Chapter 3 - Reconstruction Aid and Economic Outcomes.

Rodrigo Zeidan

The Marshall Plan was a cornerstone of the post-World War II global order. It was one of the largest income transfer programs in the world's history, with USD 13 billion going from the United States to Western Europe in the years 1948 to 1951 (De Long & Eichengreen, 1993). The Plan had multiple political objectives: to prevent the rise of extreme nationalist parties; limit the influence of socialism in the region; and increase opportunities for American companies to expand. Not all authors believe that the Plan was successful. Wood (1986) argues that it was a failure and that it was popularly defined as a success by the ex-post redefinition of its goals, going as far as stating that the subsequent Mutual Security Agency was more relevant for European stability. But regardless of its relative status, there is ample evidence of the economic impact of the Marshall Plan on European countries.

Nicola Bianchi and Michela Giorcelli (2018) study the effects of international reconstruction aid on long-term economic outcomes, by analyzing the effects of the Marshall Plan on the Italian economy. In May 1945, when WWII in Italy formally ended, GDP per capita was 38 percent lower than in 1938, while industrial production was 66 percent lower. Damages to public infrastructure represented the main challenge towards recovery: 70 percent of the roads had been damaged and 45 percent of the railroad system was no longer usable (Lombardo, 2000 and Fauri, 2006). Bianchi and Giorcelli show that provinces that received more reconstruction grants experienced a larger increase in the number of industrial firms and workers. Individuals and firms in these areas also started developing more patents. The same provinces experienced a faster mechanization of the agricultural sector. Motorized machines, such as tractors, replaced workers and significantly boosted agricultural production. Finally, they show how reconstruction grants induced economic growth by allowing Italian provinces to modernize their transportation and communication networks damaged during WWII.

The groundbreaking work by Bianchi and Giorcelli allows us to understand and disentangle the local effects of ambitious global geopolitical programs. They relate the war reconstruction effort to the damage of the bombings in Italy during World War II. They use an example of two adjacent provinces: "Verona and Vicenza, which in 1937 had similar population size (585,893 vs. 559,375), population density (189 residents per squared km vs. 201), number of industrial firms (9,133 vs. 9,018), number of industrial workers (64,557 vs. 81,479), and number of agricultural workers (128,608 vs. 105,848). In addition, the two provinces were exposed to similar total war damages: 0.47 percent of population killed during WWII in Verona, relative to 0.46 percent in Vicenza. The province of Verona, however, connected central and southern Italy to the Brenner Pass, which the Third Reich used to deliver supplies to German troops stationed in Italy. After March 1944, the Allied air forces heavily bombed the transportation and communication networks in the province of Verona (5,928 tons against troops, railways, or roads), but not in the province of Vicenza (653 tons against troops, railways, or roads). Between 1948 and 1952, the province of Verona received $101 million (2010 USD) for reconstruction, while the province of Vicenza only $75 million." They are able to compare industrial and agricultural outcomes across these two types of provinces to identify the effect of reconstructing and modernizing public infrastructure.

When relating to our version of the Solow Model, their work illustrates the interdependency between capital and labor accumulation and how economies do not take a unique path to development. The Marshal Plan was not the only factor in the development of Italian municipalities, of course, but was an important source of funds that allowed some regions to grow quicker than the others. More importantly, we should keep in mind that aid by itself is not enough. In the case of Italy, aid did lead to capital and labor accumulation over time, something that might not have happened if resources were funneled to an extractive elite.

## Questions for discussion:

1) Europe went through a Golden Age of economic growth from the end of the World War II until the recession of the mid-1970s due to, among other factors, the first oil crisis. Describe, using the framework of the version of the Solow Model in chapter 3, the mechanisms through which the Marshall Plan could influence the long-run growth of European economies.

2) Development aid is a controversial subject. Two influential figures in the global debate are Jeffrey Sachs and Willian Easterly. Sachs argues that foreign aid can be the main factor in eliminating extreme poverty (take, for instance, his 2005 article on Scientific American), while Easterly is skeptical of the tyranny of experts, claiming that the fight against global poverty suppressed individual rights (see, for instance, Easterly, 2014). The Marshall Plan helped take countries from middle income to developed status. Why would this be different than moving, through aid, countries from poverty to middle income status? Analyze the interaction between aid, institutions, and long-term economic outcomes.

3) The Syrian civil war has had a tremendous toll, with hundreds of thousands killed and millions displaced. How would you imagine that the country could recover after the war finally ends? Should foreign aid play a role?

## References:


Bianchi, N., & Giorcelli, M. (2018). Reconstruction Aid, Public Infrastructure, and Economic Growth. *Mimeo*.

De Long, J. Bradford, and Barry Eichengreen. (1993). “The Marshall Plan: History’s Most Successful Structural Adjustment Program.” In Postwar Economic Reconstruction and its Lessons for East Today. , ed. Rudiger Dornbusch, Wilhelm Nolling and Richard Layard. Cambridge, MA:MIT Press

Easterly, W. (2014). The tyranny of experts: Economists, dictators, and the forgotten rights of the poor. Basic Books.

Fauri, F. (2010). Il piano Marshall e l'Italia. Il mulino.

Lombardo, G. (2000). L'Istituto Mobiliare Italiano: Centralità per la Ricostruzione, 1945-1954 (Vol. 2). Il mulino.

Sachs, J. D. (2005). Can extreme poverty be eliminated?. Scientific American, 293(3), 56-65.

Wood, R. E. (1986). *From Marshall Plan to debt crisis: Foreign aid and development choices in the world economy* (Vol. 355). Univ of California Press.