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## **The Myth of War Prosperity, Part 2**

**by Anthony Gregory**

*Depression, War, and Cold War: Studies in Political Economy* by Robert Higgs (Oxford University Press: 2006); 240 pages; \$35.

So the New Deal was far from a success. But most conservatives and even many leftist scholars will concede this; they simply adopt a different, and even more widely accepted fallacy, the one of “war prosperity,” which Higgs canvasses in chapter 3. “According to the orthodox account,” he writes,

the war got the economy out of the Depression. Evidence for this claim usually includes the great decline in the standard measure of the unemployment rate, the large increase in the standard measure of real gross national product (GNP), and the slight increase in the standard measure of real personal consumption.

What’s more, the apparent boom is “understood by most authors as an obvious validation of the simple Keynesian model: Enormous government spending, with huge budget deficits, spurred the military economy and produced multiplier effects on the civilian economy, with the upshot being increased employment, real output, and consumption and decreased unemployment.” Higgs analyzes the various ways in which the economy supposedly improved. In terms of the unemployment rate’s plummeting,

What actually happened was no mystery. In 1940, before the mobilization [for war], the unemployment rate ... was 9.5 percent. During the war, the government pulled the equivalent of 22 percent of the prewar labor force into the armed forces. Voilà — the unemployment rate dropped to a very low level.

And Higgs reminds the reader that

the welfare significance of the decline is hardly the usual one. Of the 16 million persons who served in the armed forces at some time during the war, 10 million were conscripted, and many of those who volunteered did so only to avoid the draft and the consequent likelihood of assignment to the infantry.

For all these people, being employed did not exactly mean an improvement in their standard of living. As for the common contention that “real personal consumption increased during the war,” Higgs notes that it

fails to take sufficiently into account the understatement of actual wartime inflation by the official price indexes, the deterioration of quality and disappearance from the market of many consumer goods, the full effect of the nonprice rationing of many widely consumed items, and the additional transaction costs borne and other sacrifices made by consumers to get the goods that were available. When one corrects the data to provide a more defensible measure of what happened to real consumer well-being during the war, one finds that it declined.

The author also demonstrates how government expansion during World War II might explain why

from 1941 to 1943, real gross private domestic investment plunged by 64 percent; during the four years of the war, it never rose above 55 percent of its 1941 level [and] only in 1946 did it reach a new high.

None of this should be a surprise to those who believe free enterprise is more productive than a command-control economy. Indeed, even the New Deal allowed for far more capitalism than the war did. During the 1930s, the price system and the fundamental principles of markets were in play, severely battered though they were by Roosevelt’s policies. But during the war

the government imposed such pervasive and sufficiently effective controls that by the beginning of 1943, the economy became a thoroughgoing command system. This regime persisted until the fall of 1945, when the controls began to come off rapidly.

And in fact, as Higgs shows in starker detail than can be given here, it was the *end* of such controls — along with the expectations of the war’s ending, as such expectations began to positively revive the stock market in 1945 — that finally brought about prosperity. While Higgs does grant some possible importance to a revived faith in the power of American productivity that came about with the war, he persuasively maintains that the war itself did not end the Depression.

Indeed, “as the war ended, real prosperity returned almost overnight.” Just as the illusory methods relied on by mainstream economists have shown a supposed economic boom during World War II, so do they deceptively indicate a depression in 1946. In fact, as Higgs shows in his chapter “From Central Planning to the Market: The American Transition, 1945–47,” the immediate postwar period was an extraordinary episode of a command economy’s retracting rapidly to give way to a much more liberalized market economy. The author even compares this transition to that seen in China’s and the Warsaw Pact nations’ moves toward the market. And while

in various respects, the [U.S.] government never surrendered the powers that it had assumed during the war ... by the latter half of 1947, the economy had reverted to operating as a market system about as far as it ever would.

Among other important implications, this liberalization

encouraged investors and businessmen to act, for the first time since the early 1930s, as if their property rights in their capital and the income it generated would remain reasonably secure.

Thus did “regime uncertainty” end, and thus can we explain the relative economic prosperity America has enjoyed since the end of the Second World War.

### **The Cold War and beyond**

Of course, the Great Depression and World War II are not the only events whose contemporary accounts are riddled with macroeconomic confusion. The Cold War and the modern warfare state in general are gravely misunderstood. Thankfully, in addition to his important treatment of the New Deal and the myth of wartime prosperity, Higgs takes on many other standard misconceptions and neglected issues of 20th-century U.S. political economy. The chapter “The Cold War Economy: Opportunity Costs, Ideology, and the Politics of Crisis” is a mini-treatise on the political economy of the Cold War, the uniqueness of which is generally ignored, despite its being a relatively recent, unprecedented development.

Before World War II, the allocation of resources to military purposes remained at token levels, which occurred infrequently. Wartime and peacetime were distinct, and during peacetime — that is, nearly all the time — the societal opportunity cost of “guns” was nearly nil. The old regime ended in 1940.... Despite an enormous demobilization after the war ended, in 1947, at the postwar trough, the military sector still accounted for 4.3 percent of GNP, three times the 1939 share.

So unlike what happened after other major wars, at the end of World War II a huge military apparatus remained. This unique character of the Cold War manifests itself in many ways, especially in the political dynamics of spending. Higgs uncovers a distinct reverse correlation between military spending, on the one hand, and private spending and nonmilitary government spending on the other, and ponders such puzzles as how to account for the buildup during the Carter-Reagan years, which no major hot war such as Vietnam could explain.

Running through the book from beginning to end is a deep analysis of the many facets of the U.S. warfare-state economy. Chapter 4 investigates the profound effects of government involvement in investment, its displacement of private investors, and its distortion of capital formation during the 1940s. The perversity of politicized incentives in supposed “national defense” spending is exposed in chapters 7 and 8, where Higgs scrutinizes the tendency of Congressional “pork hawks” to funnel large sums of tax dollars to pet projects for electoral purposes, even when the Pentagon itself has not requested such lavish expenditures.

Then there’s chapter 10, titled “Public Opinion: A Powerful Predictor of U.S Defense Spending” and coauthored with Anthony Kilduff, in which Higgs and Kilduff suggest that, while spending tends to go up and down with public support for militarism, we can probably suspect public opinion itself to be influenced considerably by politicians motivated, independent of popular interest, to promote militarism. Particularly of note is the way Higgs has homed in on the defense contractors, the corporate players that reap the gains of a bureaucracy gone out of control and with virtually no accountability to anyone. Misunderstood as the free market in action both by enemies on the Left and by supporters on the Right — in 2004, there was even a *Wall Street Journal* editorial defending Halliburton as a paragon of “private enterprise” — the defense industry is actually one of the greatest disgraces to capitalism in our time, and Higgs has been one of its most trenchant critics for decades.

In chapter 2, “Private Profit, Public Risk,” Higgs chronicles the entrenchment of what has become a permanent sector of the American economy, an enormous corporate apparatus with twisted incentives and all its operational costs socialized to taxpayers. He shows in particular how, despite conventional wisdom, “the essential foundations of the modern military-industrial complex were laid out during the defense period preceding the Japanese attack on Pearl Harbor” — that is, in a time of relative peace, and all thanks to Franklin Roosevelt.

In chapter 9, he, along with coauthor Ruben Trevino, scrutinizes the profits reaped by defense contractors, concluding that over a two-decade period at the end of the Cold War, “by every measure, the top defense firms outperformed the market by a huge margin.”

### **The once unseen now revealed**

The Iraq War has not brought about war prosperity as advertised, nor has it resulted in cheaper gas the way cynical leftist critics thought it was intended to. People might have learned a

bit of a lesson about this, but in the future we can expect economic misunderstanding to once again flavor discussion about a forthcoming war. To avoid repeating this sordid dialogue ad nauseam, we need to attack the fundamental reasons that people keep buying into the same old myths. For many years, libertarians have complained about big government and have understood on a theoretical level at least how even such universally accepted government projects as World War II and the permanent warfare state it ushered in, as much as any lesser public program, must subsist at the cost of, not toward the advancement of, America's general economic well-being. Unfortunately, the myths and misunderstandings surrounding the U.S. garrison economy — its alleged promotion of productivity and the general welfare and its ostensible nature as an essentially capitalistic sector free of the trappings borne by the classic archetypes of socialist central planning — have endured.

To defeat these myths, which enable the World War II–Cold War military-industrial-complex to persist at great cost to Americans' wealth, to say nothing of their liberty, we need more than just theory. The broken-window parable and similar wisdom are necessary to our understanding but not sufficient for winning the intellectual and ideological struggle to reclaim our freedom from the warfare state. We also need hard facts and deep analysis if we are to let stubborn myths about war prosperity die and if we are to defeat the deceptions obscuring leviathan and preserving the military establishment. In *Depression, War, and Cold War*, Robert Higgs has done the work of many scholars toward this goal of unsurpassable importance.

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**This article was originally published in the January 2007 of *Freedom Daily*.**