the formation of the Popular Front, though, there was universal agreement on the importance of pursuing a balanced budget and maintaining the gold standard. One of the most dramatic steps was taken by Pierre Laval, who in 1935 attempted to impose deflation by decree (what we would now call internal devaluation). He cut the salaries of civil servants by 10 per cent, reduced rents, forced down the price of bread and coal, and lowered gas and electricity rates. Laval also tried to reduce wages in the private sector and increased the tax burden on high-income earners. Despite his efforts, all he ended up achieving was another recession: GDP per capita in 1935 was 14 per cent below the 1929 level. It was not until Léon Blum accepted the devaluation of the franc in September 1936 that France started to recover.

The Great Depression of the 1930s in the periphery

In this section we analyse the impact of the Great Depression of the 1930s on peripheral economies, comparing the trajectories of two countries in Latin America and two in Asia.[5] First, we consider the case of Argentina and Brazil, both of which had a low level of industrialisation and a high degree of trade openness when the Depression hit. As a result of the crisis, both countries experienced a huge drop in exports, a drying-up of foreign credit, forced suspension of the gold standard, and a drift towards authoritarianim. The difference was that Argentina implemented a severe adjustment and gave priority to servicing its foreign debt with Britain, whereas Brazil suspended debt repayments from September 1931.

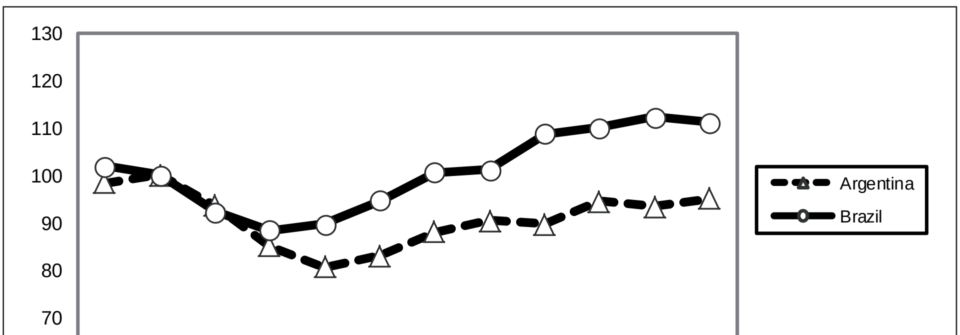
5. In my analysis of the Great Depression in the periphery, the following works were particularly helpful: Díaz Alejandro (1980), Maddison (1985 and 1992), Rothermund (1988, , 1992 and 2012), Thorp (1985 and 1998), Richardson (1999), Lynch (2001), Sivasubramonian (2002), Rapoport (2005), Reinhart and Rogof (2009), Marichal (2010), Wolfe (2010), Kudaisya (2011), Roy (2011), and Belini and Korol (2012).

In Argentina, exports and foreign credit contracted in the course of 1929, and the external imbalance led the government of Hipólito Yrigoyen to order the closure of the *Caja de Conversión* in December, which was tantamount to abandoning the gold standard. In September 1930, the radical Yrigoyen, the father of the country's nascent welfare state, was overthrown in a military coup that brought Lieutenant General José Félix Uriburu to power. Uriburu tried to restore budgetary balance by cutting spending and increasing revenue. To reduce expenditure, he cut salaries in the public administration and brought new public works to a standstill. To boost revenue, he increased tariffs, inheritance tax and stamp duty, as well as introducing new income and fuel taxes. He also pledged to continue servicing both foreign and domestic debt. The government introduced exchange controls, but continued to authorise outflows of gold to service foreign debt. As a result of these policies, GDP per capita in Argentina fell sharply: in 1932 it was 19 per cent below the 1929 level.

Agustín Pedro Justo became the president of the republic in 1932. Although the tax burden remained high, at the end of 1933, a system of multiple exchange rates was introduced and the currency was devalued by 20 per cet. The exchange-control system continued to give priority to servicing foreign debt. In fact, the Roca-Runciman Treaty, signed with Britain in 1933, in addition to reducing duties on two hundred British articles, required Argentina to fully service its foreign debt. In return, Britain agreed to import a minimum tonnage of meat equal to the average for 1931–1932, a condition that served the interests of ranchers of the Argentinean pampas.

Argentina's GDP per capita began to recover in 1933, but the improvement was extremely slow. The Central Bank of Argentina, in which the gov-

FIGURE 4 ▪ *Indices of GDP per capita in 1990 GK $ (1929=100)*



Source: By the author, from Maddison. See Note 3.

ernment had a limited influence, was established in 1935. In 1936, the Roca-Runciman Treaty was renewed and Argentina continued to give priority to servicing its foreign debt with Britain. In 1938, the price level was still below that for 1929, and when the Second World War broke out, Argentina's GDP per capita had still not risen above the 1929 level.

In Brazil, President Washington Luís Pereira de Sousa, who represented São Paulo coffee interests, pursued an orthodox budgetary policy and tried to maintain the gold standard until the country's reserves ran out in October 1930. Like Yrigoyen in Argentina, Washington Luís was overthrown by a military uprising, led in this case by Getúlio Dornelles Vargas, the governor of the cattle-raising state of Rio Grande do Sul. However, those who had seized power in the two countries pursued markedly different policies.

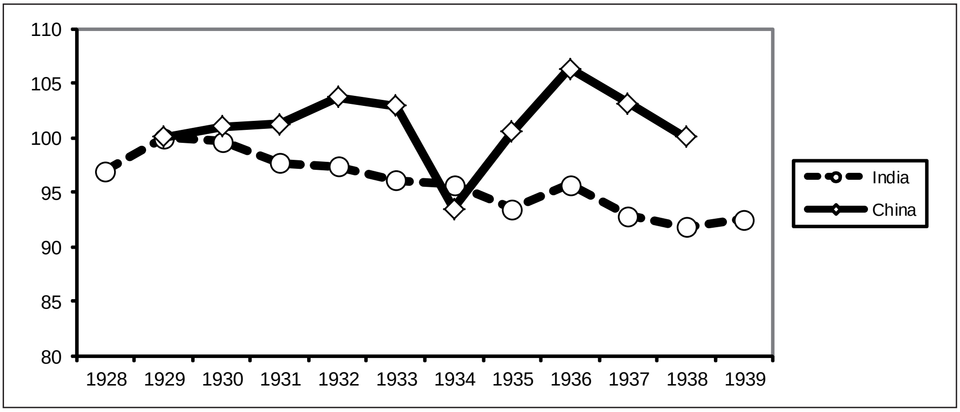
Vargas served as interim president until 1937, later becoming a self-confessed dictator and proclaiming the *Estado Novo* (New State). From 1931, Vargas implemented measures to support agricultural income, based on purchasing coffee and destroying any surplus production. In September, he declared a moratorium on foreign debt, suspending debt payments to the United States and orienting the country's trade relations towards Germany. He implemented expansionary fiscal and monetary policies, doubled Brazil's road mileage between 1930 and 1938, and passed a law to establish a social security system for urban workers.

In 1931, Brazil's level of GDP per capita was 13 per cent lower than it had been before the crisis started. However, the policies pursued by Vargas facilitated a rapid recovery. Unlike Argentina, Brazil emerged from the crisis in 1936, at which point the price level was 28 per cent higher than in 1929.

India and China, two much poorer peripheral economies with higher populations, also experienced very different results due to the radically different policies they pursued. Because their economies were less open than those of the Latin American countries, the impact of the Depression was much less severe. However, while colonial India was gradually dragged into the Depression, China followed a clearly expansionary path during the period.

In British India, the onset of the Depression coincided with the launch of the second Satyagraha campaign by Mahatma Gandhi. The economic demands set out, which coincided with those of the Federation of Indian Chambers of Commerce and Industry, included proposals to devalue the rupee, protect the cotton industry, reduce land tax, and end the salt tax. George Schuster, finance minister of the Council of India, came to support the proposed devaluation of the rupee, but received orders from Britain to adopt a deflationary policy. London devalued the pound in 1931, but was unwilling to allow the rupee to depreciate against the British currency. On the contrary, colonial authorities imposed an extremely deflationary fiscal policy. This meant reducing salaries in the public administration, increasing consump-

FIGURE 5 ▪ *Indices of GDP per capita in 1990 GK $ (1929=100)*



Source: By the author, from Maddison. See Note 3.

tion and income taxes, raising tariffs, and cutting back on public works (which had a particularly significant impact on railway construction and irrigation works). The colonial government did not declare a debt moratorium and continued to service its foreign debt. The price level fell by 35 per cent from 1929 to 1935.

As a result of this policy, India's GDP per capita, which in 1930 had not fallen by even 1 per cent from the 1929 level, continued to contract throughout the 1930s. According to Maddison's estimates, in 1938, India's GDP per capita was 8 per cent below the 1929 level. This decline was not entirely the result of the deflationary policy adopted: fluctuations in harvests and the country's high birth rate were also contributing factors. However, the massive internal devaluation imposed on India did nothing to stimulate growth.

Unlike British India, China was independent. However, in 1928 the country was just coming out of a period of civil war, with the victory of Chiang Kai-shek, and was about to experience another insurrectionary period with the uprising of the Red Army in 1930 and Mao Zedong's Long March, which began in 1934. A further complication was Japan's seizure of Manchuria from China in Chiang Kai-shek's policy was by necessity expansionary because the Kuomintang government had a limited ability to enforce tax collection in the country as a whole and could not avoid high deficits. However, China regained sovereignty by cancelling some foreign concessions and abolishing foreign extraterritorial rights. The country had experienced foreign debt moratoria in the 1920s, and in the 1930s there were further delays in debt service. The Kuomintang also decided to increase customs duties, which by 1936 were almost four times higher than they had been in 1929. All of these measures helped stimulate domestic demand and industrial expansion, which was quite significant until the Japanese attack in 1937.

In contrast to India, China never adopted the gold standard; its monetary system was based on silver. Up until 1931, the price of silver fell against gold, which contributed to the depreciation of the yuan. In contrast to what happened in its Asian neighbour, prices in China rose by 23 per cent from 1929 to 1931. Chinese competitiveness began to suffer the consequences of the pound and the yen abandoning the gold standard in the previous year, followed by the US currency in 1933. This situation resulted in outflows of silver and a drop in Chinese prices from 1931 to 1934. In 1935, the Kuomintang decided to introduce a fully fiduciary monetary system (based on the *făbì*), and prohibited the circulation of silver yuan. The issue of banknotes pushed prices up again and they ended up skyrocketing during the Japanese invasion of 1937.

Despite political instability, an emphasis on monetary and fiscal expansion favoured the growth of the Chinese economy during the 1930s. China was largely unaffected by the international depression until 1933, and a poor rice harvest was a significant factor behind the decline in GDP recorded in 1934. GDP per capita had recovered again three years later.

In summary, the cases studied in Latin America and Asia corroborate the fact that in a crisis of effective demand and deflation, like the one that occurred in the 1930s, the countries that adopted expansionary policies, such as Brazil and China, were able to recover from the crisis. In contrast, Argentina and India, countries that pursued deflationary or internal devaluation policies, were plunged into the abyss.

Stagflation crises in the 1970s and 1980s

As pointed out above, there was a downward trend in the number of crises after the Second World War and at a certain point they practically ceased to occur. In our sample, the number of economies in crisis went from 11 in 1945 to just one in 1970–1973. We cannot digress to offer an in-depth analysis of the factors that explain the absence of crises during this economic golden age, but we will highlight two reasons we see as critical, both of which relate to the legacy of Keynes. First, the Bretton Woods system gave governments autonomy to decide their macroeconomic policy, a freedom of action they lacked when the gold standard was in place. This allowed for devaluation and the imposition of controls on capital movements. Second, during the war most Western governments adopted demand-management policies: when real growth was at risk, they tended to implement expansionary fiscal or monetary policies, and when the threat was inflation, they reduced budget deficits or raised the cost of credit.

Excessive money printing by the Federal Reserve and speculation against the dollar contributed to the erosion of the Bretton Woods system, which ended up collapsing between 1971 and 1973. However, in this case speculation was not the main factor that brought an end to the golden age or the reason why half of the economies in our sample were once again immersed in a widespread crisis by 1975. The price of a barrel of oil quadrupled as a result of an embargo imposed by OPEC countries in the wake of the Yom Kippur War. The growth of industrial economies during the second technological revolution was based on increasing consumption of hydrocarbons, which could not be replaced by another energy source in the short term. The dramatic price hike significantly increased costs and intensified the distributive struggle among Western economies. It also caused an outbreak of inflation and reduced rates of profit, which led in turn to a fall in investment. The decline in capital formation put an end to the exceptional growth rates recorded during the golden age. Thus the economic situation that prevailed from the early 1970s to the mid-1980s is described as one of stagflation: stagnation combined with inflation. The stagnation was not overly pronounced, economies did grow during this period, but at much lower rates than those seen between 1945 and 1973.

The combination of relatively high inflation rates and falling growth rates (which meant the return of mass unemployment in many countries) presented governments with a dilemma for which Keynesianism offered no clear solution.[6] The question was whether to focus on controlling inflation by implementing contractionary policies, or to stimulate demand in order to tackle unemployment. It is important to note that unlike the Great Depression, when there was a general deflationary trend, in the crisis of the 1970s, in a climate of price acceleration, one could hardly speak of a lack of effective demand.

Industrial countries were split on how to deal with this dilemma. During the first oil shock, most economies opted to implement expansionary policies that accelerated inflation. Countries like Germany and Switzerland, which gave priority to controlling inflation, were the exception. However, their experience showed that the costs in terms of growth (and unemployment) were lower if the acceleration of inflation was halted at the outset rather than delaying, only to end up causing a recession in order to curb spiralling inflation. Thus, when the second oil shock hit in 1979–1980 as a result of the overthrow of the Shah, there was more of a consensus in the West that the focus should be on controlling inflation.

We will now consider two further comparisons to support the thesis that during the period of stagflation avoiding price growth from the start yielded

6. Some of the key works I have used to analyse the stagflation crises are: Maddison (1985 and 1992), Rowthorn and Glynn (1990), Pekkarinen, Pohjola and Rowthorn (1992), Cárdenas (1996), Carlin (1998), Thorp (1998); Buchheim (1999), Woodward (1999), Tomlinson (2004), Von Tunzelmann (2004), Rapoport (2005), Brenner (2006), Eichengreen (2007), Rougier and Belini (2008), Marichal (2010), and Belini and Korol (2012).

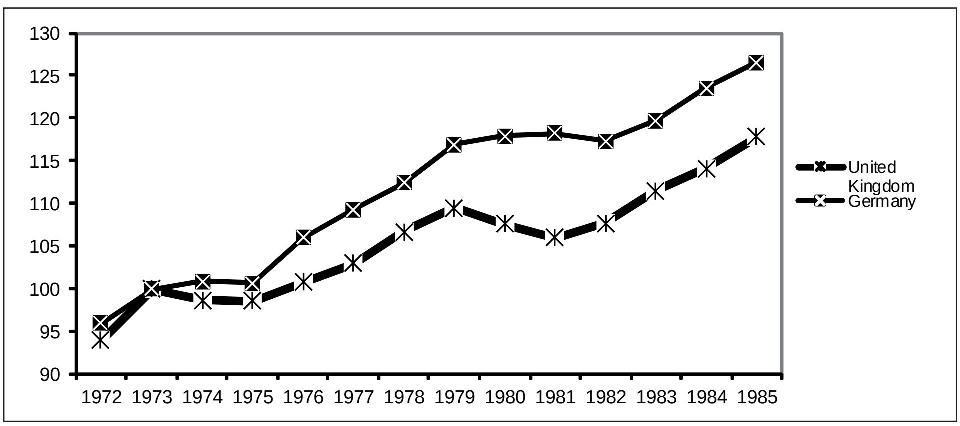
better results in terms of growth. First, we will contrast the experience of West Germany and the United Kingdom, highly industrialised countries with comparable levels of per capita income. We will then analyse the case of Mexico and Argentina, two peripheral countries that both pursued import-substitution strategies during the post-war period, but which had quite different inflationary experiences in the 1970s and 1980s.

In 1973, the United Kingdom had just entered the EEC. The Labour government of Harold Wilson allowed inflation to rise from 9 per cent in that year to 25 per cent in 1975. The following year, Wilson resigned and was replaced by James Callaghan. The new prime minister had to negotiate a financial assistance package with the IMF, which would entail significant cuts in public spending. He managed to reduce the growth rate of the consumer price index to 8 per cent in 1978, but labour unrest and discontent were growing. These circumstances paved the way for Margaret Thatcher's victory in 1979.

Inflation accelerated again during the second oil shock, but somewhat less than it had in the mid-1970s: 1980 closed with an increase in the cost of living of nearly 18 per cent. In addition to closing mines, the Tories facilitated the sale of council houses to private individuals and privatised railways, abolished controls on capital movements, and implemented a drastic fiscal and monetary adjustment. By 1983, they had brought the inflation rate down to 5 per cent, but for the first time since the Great Depression, the number of unemployed had risen above 3 million.

Fiscal policy in Helmut Schmidt's West Germany was quite expansionary during the first oil shock (the deficit was 6 per cent in 1975), but the sole objective of the Bundesbank since its establishment was to maintain price stability, and the bank kept interest rates relatively high in 1973 and 1974. Also,

FIGURE 6 ▪ *Indices of GDP per capita in 1990 GK $ (1972=100)*



Source: By the author, from Maddison. See Note 3.

the SPD's tradition of corporatist negotiation prevented the kind of labour unrest seen in Britain. As a result, in the worst moment of the oil shock (1973) the inflation rate in Germany was just 7 per cent.

Since inflation did not get out of control, the Bundesbank gradually reduced interest rates in West Germany. The overnight interbank rate went from 10 per cent in 1973 to just 4 per cent in 1976. At the end of 1976, the annual growth rate in the consumer price index was less than 4 per cent and the inflation rate was even lower than in 1972.

During the second oil shock, the Bundesbank again raised interest rates. The overnight interbank rate rose from 3 per cent in 1978 to 11 per cent in 1981. This drastic increase was related to the shift toward monetary tightening implemented by Paul Volcker at the Federal Reserve.

In Germany, the most inflationary period during the second oil shock was 1981, when consumer prices rose by 6 per cent. The rate was moderate and it was not necessary to undertake an adjustment like the one implemented in Britain (and other countries, including Italy and Spain). Germany could still afford the luxury of closing the budget with a relatively high deficit (4 per cent of GDP). In 1981, German GDP per capita was 18 per cent higher than the 1973 level, whereas in Britain there had only been a 6 per cent increase over the same period. Eleven per cent of the workforce was unemployed in the United Kingdom, compared to only 4 per cent in West Germany. The CDU returned to power in 1982 after the liberals abandoned their SPD partners. However, unlike the British conservatives, the new administration did not make a radical break with the policy of the previous government headed by Schmidt. They continued to combine negotiated wage agreements with prudent monetary policy, while maintaining relatively high levels of social expenditure.

Another effect of the oil shocks was to create large deposits of dollars and other currencies, from payments for oil, in branches of banks that did not operate in their countries of origin. The so-called Eurodollar market was outside the regulation of national governments and experienced a major expansion thanks to increased deposits by oil exporters. In the 1970s, this market, which contrary to standard practice at the time lent money at variable interest rates, provided emerging countries with large loans that appeared to be backed by strong guarantees. Animal spirits came into play in decision-making on lending, and there was a generally rosy view of the future solvency of recently industrialised countries such as Mexico, Argentina and Brazil, and communist countries like Poland, Hungary and Romania.

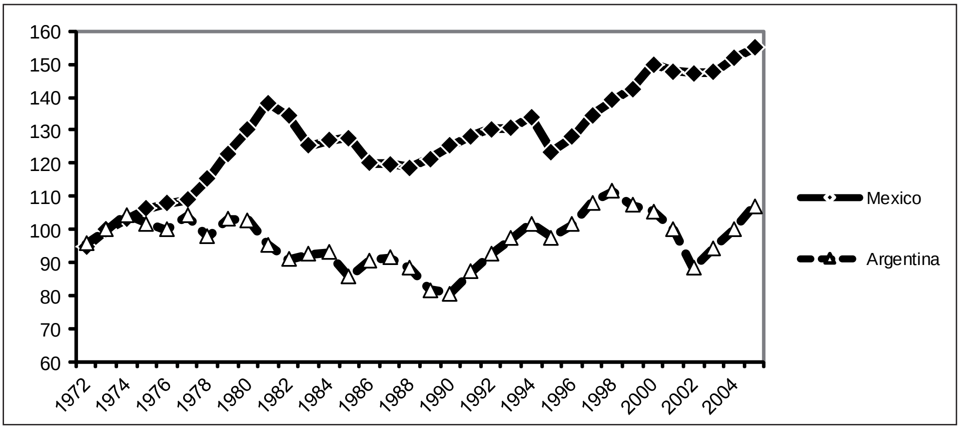
Mexico, for example, had undergone an intense process of industrialisation from 1939 to 1973 based on import substitution. Unlike the vast majority of European countries, Mexico was an oil producer and in theory should have benefited from the spike in oil prices in 1973–1974 and 1979–1980. In the event, during the presidencies of Luis Echeverría and José López Portillo, Mexico's foreign debt continued to rise. A high-spending administration and short-sighted international banks allowed Mexico's public debt to increase from $4.3 billion in 1970 to $68.5 billion in 1982. However, from the point when Paul Volcker changed the monetary policy of the Federal Reserve in 1979, the cost of servicing the debt became increasingly burdensome. Finally, one weekend in August 1982, the finance minister, Jesús Silva Herzog, announced in Washington that without immediate help the country would not be able to meet its upcoming debt maturitie. Mexico's foreign debt crisis erupted and immediately spread to other large debtors such as Brazil. The debt of these countries had to be refinanced by the IMF and other sources of public money, while banks that had previously lent freely now pulled out of Latin America in disarray.

Mexico's expansionary excesses in the 1970s are another clear case of erroneous policy, as evidenced by the fact that inflation gradually rose from 6 per cent in 1972 to a dramatic 61 per cent in 1982. However, without the easy credit provided by short-sighted banks with mistaken expectations, the astronomical levels of indebtedness reached by the Latin American nation would not have been feasible.

López Portillo announced the nationalisation of banks in September 1982, but in the end, the country had no choice but to implement severe adjustments during the six-year term of Miguel de la Madrid. When the president took office in 1983, he adopted contractionary and liberalisation measures to curb inflation, which was running at 90 per cent. The process of debt renegotiation required adjustments throughout the decade and, despite substantial debt reduction under the Brady Plan, Mexico was still in crisis in 1990 when President Carlos Salinas de Gortari proposed the North American Free Trade Agreement. The announcement of the deal improved expectations and led to a new period of euphoria in terms of capital inflows, leading eventually to the so-called Tequila crisis in 1994–1995. Only three years later did Mexico's GDP per capita rise above the pre-crisis level. Thus the Mexican debt crisis did not result in a lost decade, as has often been said: the slump actually lasted around 16 years.

However, the handling of the crisis could have been worse. Although the sheen of the golden age had not been quite as bright in Argentina as elsewhere, like Mexico the country had undergone rapid industrialisation based on import substitution between 1946 and 1974. The Justicialist Party returned to power in 1973 under the leadership of Héctor Cámpora, and Juan Domingo Perón himself returned from exile. At the time, Perón was a supporter of Argentina's social pact, but labour unrest was on the rise and the public deficit reached 6 per cent of GDP. The elderly leader died in 1974 and his wife, Isabel Perón, took over as president. The year closed with an inflation rate of 24 per cent, in line with that of some industrial countris. However, a spiral

FIGURE 7 ▪ *Indices of GDP per capita in 1990 GK $ (1972=100)*



Source: By the author, from Maddison. See Note 3.

of strikes and the lax policy of Isabel Perón's finance ministers allowed inflation to rise to 182 per cent in 1975 and 444 per cent in 1976. The crisis also hit the real economy in these two years.

The military seized power again in 1976 and established a National Reorganisation Process headed by General Jorge Videla. Despite its undeniable political authoritarianism, the military dictatorship chose an extremely liberal finance minister, José Martínez de Hoz, who signed an agreement with the IMF in August 1976 and imposed a brutal economic adjustment that included wage freezes, cutting the public deficit, reduction of tariffs, and liberalisation of interest rates. The new minister managed to cut the deficit from 14 per cent to 3 per cent of GDP and reduce the inflation rate to 259 per cent in 1979, but the real economy collapsed and the country began a dramatic process of deindustrialisation.

From late 1978 to 1981, Martínez de Hoz adopted a system of pre-announced currency depreciation (the *tablita*), but the system had only a limited impact on price developments. The *tablita* policy encouraged capital flight, and the country's external indebtedness rose from $12 billion in 1978 to $33 billion in 1981. Once again international banks were happy to finance a country that seemed to take seriously the recommendations of supply-side economics and rational expectations theorists.

After a brief interlude when the country was under the command of General Roberto Viola, Leopoldo Galtieri became the head of the military junta in late 1981. The conflict with the United Kingdom over the Falkland Islands once again accelerated the rate of inflation, which went from 105 per cent in 1981 to 165 per cent in 1982. As a result of the Mexican debt crisis, Argentina also received a new IMF loan so that it could continue servicing its debt.

But inflation soared to 343 per cent in 1983. GDP per capita remained low; when the dictatorship ended it was 11 per cent below the 1974 level.

In December 1983 a new, democratically elected president —the radical Raul Alfonsín— took office, but he was unable to prevent the inflation rate from reaching 671 per cent in 1984. The Austral Plan appeared to contain inflation in 1986–1987, but expansionary excesses at the end of Alfonsín's term led to another upward spiral in prices. In 1989, the year of the transition to the presidency of Carlos Saúl Menem, Argentina ended the year with an increase in prices of more than 4,000 per cent, that is, hyperinflation.

The Justicialist president implemented a rigorously neo-liberal programme based on privatisations, spurred on by Mercosur, and deregulation. His finance minister, Domingo Cavallo, who was appointed in early 1991, succeeded in turning around inflationary acceleration by restoring a convertibility system that fixed the dollar-peso exchange rate at one peso per US dollar. Argentina had an inflation rate of 0 per cent in 1996. The defeat of hyperinflation was an undeniable success, but the fixed exchange rate with the dollar, combined with the impact of devaluations by Brazil, generated new problems of competitiveness in Argentina towards the end of the twentieth century, leading ultimately to the *corralito* (a partial freeze of bank accounts).

In short, a series of expansionary excesses and the need for dramatic adjustments to curb bouts of inflation caused Argentina's GDP per capita to remain below the 1974 level for nearly two decades. These excesses, which were not the direct result of import substitution, also led to the country's industrial decline.

The first crises of deregulation and European unification

The experience of the 1970s and 1980s had shown that expansionary policies did not work in the medium term in a context of high inflation. However, the best results achieved by prudent responses to the evolution of the price level during the crisis were interpreted —I believe wrongly— as a defeat for Keynesian principles. The prevailing view among academics and politicians (the so-called Washington Consensus) was that rather than managing demand, governments should free markets of any state intervention. Although the Argentine experience tended to refute this view, many industrial countries followed the lead of Margaret Thatcher in the United Kingdom and focused on deregulation.[7]

7. To examine the crises associated with deregulation and the process of European monetary unification, I have used the following works, among others: Osugi (1990), Pekkarinen, Pohjola and Rowthorn (1990), Fitoussi (1996), Korpi (1996), Rothermund (1998, 2008 and

The East did not escape this shift towards deregulation. In this section we will begin by comparing the recent experience of Asia's two great democracies: Japan and the Republic of India. Both countries underwent deregulation processes from the 1980s onwards, but while Japan implemented changes rapidly without placing any limits on speculative excesses, India introduced greater market competition gradually, without completely breaking with the mixed-economy model that had been adopted by the Indian National Congress party after the country gained independence in 1947.

During the economic golden age, Japan had grown very strongly by importing technologies developed in the West during the second industrial revolution and adapting them to the local context. A national innovation system and a distinctively Japanese institutional framework had contributed to improving Western technologies. The reforms imposed by General MacArthur sought to put an end to the *zaibatsu* (family-controlled holding companies), but special relationships between industrial companies and banking houses were rebuilt in the post-war period, giving rise to the *keiretsu*. Cross-shareholding ensured group companies privileged access to credit. These cooperative ties between industry and finance were reinforced by the strategic policy of the Japanese Ministry of International Trade and Industry (MITI). Dominant cooperative relationships, strongly influenced by the legacy of Confucianism, also included suppliers and workers. The latter were guaranteed jobs for life, and salaries were strongly linked to seniority. The deregulation of the capital market around 1984 was intended to give banks the freedom to operate without government-imposed restrictions. Interest rate ceilings on deposits were eliminated, barriers between commercial and investment banking were removed, and banks were allowed to borrow abroad. In a country with little land in relation to its population, banks threw themselves into financing the real estate sector, spurred on by a sharp reduction in interest rates by the Bank of Tokyo. They also focused on financing stock exchange transactions, which in the short term offered much higher yields than industry thanks to the meteoric rise of the Nikkei index.

The resulting property and financial bubble in Japan led countless families to sign two-generation mortgages. At one point, the square mile surrounding the Emperor's Palace in Tokyo reached a value equivalent to that of all the land in the state of California. The market capitalisation of Japanese listed companies ended up exceeding that of all US corporations, even though

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2012), Krugman (1999 and 2012), Catalan (2002 and 2012), Stiglitz (2003), Brenner (2006), Panagariya (2008), Eichengreen and O'Rourke (2009), James (2009), Koo (2009), Chang (2004 and 2010), Roubini and Mihm (2010), Amatori and Colli (2011), Kobrak and Wilkins (2011), Kudaisya (2011), Parejo and Sudrià (2012), Boyer (2013), Louçã and Mortágua (2012), Comín and Hernández (2013), Fitoussi and Saraceno (2013) and Llopis and Maluquer (2013).

the Asian country had less than half the population of the USA. Japanese banks enthusiastically provided unlimited credit for property purchases and stock exchange transactions in a manner that evoked the Keynesian animal spirits that had driven the 1929 bubble. And the end result was similar.

After the bubble burst, the Nikkei index gradually fell from almost 40,000 points at the end of 1989 to 15,000 points in 1992, and just 8000 points in 2003. Commercial property prices in Japan's six major cities declined by 87 per cent from 1990 to 2004.

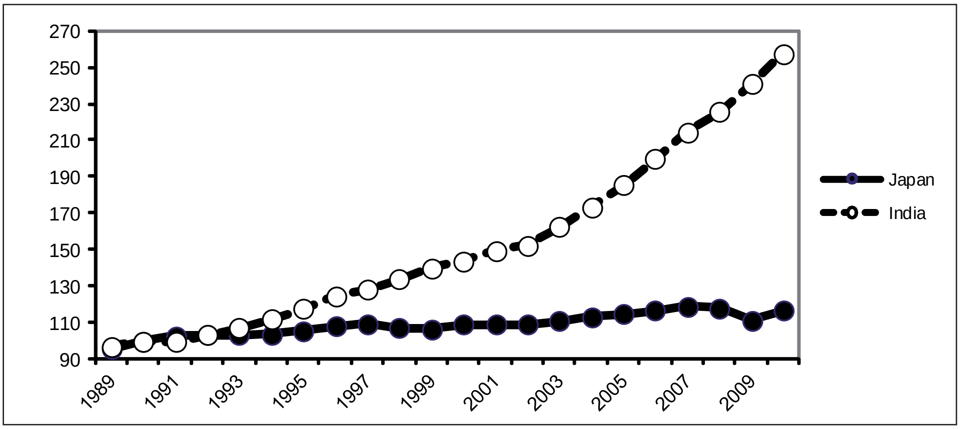
The Japanese government implemented a strongly expansionary monetary and fiscal policy, as Keynes would have recommended. The short-term interest rate was lowered from 7.7 per cent in 1990 to 0.6 per cent in 1996. The budget went from a surplus of 2.9 per cent of GDP to a deficit of 4.2 per cent over the same period. Although the policy could not prevent a fall in the Japanese growth rate, it did help ensure that GDP per capita declined only in 1993.

In 1996, inflation in Japan was negligible (0.1 per cent growth in the cost of living). Nevertheless, in 1997, the government of Prime Minister Ryutaro Hashimoto (like Roosevelt in 1937) attempted to balance the budget by increasing the consumption tax rate and social security contributions, eliminating deductions on income, and reducing public spending. This policy, which remained in place in 2001 under the Koizumi Cabinet, aggravated the banking crisis and led to the longest decline in Japan's GDP per capita since the 1950s (from 1998 to 2002). Subsequent governments adopted a more expansionary policy, but the situation became critical once again when the global slump began in 2008. From 1950 to 1990, Japan's GDP per capita grew at an average rate of 5.9 per cent annually. In contrast, since 1990 it has risen at an average rate of just 0.9 per cent. Rapid deregulation and lax monetary policy in the second half of the 1980s and misguided attempts to achieve fiscal consolidation at the end of the century stifled Japanese growth.

After gaining its independence, India pursued a strategy of import-substitution industrialisation, first undertaken by Jawaharlal Nehru in 1947, and intensified by his daughter, Indira Gandhi, from 1966. Growth in GDP per capita was much slower than in the more open, industrialised economy of Japan, averaging only 1.4 per cent annually from 1950 to 1980. However, this was still a significant improvement on the period of British rule, when GDP per capita had remained stagnant from 1890 to 1947.

Lack of competition, made possible by a very restrictive system of investment licences known as the "Permit Raj", made industry in India very uncompetitive at the international level and caused the country's global export share to fall from 2 per cent in 1947 to just 0.4 per cent in 1980. However, import substitution in the Asian country did not create the kind of extreme imbalances experienced in Latin America. At the worst point in the turbulent 1970s (1974), inflation was 28 per cent, a rate similar to that recorded in the

FIGURE 8 ▪ *Indices of GDP per capita in 1990 GK $ (1990=100)*



Source: By the author, from Maddison and OECD. See Note 3.

bad years in the European periphery, and negligible compared to the rates seen in Mexico and Argentina. Although India borrowed from international lenders and ended up requiring assistance from the IMF, when the Mexican crisis broke out, foreign debt per capita was much lower than in Latin American countries: $39 per capita in India as opposed to $1,261 per capita in Argentina in 1983.

India began a period of gradual reforms that did not break sharply with the import-substitution model or the mixed-economy approach that had been advocated by the Congress Party since the end of British rule. After his mother's assassination by her Sikh bodyguard in 1984, Rajiv Gandhi abolished the licence system in 30 industries, promoted the creation of joint ventures with foreign capital, and intensified efforts to reign in price growth. Although the Congress Party lost the 1988 elections and Nehru's grandson handed over power, the annual inflation rate had been reduced to just 7.5 per cent by that time.

India experienced its most recent major crisis in 1991. The country had borrowed excessively between 1988 and 1991 and its foreign debt had risen from 55 to 79 per cent of GDP. In 1990, Indian emigrants left the Gulf as a result of the war that followed the invasion of Kuwait, and external reserves plummeted. The assassination of Rajiv Gandhi by the Tamil Tigers in the middle of the 1991 election campaign contributed to a lowering of expectations.

Following the return of the Congress Party to power the same year under the leadership of Narasimha Rao, Manmohan Singh was appointed finance minister. Singh, an economist trained at Cambridge University, took reforms further. He definitively abolished the Permit Raj, reduced tariffs, facilitated foreign investment, and substantially devalued the rupee. Industry and services responded positively to this package of incentives. Since then, the country has experienced accelerated expansion in areas related to the third technological revolution, such as software production and telecommunications, as well as more traditional areas (from diamonds to cars and pharmaceuticals).

In 2004, following the election victory of a coalition led by the Congress Party, Singh was chosen as prime minister. He has continued along the path of reform without breaking completely with the legacy of the past. Inequality on the subcontinent has continued to decline since the 1970s. The mixed economy has stood up well, with government-owned corporations in the banking sector, the steel industry, and the energy and rail sectors. From 1990 to 2011, India's GDP per capita grew at an annual rate of 5 per cent. By pursuing gradual reforms and avoiding speculative excesses, India was able to shift from slow to rapid growth. As a result of rapid deregulation and rampant speculation, in Japan the opposite happened.

Turning our attention once again to the West, there have been three major crises since the triumph of deregulatory policies in the United States and Europe: the slump of the early 1990s, the crisis associated with the bursting the dot-com bubble around the turn of the century, and the current major slump, which began around 2007. According to our indicator, the two crises that have had the greatest impact are the first (eight economies) and the last (ten economies). We will therefore focus on these two slumps. However, before turning to this final comparison, it should be noted that yet again the worst moments of crisis were preceded by intense speculation. Before 1993, investment funds bet in favour of the Deutsche Mark and against the weaker currencies of the European Monetary System (EMS), such as the pound and the currencies of Mediterranean and even Nordic countries. In the second half of the 1990s, the frenzy focused on shares in technology companies involved in information processing and transmission. In the early 2000s, speculation revolved around subprime mortgages and was facilitated by the repeal of the Glass-Steagall Act in the United States and financial innovations such as securitisation. These three bouts of euphoria gave rise to broader crises that varied in intensity according to the imbalances generated and the policies adopted to tackle them.

In Europe, the surrender of monetary sovereignty, part of a half-hearted move towards unification, has been an additional and particularly damaging element of instability. The criteria agreed at Maastricht in 1991, intended to pave the way for monetary union, were a key factor behind the intensity of the crisis of the early 1990s. The adoption of the euro and the fact that most central banks in the European Union have given up the right to issue their own currency has also been a major factor in the magnitude of the current slump.

In order to test the theses set out above, we will compare the case of Sweden and Spain, two EU countries that drew very different lessons from the crisis of the 1990s, and whose policies clearly diverged towards the end of that decade. Sweden, though a member of the EU since 1995, has never given up its right to issue kronor, whereas Spain abandoned the peseta with the faith of a true believer.

In the second half of the 1980s, Sweden had low inflation, a budget surplus, an extremely low unemployment rate (1.5 per cent in 1989), and one of the lowest levels of inequality in the world. However, the Social Democratic government of Ingvar Gösta Carlsson chose to change direction, abandoning the path that the country had followed since the 1930s. The domestic financial system was deregulated, exchange controls on capital transactions were eliminated, and a fiscal counter-reform that reduced direct taxes and progressivity was implemented. These measures resulted in a major housing boom. Also, in 1991 the krona entered the EMS with a narrow fluctuation band of 1.5 per cent.

It was in 1991 that the real estate and financial bubble burst. GDP per capita fell and the first bank rescue took place. The Social Democrats lost the elections and were replaced by the conservative cabinet of Carl Bildt, who cut public spending, raised taxes, imposed privatisations, and pursued a tight monetary policy to maintain the parity of the krona within the EMS. During the monetary storm that hit late in the summer of 1992, the Sveriges Riksbank increased the discount rate to an astronomical 500 per cent to defend the krona against attacks from speculators. In September the institution was able to withstand the pressure, but only by massively increasing the cost of money. In November, the situation became unsustainable and the krona left the EMS, becoming a free-floating currency again.

As a result of the policies adopted, investment fell by 17 per cent in 1993. The unemployment rate climbed to 8.2 per cent, and a quarter of banks had to be bailed out with public funds. The budget deficit grew to an astronomical 15 per cent of GDP in 1994, and by 1996 the public debt had reached 73 per cent of GDP. Sweden experienced the longest crisis in its history. It was not until 1996 that GDP per capita rose above the 1991 level, which means the country went through a five-year slump. In contrast, the crisis of the 1930s lasted only three years in Sweden (which abandoned the gold standard along with Britain).

The depth of the crisis favoured the return to power of the Social Democrats under the leadership of Carlsson. In 1996 he was succeeded as prime minister by Göran Persson, who up until that time had been the finance minister. To tackle the ballooning deficit and debt, Persson increased the tax burden on high-income earners and capital and cut military spending. Corporate agreements, which are characteristic of the Nordic model, facilitated control of inflation. As the economy recovered, the deficit was reduced and in 1998 the budget was back in surplus. The Swedish government decided not to rejoin the EMS, so it was not part of the majority group of EU countries that adopted the single currency in 1999. The Swedish people confirmed this rejection of the single currency in a referendum held in 2003. At that point, Sweden was continuing to run a budget surplus and the public debt had fallen to 51.7 per cent of GDP. Persson had reaped the rewards of exercising fiscal discipline during a period of growth, as recommended by the Keynesian paradigm.

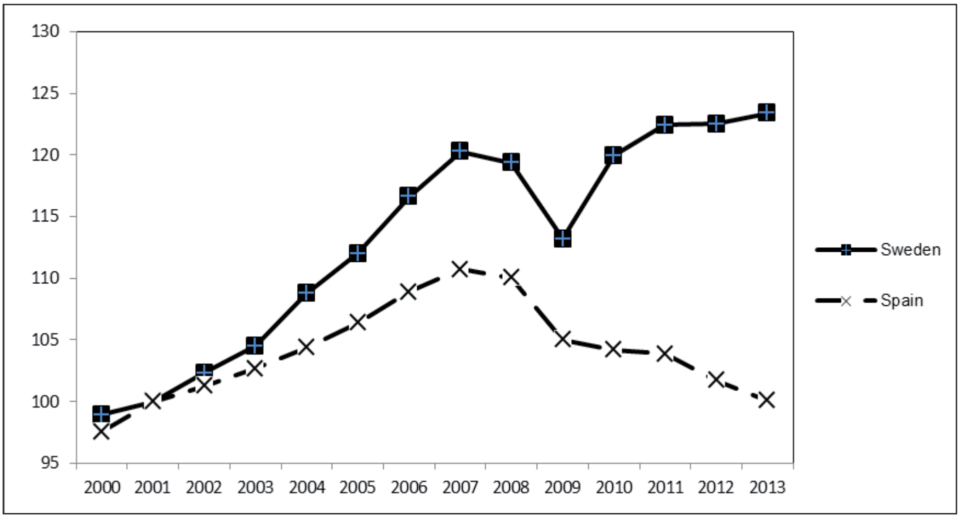
Outside the euro, Sweden recorded a GDP growth rate that was quite acceptable for a rich country (2.5 per cent annually for 2000–2007). The debt shrank to 45.3 per cent of GDP in 2006. Despite these good results, in 2006 John Fredrik Reinfeldt emerged victorious in the Swedish general election as the leader of the Alliance for Sweden coalition. The Scandinavian country has not been able to completely avoid the impact of the current slump, because it depends on the level of activity of its European partners. However, at the worst point in the downturn (2009), Sweden's GDP per capita was only 10 per cent below the 2001 level. According to our criteria, Sweden emerged from the crisis in 2011. In April 2013, the unemployment rate was just 8.4 per cent. The contrast with the trajectory of the so-called PIIGS or GIPSI countries in the European periphery could not be more revealing.

Spain joined the EMS in 1989 with a fluctuation band of 6 per cent and a central parity that overvalued the peseta. In a country experiencing higher inflation than its trading partners, this exchange rate could only be maintained thanks to increasing foreign capital inflows in the years leading up to the Olympic Games in Barcelona. Despite high growth over this period, the government of Felipe González did not reduce the public deficit; in fact, it rose from 3.3 per cent of GDP in 1988 to 4.3 per cent in 1992. Moreover, one of the macroeconomic convergence criteria set out in the Maastricht Treaty for future members of the monetary union was the observance of the normal fluctuation margins provided for by the EMS exchange-rate mechanism for at least two years without any parity changes.

When speculators attacked weak currencies in the zone and caused the monetary storm of 1992, Spain was one of the first members to devalue its currency (in September of the Olympic year). Successive devaluations continued until 1995, and the country also benefited from a broadening of the EMS fluctuation band to 15 per cent, which in practice meant the abandonment of a fixed-rate system.

During the crisis, the deficit rose to 6.7 per cent of GDP in 1993, and unemployment reached 23.7 per cent of the workforce in 1994, while the public debt was over 66 per cent of GDP. The 1993 slump had a relatively mild impact on Spain's GDP per capita thanks to the effect of the depreciation of the peseta on external trade. However, high unemployment, which was still running at 22.2 per cent in 1997, paved the way for the victory of the Popular Party in the general elections held that year.

FIGURE 9 ▪ *Indices of GDP per capita in 1990 GK $ (2001=100)*



Source: By the author, from Maddison and OECD. See Note 3.

The first government of José María Aznar reduced the deficit by pursuing a broad programme of privatisations and was able to reduce the budget deficit to 1.0 per cent of GDP in 2000. The public debt declined to 59.4 per cent of GDP, the inflation rate was around 3.5 per cent, and unemployment fell to 10.8 per cent of the workforce.

Strong growth in the last five years of the twentieth century was driven largely by the devaluations of 1992–95. Despite this, conservative and socialist politicians, along with the vast majority of Spanish academics, eagerly embraced the single currency. Unlike their counterparts in Sweden and the United Kingdom, decision-makers in Spain were unwilling to learn from the crisis of the early 1990s. Few mourned the death of the peseta or the transfer of monetary sovereignty to the European Central Bank.

Aznar's second government and the first one headed by José Luis Rodríguez Zapatero benefited from the false euphoria generated by accommodative US monetary policy and the initially high expectations generated by the adoption of the euro. The repeal of the Glass-Steagall Act and Alan Greenspan's decision to lower interest rates in 2001 (in response to the bursting of the technology bubble), combined with innovations such as securitisation, facilitated the rise of subprime mortgages. These developments gave rise to a new financial and real estate bubble in the West. Moreover, in the euro zone, downward convergence of interest rates led the peripheral countries to increase their indebtedness at a dizzying pace. In the case of Spain, this madness was particularly strong due to intense migratory flows in the early 2000s. In the Iberian Peninsula the euphoria also reflected the animal spirits that were driving decision-making in financial institutions. Savings banks had been deregulated around 1990 and grew at a frenetic pace by opening branches throughout the country and concentrating their assets in mortgages and loans to property developers.

Governments took advantage of strong growth up to 2007 to reduce the deficit and the debt of public authorities. At the end of the year, there was a budget surplus of 2 per cent of GDP, and public debt fell to just 36.3 per cent of GDP. Inflation, though, was always significantly higher than in Spain's major trading partners, France and Germany.

Nevertheless, in the run-up to the 2008 elections and in 2009, the governments of José Luis Rodríguez Zapatero took the deficit to a level that was unprecedented in modern history: over 11 per cent of GDP. Although inflation was close to zero and a certain degree of fiscal expansion could be justified, the magnitude of the stimulus was excessive. Most importantly, the fiscal expansion did not take into account the fact that the Bank of Spain could no longer issue currency if unable to find buyers for its debt. Furthermore, in an effort to tackle the insolvency of a growing number of financial institutions, the government and the central bank pursued a policy of forced bank mergers and privatisation of savings banks, which has turned out to be a complete fiasco. This policy has led to the virtual disappearance of institutions whose origins date to the nineteenth century and an unprecedented socialisation of losses.

In the spring of 2010, major creditors informed the Spanish prime minister that they were unwilling to continue buying public debt unless there was a radical change of policy. Speculators started to demand higher premiums to buy Spanish debt.

From that point on, Zapatero's government changed the policy direction and began to implement what could be called the Berlin Consensus, imposing a severe fiscal adjustment that was to have a particularly significant impact on workers' wages, public investment and social expenditure. The Popular Party government of Mariano Rajoy, which took office in 2012, continued down the same path. A draconian labour reform was implemented, the tax burden was further increased, and a European loan of up to €100 billion —guaranteed by the Spanish budget— was negotiated to recapitalise insolvent financial institutions.

The route of internal devaluation, adopted in May 2010, has barely made a dent in the deficit, which after the 2012 bank rescue was again around 11 per cent of GDP. The public debt has soared to 84.2 per cent of GDP, and unemployment reached a historic high of 27 per cent in the spring of 2013. According to our indicator, Spain has now gone through a gruelling six-year slump. Moreover, the problem is not confined to the Iberian Peninsula. A number of peripheral EU states (the so-called PIIGS or GIPSI) are affected, and unlike Sweden or Denmark, these are countries that embraced the euro with blind enthusiasm.

Conclusions

For the purposes of this paper, we have defined a crisis as a period during which real GDP per capita remains below the previously recorded peak. When this criterion is applied to a sample of 12 economies representative of the global economy, we find that the worst moment between 1928 and 2013 was the three-year period from 1931 to 1933 (when 11 countries were experiencing a slump). The crisis was caused by the speculative excesses of Wall Street between 1926 and 1929, and the contractionary policies subsequently implemented turned it into a Great Depression. Since the crisis was one of effective demand and therefore entailed generalised deflation, countries that applied expansionary policies and broke the rules of the gold standard recovered more quickly.

Crises became less frequent after 1945 thanks to the Bretton Woods Agreements and the application of demand-management policies. The former allowed for devaluation and establishment of exchange controls on capital movements; the latter made it possible to expand the economy when the problem was lack of growth and cause it to contract when inflation was the greater risk. As a result, the number of countries in crisis gradually decreased until they practically disappeared in the 1970s.

From 1974, crises became more frequent again. Those which occurred during the period of stagflation were caused mainly by oil shocks, but short-sighted lending practices in the lightly regulated Eurodollar market also had a destabilising effect. The simultaneous occurrence of inflation and a drop in economic activity posed a significant dilemma for demand-management policies. Countries that controlled inflation from the outset and were prudent in their use of credit experienced milder crises than those which adopted highly expansionary policies, allowed inflation to accelerate, and relied heavily on external financing. Countries that took the latter approach ended up requiring severe adjustments that had a high cost in terms of real growth.

The main slumps since 1990 have again been caused by the speculative excesses of deregulated capital markets, which were rapidly liberalised in a context of lax monetary policy. Europe's process of unification by half measures also contributed to increasing global instability. With ten of the sample countries in crisis in 2009, the current slump is the most intense to hit the global economy since 1945. Like the gold standard in the interwar period, at the outset of the twenty-first century the dream of the euro led much of Europe into an economic catastrophe.

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From the Great Depression to the Euro Crisis, 1929-2013: A Global Approach

ABSTRACT

This article identifies the main global crises that have occurred since 1929 and analyses their causes by focusing on a sample of 12 significant economies. A comparative historical analysis is used to show that major global slumps resulted from a combination of excessive speculation in financial markets and government mishandling of demand-management policies.

KEYWORDS: cycles, global depressions, financial crises, demand-management policies

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De la Gran Depresión a la crisis del euro, 1929-2013: un enfoque global

RESUMEN

Este artículo identifica las principales crisis globales desde 1929 y analiza sus causas, a partir del estudio de una muestra de 12 economías relevantes. Utiliza la historia comparativa para postular que las grandes depresiones globales han derivado de la combinación de excesos de especulación financiera y la falta de acierto en la aplicación de políticas de regulación de la demanda.

PALABRAS CLAVE: Ciclos, depresiones globales, crisis financieras, políticas de demanda

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