ECONOMIC RECOVERY AFTER IMMEDIATE POST-WORLD WAR II (1945-1947) IN THE UNITED STATES: LESSONS FOR POLICY OPTIONS IN THE US AND LATIN AMERICA AFTER COVID-19 COMPARING CHALLENGES, RESULTS AND POLICIES

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ABSTRACT: The economic recovery in the years after VJ Day (1945–1949), alongside the Great Depression or WWII, can be considered a learning experience in economic policy for current challenges faced by national economies for recovery after the outbreak of COVID-19. The policy lessons and procedures on demobilization, employment, expedited industrial reconversion, and macroeconomic stabilization are valuable of their own accord, but even more valuable is the role of government, public debate, confidence in planning, and collective action. These are the important resources that American and Latin American societies and policy markers could develop to face current challenges similar to those faced after WWII.

Keywords: American economic history; Latin American; COVID-19; Economic planning; collective action; public policies.

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INTRODUCTION

The Great Depression of 1929, often viewed as a crisis of effective aggregate demand, has been widely referenced in the search for events in economic history that might illustrate options for economic recovery in the United States (US) post-COVID-19 (Vernango 2020), as well, for Latin American economies. Vernango (2020) suggests World War II (WWII) as a complementary illustrative model for such context. In this respect, Galbraith (2020), and Sneader and Singhai (2020) also provide an analysis of the complete post-WWII period for a historical reference in terms of economic policy after COVID-19.

In this article, I propose adding the immediate postwar period (1945–1947) in the US to the above-mentioned historical events. An analysis of this period offers additional elements that may help to identify other relevant factors for a broad recovery after COVID-19. The postwar recovery process, which I argue was exceptional in 20th century economic history, was based on extensive indicative planning prior to and during the event, legislation and economic policies geared towards the coordination of aggregate demand and supply, and comprehensive employment policies. There was also a shock due to unfulfilled expectations in the private sector (there was broad confidence in the future among economic actors despite pessimistic forecasting) and, incidentally, a significant reduction in public spending.

Recently, Professor Tcherneva (2020) wrote an op-ed analyzing the subject of this article, titled "What Would Roosevelt Do?" I expand on this concept and offer some complementary ideas that lead us to further ask, "What would Truman do?".

In the following section, I present the similarities and differences between the challenges faced by the US economy in 1945 and in 2020. The second section describes the economic situation of the US circa 1948. The third section describes the economic policies and other actions that led to economic recovery. Finally, this article concludes with lessons that could be used as strategies to support the American economic recovery after the outbreak of COVID-19.

With this article, I would like to convey to the American and Latin American societies that there have been similar challenges to those of the current situation. These challenges were solved then, and similarly, they can be solved now through coordination and collective action.

2. SIMILARITIES AND DIFFERENCES BETWEEN THE CHALLENGES FOR THE AMERICAN ECONOMY: 1945 AND 2020

In this section, I identify the similarities and differences between the challenges faced by the US economy during both periods. In particular, I compare national output, employment, the need for industrial reconversion, as well as a forced and accelerated obsolescence in some economic activities. The public spending dynamics in 1945 and 2020 are also relevant and will be discussed.

There are similarities in terms of gross domestic product (GDP) between 1946 and 2020 in the transition from an economic expansion to a recession. In the first quarter of 2020, the US economy ended one of the longest periods of growth in its history –128 months of consecutive growth beginning in June 2009– by dropping an estimated 1.2% compared to the previous quarter, which is equivalent to a 4.8% drop in the annualized quarterly rate. This drop is due to the lockdown that was imposed to prevent the spread of the coronavirus. GDP contracted by 32.9% in the second quarter (as the annualized quarterly rate), which is the worst recorded performance since the collection of GDP quarterly data started in 1947.

From 1941 to 1944, the annual growth rate in the US economy averaged 15% with a drop of -10.9% in 1946 and -1.1% in 1947.

Regarding employment dynamics, the same transition from an expansion to a recession can be observed in both years, as with GDP. By 2020, the lockdown imposed by countries around the world to stop the spread of the coronavirus plunged the US into a recession, and unemployment has risen from 3.5% in February to 20% in May as a result.

The period prior to 1945 can be characterized by full employment due to the "departure" of workers to the armed forces, mainly by conscription, and the need for employment in activities related to war industries. During the war, the recorded unemployment rate was 1.9% for 1943, 1.2% for 1944, and 1.9% for 1945. However, in the immediate postwar period, the Department of Defense recorded the following, which is recounted by Higgs (1999):

> After VJ Day, however, the armed forces rapidly demobilized, shrinking from 12.12 million uniformed personnel in mid-1945 to 1.58 million in mid-1947. Simultaneously, civilian employment by the armed forces fell from 2.63 million persons to 0.86 million, and military-related employment in industry dropped from 11.0 million persons to 0.79 million. Therefore, total military-related employment fell in just two years from 25.75 million (39.2 of the total labor force) to 3.23 million (5.3 percent of the total force) (612).

Using other unemployment estimates, Taylor and Vedder (2010) documented the following:

> In August 1945, the Office of War Mobilization and Reconversion forecast [sic] that 8 million would be unemployed by the spring of 1946, which would have amounted to a 12 percent unemployment rate. In September 1945, *Business Week* predicted unemployment would peak at 9 million, or around 14 percent. Leo Cherne of the Research Institute of America and Boris Shishkin, an economist for the American Federation of Labor, forecast [sic] 19 and 20 million unemployed respectively –rates that would have been in excess of 35 percent.

Another similarity in both periods is the need for extensive industrial reconversion in 1945 and the supply chain problems in 2020. During the war years (1940–1945), public and private companies in the US focused on contributing to the production of military goods. Higgs (1999) estimates that the demand for these goods was about 55% of gross national product (GNP). Much of this demand "vanished" after Victory over Japan (VJ) Day and efforts were made to redirect the lagging demand for the durable and non-durable consumer goods that were limited during the war years. Post-pandemic economic activity will face a similar kind of reconversion due to problems caused by disruptions in the global supply chain and its effect on the US.

Another similarity, in some way related to the industrial reconversion, arises from the need for accelerated obsolescence: replacing military goods and assets in 1945, and replacing an economy based on in-person services in 2020. It is well-known that technical progress generates obsolescence in some capital goods, what Schumpeter and Domar (1946) termed creative destruction, but in the case of COVID-19, this occurs through a change in the social forms of consumption.[1]

In this context of similar challenges, there is one significant difference between the time periods: public spending was reduced in 1945 but increased in 2020. In mid-May 2020, Congress approved four separate spending bills amounting to almost $2.9 trillion, which is more than double the recovery effort amount that was approved after the 2008 financial crisis. Together, this response is almost 14% of US GDP.

In contrast, Bohanon (2012) pointed out that,

> In 1944, government spending at all levels accounted for 55 percent of gross domestic product (GDP). By 1947, government spending had dropped 75

1 I thank professor James Gerber for the reinforcement of this idea.

> percent in real terms, or from 55 percent of GDP to just over 16 percent of GDP. Over roughly the same period, federal tax revenues fell by only around 11 percent.

Accordingly, the US government canceled war contracts and spending fell from \$84 billion in 1945 to under \$30 billion in 1946. By 1947, the government was paying back its massive wartime debts with a budget surplus of close to 6% of GDP.

Keeping the Great Depression in mind and the discussion surrounding stagnation à la Hansen (de León 2018), it is important to point out that by 1945, precisely because of the anticipated reduction in public spending, most economists (Keynesians?) anticipated a recession and viewed a reduction in public spending as problematic. For instance, in the 1945 symposium *Financing American Prosperity*, as referred to in Mises Wiki (wiki.mises.org), several prominent economists discussed the financial and economic problems of the transition after WWII and suggested solutions. Except for Benjamin Anderson, all contributors advocated for a scope of federal expenditures much larger than that before the war (see Homan and Machlup,1945).

The prevailing opinion of that time was that the US would sink into a deep depression at the end of the war. In 1943, Paul Samuelson, a future Nobel Prize winner, wrote that upon cessation of hostilities and demobilization "some ten million men will be thrown on [sic] the labor market". He warned that, unless wartime controls were extended, there would be "the greatest period of unemployment and industrial dislocation which any economy has ever faced". Another future Nobel laureate, Gunnar Myrdal, predicted that postwar economic turmoil would be so severe that it would generate an "epidemic of violence" (Bohanon 2012). De León (2018) has also outlined this discussion within the framework of secular stagnation.

3. THE SITUATION OF THE US ECONOMY CIRCA 1948

Given the scenario anticipated by most analysts after VJ Day, the US economy in 1946 is an interesting case study; contrary to expectations, and because of a combination of events and economic policies, as well as "unfulfilled" expectations, the economy experienced a process of economic expansion. In this section, I describe the results associated with the actions implemented by the government and the private sector between 1945 and 1947, which surprised many economic analysts. In the following section, these actions are described in more detail.

In terms of GDP growth, after a period with an average annual growth rate of 15%, a drop of -10.9% in 1946, and of -1.1% in 1947, growth increased by 4.4% in 1948 and 8.7% in 1950.

Regarding employment/unemployment circa 1948, the following quote from President Truman (Economic Report 1947, 1) mentioned by Higgs (1999, 600) is apt:

> At the end of 1946, less than a year and a half after VJ day, more than 10 million demobilized veterans and other millions of wartime workers found employment in the swiftest and most gigantic change-over that any nation has ever made from war to peace.

After the WWII, unemployment rates, which were artificially low because of wartime conscription, rose slightly but remained below 4.5% in the first three postwar years –below the long-run average rate of unemployment for the 20th century. Some workers voluntarily withdrew from the labor force, choosing to go to school or return to prewar duties as housewives. However, many who lost government-supported jobs in the military or in munitions plants found employment as civilian industries expanded production; civilian employment grew by over 4 million between 1945 and 1947.

As Bohanon (2012) has pointed out,

> Just as important, the double-digit unemployment rates that had bedeviled the prewar economy did not return. Between mid-1945 and mid-1947, over 20 million people were released from the armed forces and related employment, but nonmilitary-related civilian employment rose by 16 million. In particular, the unemployment rate rose from 1.9 percent to just 3.9 percent.

In this respect, Higgs (1999, p. 613) compellingly mentioned,

> It was no miracle to herd 12 million men into the armed forces and attract millions of men and women to work in munitions plants during the war. The real miracle was to reallocate a third of the total labor force to serving private consumers and investors in just two years.

Furthermore, household consumption, business investment, and net exports all boomed as government spending receded. An accelerated industrial reconversion transformed war industries into investment and consumer goods industries and obsolete products that were no longer required were disposed of. As Mills (1984, p. 223) summarized, “The anticipated recession never materialized and the major economic problems of the postwar era were those of inflation, not recession”.

4. ECONOMIC POLICIES AND OTHER ACTIONS THAT LED TO RECOVERY

In this section, I analyze the policies and events that led to one of the most surprising postwar recoveries in the history of the American economy. The policies are categorized as follows:

- Planning and demobilization plans
- Employment policies
- Industrial reconversion (economic policies to coordinate aggregate supply and demand)
- Other policies and events

4.1 PLANNING AND PUBLIC/PRIVATE DEMOBILIZATION PLANS

The extensive effort to coordinate military and economic demobilization activities is an often-forgotten aspect of the post-WWII period. Ballard (1983) details an extensive set of planning initiatives carried out at the federal level, at the state level, and through labor associations and businesses, as well as by the general public. Rep. E. Dirksen echoes this recognition of the need for planning in 1943 when he said, “It is amazing how this planning idea has gotten into the consciousness of everybody everywhere” (Ballard 1983, p. 28).

Among the planning agencies, several standouts include the National Resources Planning Board (NRPB) from 1940 to 1943, the influential Baruch-Hancock Report of early 1944 and after, as well as the office of War Mobilization and Reconversion (OWMR), which replaced the Office of War Mobilization in October 1944 and facilitated the centralization of the demobilization operation (Ballard 1983).

In fact, as Ballard (1983, 57–59) pointed out,

> Planning became an essential function of government and the idea gained considerable acceptance in other parts of the American society… the timing, breadth, volume, and centralization of planning, aided by a most favorable milieu, helped mark this postwar preparation as a unique phenomenon.

Additionally, it is important to mention that planning was accepted as a strategic administrative function both in government and by corporations, which led to its recognition as a fundamental pillar of the *New Industrial State* by John K. Galbraith (1967).

4.2 EMPLOYMENT POLICIES FOR RECOVERY

Planning for postwar employment occurred in two phases for full employment. The first phase required a huge demobilization of both military personnel and civilians working in war-oriented industries, and the second phase required the incorporation of those demobilized into civilian postwar production activities.

At that time, reducing a large military force in a short span of time was a phenomenal achievement. For example, the number of army personnel outside the continental US fell from 5.2 million in June 1945 to 0.8 million a year later (Ballard 1983). The activities needed just to process such a large number of people were impressive. Moreover, discharged service members had to be reabsorbed into civilian life and, more critically, into the workforce.

With respect to jobs, planners and government officials set the goal of maintaining a continuous high rate of employment or even full employment in the immediate postwar years. Their determination to reach such an extraordinary goal, as evidenced by the Employment Act of 1946, played an important role in this accomplishment.

Among other labor policies, there were liberal provisions including job assistance centers, the Mustering-out Payment Act, unemployment compensation, and the GI Bill to assist veterans in their transition.

There were also several fortuitous developments in the civilian labor force including i) the withdrawal of a large number of women, youth, and retirement-age persons from the workforce; ii) a big boom in the agriculture, construction, and industrial sectors; and iii) the return to a forty-hour week. All of these developments contributed to a faster and more simplistic accommodation of both veterans and former war workers.

Furthermore, the interim adjustment period between Victory in Europe (VE) Day and VJ Day provides a fuller picture of transitional employment; war plant employers and some veterans began shifting jobs before the end of the Pacific War.

As is shown in the following section, the success of the industrial reconversion helped to alleviate the employment problem significantly.

4.3 INDUSTRIAL RECONVERSION

In this section, I analyze the industrial reconversion from an aggregate supply and demand perspective. The objective from the aggregate supply side was to facilitate the transition of productive resources, which were previously dedicated to military production, to civilian use. Here, I highlight the following policies: the orderly termination of war contracts that triggered the economic reconversion and the disposition of surplus material that impacted peacetime production. This was formalized through the War Surplus Disposal Act. Along the same lines, Ballard (1983) pointed out the following:

Careful preparations for war contract terminations, promoted to a great extent by lessons derived from WWI, paid off handsomely in greater uniformity of contractual arrangements and quicker notice of terminations. Likewise, expedited contract settlements on relatively generous terms for industry with provisions for interim funding meant industry had a combined boost of working capital and ready facilities. The government predominantly reached the goal of clearing war inventories from factories within the sixty-day time limit. The availability of reconversion machine tools, large industrial capital reserves, and better prepared company management further assisted in the industrial war to peace changeover (p. 141).

The objective from the aggregate demand side was to promote increased demand for consumer-related goods, mainly durable goods (new cars, household appliances, and houses) and goods intended for productive investment to replace the previous demand for military goods. To achieve this, a series of economic policies came together with coinciding actions of families and companies.

In fact, Boahnon (2012) stated that "destimulation" in public spending did not result in a collapse of consumption spending or private investment. Real consumption rose by 22% between 1944 and 1947 and spending on durable goods more than doubled in real terms. Gross private investment rose by 223% in real terms, with a whopping six-fold real increase in residential housing expenditures.

There is consensus that private consumption was promoted by reduced savings, the sale of war bonds accumulated by families, and reducing the relatively high savings rate that families maintained during the war years. According to Higgs (1999), the personal savings rate (personal savings relative to disposable income) was 25.5% in 1944 and 19.7% in 1945, and then fell to 9.5% in 1946 and 4.3% in 1947. This may have been due to families' perception that increases in income were permanent.

There were also several coinciding policies and events that stimulated private consumption, including the gradual reduction of price controls, the perception of greater increases in permanent income (although wages were lower), and the expansion of bank credit.

As for investment, according to Higgs (1999), gross private domestic investment related to GNP in 1945 was 5.0% compared to 14.7% in 1946 and 1947, and 17.9% in 1948.

According to President Truman's economic report for January 1948, "the extraordinary rate of business income in general allowed investment to proceed at record levels. Even greater expansion was prevented mainly by lack of material rather than by lack of intention to invest or lack of financial resources" (Higgs, 1999, p. 611).

There were other economic policies that supported investment promotion in addition to the orderly termination of war contracts and the disposal of surplus material, such as reducing the tax liability which increased current retained earnings (i.e., the Revenue Act of 1945 lowered the top corporate income tax and repealed the excess profit tax). The gradual reduction of price controls and continued wage control were other policies that contributed to the expansion of investment.

In addition to the aforementioned policies, financing and investment were facilitated by the selling of various government securities acquired by firms during the war and the high demand for securities issued by companies in the bond and stock market.

At this point, I would like to add several ideas from Domar (1948) that refer precisely to this period and how unfulfilled expectations were relevant for some economic actors. For the purpose of this analysis, the following quote clearly synthetizes Domar's (1948) approach:

> Theoretically speaking, the issue is this: we have found that if firms were "somehow" induced to invest a sufficient amount, so that national income rose at the required rate, no disappointments would follow. Suppose now that it were possible for the government (presumably) to guarantee that income would actually grow at this rate for some time to come. Would not this guarantee, if taken seriously by the business public, call forth sufficient investment and thus make income grow at the required rate? This is full employment by magic! Yet as one reads Leo Barnes´s most interesting note [article included in my list of references] describing how C.E.D. [Committee for Economic Development], by making a few (undoubtedly unintentional) errors, managed to "persuade industry into a prosperity", one gets a feeling that magic sometimes works. We do not know, however, how seriously these

> C.E.D. forecasts were actually taken; still the idea is highly suggestive. [….] On a more serious and practical level, this much can be said for the argument. Past depressions do exert a profound influence on business thinking, and an assurance that they will not recur would undoubtedly brighten the future and make many marginal projects worth undertaking. If, in addition, businessmen could confidently expect growing economy, the effect would be so much stronger (pp. 793-794).

In the following section, I present some lessons derived from the policies and events described in this section that could be helpful in facilitating the American economic recovery after COVID-19.

5. LESSONS

The case of the US economy (1945–1947) presented in this article seeks to outline the actions that made it possible to overcome a situation that is somewhat similar to the current situation in 2020 due to the coronavirus pandemic. It is thus useful to contextualize the severity of the challenges and the available resources in American society that were used to face crises of a similar nature to the current one.

Planning, and the social consensus built regarding its urgency and relevance, was among the resources available to the American economy in the immediate postwar period. This was the case in part because there was a need to not repeat the demobilization process that occurred after WWI, and the broad institutional structure developed to deal with the great recession (e.g., unemployment insurance and the National Resources Planning Board). From this perspective, the role of planning offers a lesson for the current challenges faced due to the COVID-19 pandemic.

Considering the coordination between aggregate demand and supply, the reorientation of spending towards reactivation was another element taken into account through policies conducive to the reconversion of consumption, investment, and confidence in the future.

The implementation of the Marshall Plan is an aspect not mentioned in this article due to its rather international nature, but it has been suggested by other analysts. The Marshall Plan not only stimulated an entire strategy of support for reconstruction in Europe but also sent positive signals to economic agents in the US (see Steil, 2018).

The role of confidence in a better future, as illustrated in Domar (1946), might have also complemented the government's actions.

Among the resources available to the American economy during those years, it is important to consider the role of institutionalist economists in advisory and managerial positions in government agencies and in corporations, who maintained their own perspective on economic and social relations and the pragmatic role of public action. See Mitchell (1937) for a good illustration of this contribution.

This article emphasizes similarities in the challenges faced by the American economy post VJ Day and after the outbreak of COVID-19 in 2020, however, there are also many differences that shape the design of recovery policies. Some differences may be related to the size of the economy. For example, the US economy is seven times greater in 2020 than it was in 1946, and thus the challenges are greater than they were before. The role of deficient aggregate demand is more relevant now than it was then, which may be one of the biggest differences in demand between 1946-1948 and 2020-2021. After WWII, people in the US had an income and savings, but in 2020 they do not have a stable income, and many survive by spending their savings on basic items such as rent and food. Furthermore, the dollar's international position could mean that there is a greater possibility of resorting to fiscal and monetary policies as essential components for recovery in 2020 instead of implementing planning initiatives. Lastly, the degree of uncertainty may be greater in 2020 than in the past, but this remains to be seen. These differences are undoubtedly just a few among many others.

Nonetheless, taking into consideration some of these limitations, I present these factors to convey to the American and Latin American policy markers that there have been similar challenges as those of the current day, and these challenges were solved through coordination and collective action.

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