

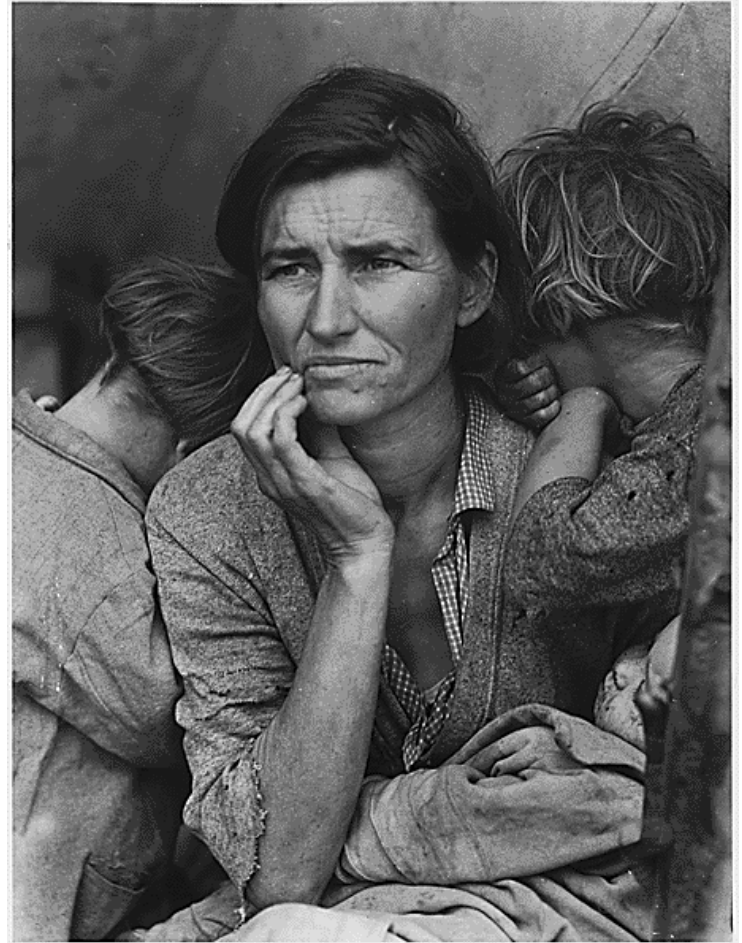


# **Why Was the Depression so Great?**

**THE CAUSES OF THE WORST ECONOMIC  
DISASTER IN AMERICAN HISTORY**

# Overview

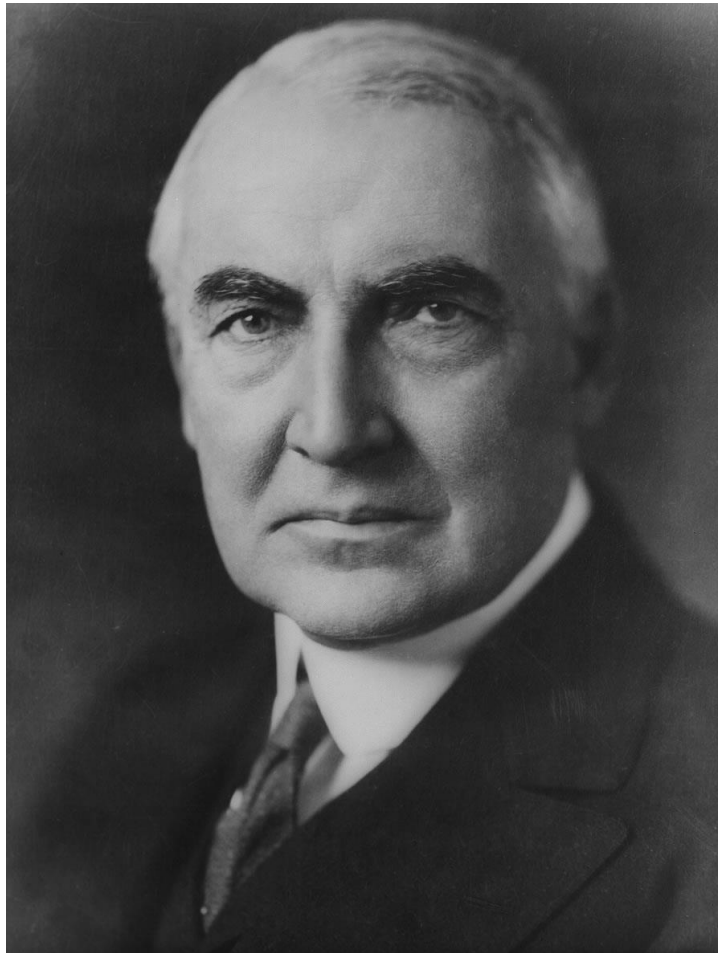
- The Stock market crash of 1929 did not, by itself, cause the Depression.
- Swings in the money supply also have contributed to the crisis.
- Hoover and FDR's activist programs helped turn a recession into the Great Depression.



# The Depression that Wasn't

- After World War I, America entered a sharp recession in 1920.
- During the war, the Federal Reserve kept interest rates low, so people borrowed more.
- When they raised rates after the war, many investments became unprofitable.
- Prices fell almost 20%, GNP by 17%, and unemployment rose to 12%.

# Government Response and Recovery



- Under President Harding, federal spending fell by nearly half from 1920 to 1922 and tax revenues by 40%.
- The economy then recovered quickly with unemployment falling to 2.4% by 1923.
- Commerce Secretary Herbert Hoover, on the other hand, made the case for “more” government intervention in 1921.

# Why the Twenties Roared

- There was substantial economic growth in the 20's, but some of it was an illusion of growth.
- Expansion of the money supply may have contributed to stock market bubble.
- Money supply grew 55% between 1922 and 1929.



# Reckoning and Reaction

- In October, 1929, the stock market bubble burst.
- Credit contracts.
- President Hoover intervened:
- Urged businessmen to keep wages up.
- Increased spending by almost 50% from 1929 to 1932.
- Doubled income tax in 1931.
- Imposed huge Smoot-Hawley tariff—decreased trade by half.





# Public Works



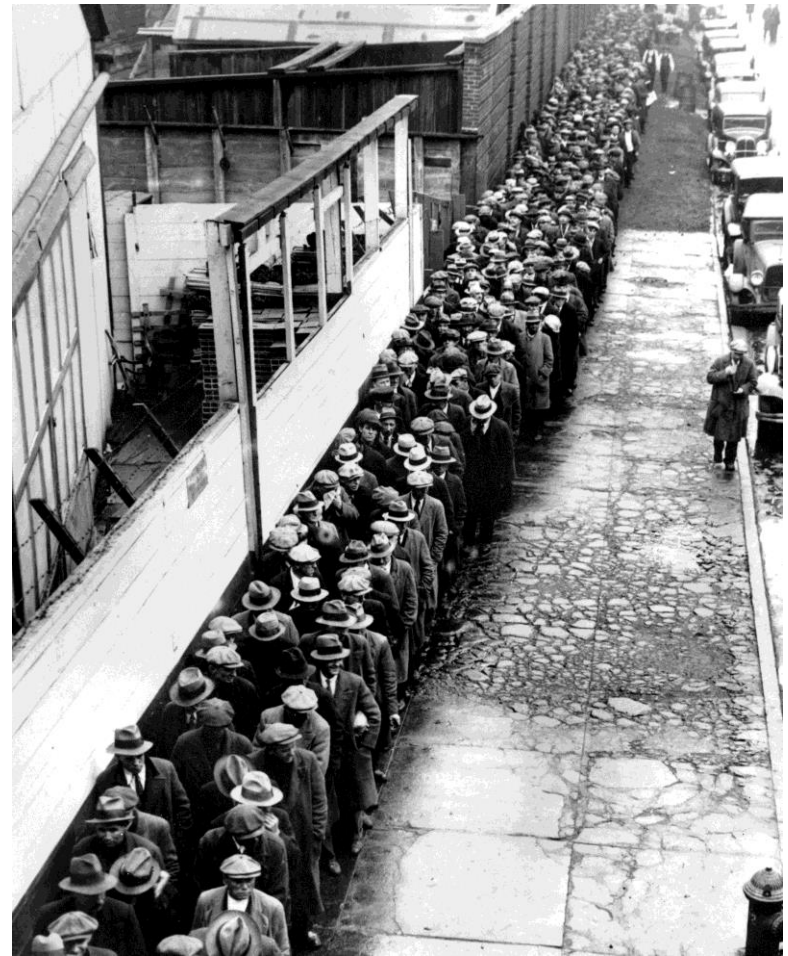
“I determined that it was my duty, even without precedent to call upon the business of the country for coordinated and constructive action to resist the forces of disintegration...Our leading business concerns have sustained wages, have distributed employment, have expedited heavy construction. The Government has expanded public works, assisted in credit to agriculture, and has restricted immigration...Our present experience in relief should form the basis of even more amplified plans in the future.”

-Herbert Hoover, October 1930



# What Followed

- Unemployment rose to 25% by 1933. (Eight months after the stock market crash it was 6.3%.)
- GDP fell by a quarter, with the worst decrease coming in 1931.
- Set the stage for the election of FDR, who expands on Hoover's interventions.



# Candidate Roosevelt



- FDR campaigned *against* Hoover's big government policies.
- Democratic Party Platform pledged a 25% reduction in federal spending and a balanced budget.
- Lower tariffs. (He delivered on this one.)

# President Roosevelt

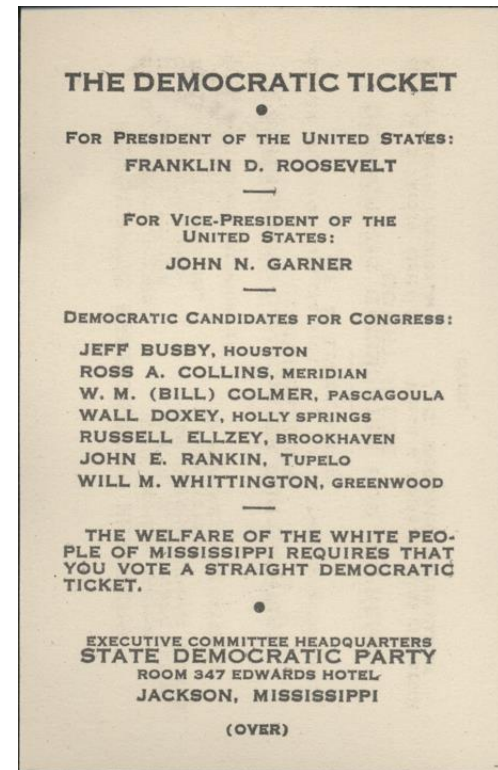
- Expanded Hoover's policies of higher prices and taxes.
- NIRA and NRA suspended antitrust laws and created business cartels to set prices, wages, and production.
- WPA creates massive public works—many of questionable merit.
- “The ideas embodied in the New Deal Legislation were a compilation of those which had come to maturity under Herbert Hoover's aegis.” Rexford Tugwell, 1946

# Big Business and the New Deal

- The New Deal was good for big business as it allowed them to set prices and limit competition.
- Consumers and small businesses suffered.
- Schechter Poultry Company, a small firm, ran afoul of the law when it sold chickens below the cartel set price.
- Larger poultry firms complained about competition, so the government fined Schechter.
- Supreme Court struck down NIRA in this case.

# Discriminatory Effects of the NRA

- Forced unionization and minimum wages kept blacks from competing.
- A 1934 NAACP publication noted that "union labor strategy seems to be to obtain the right to bargain with the employees as the sole representative of labor, and then close the union to black workers."





# Agricultural Adjustment Act

- Designed to raise agricultural prices.
- Paid farmers not to grow crops.
- Also destroyed thousands of livestock animals that were meant for consumption.
- Many sharecroppers kicked off the land, while the top 1% of farmers received 21% of the benefits.
- Decreased farm output and increased prices for food.

# Where Did the Money Go?

- Relief spending did not go to the poorest states.
- Instead, it was directed to the states and districts where it would win the most political favors.
- Historian Leonard Arrington showed that the South received less money per person than the West even though it was poorer.



# Did Any of It Work?

- Unemployment never dropped below 14.6% until the onset of World War II.
- In 1939, 2 out of 3 Americans believed FDR's attitude to business was delaying recovery.
- Two UCLA economists estimate that FDR's policies delayed recovery seven years.
- Per capita consumption did not recover; it was 25% below the 1929 trend throughout the New Deal.

# Don't Take My Word For It

- Even FDR's Treasury Secretary admitted the New Deal didn't work:
  - “No, gentlemen, we have tried spending money. We are spending more than we have ever spent before and it does not work. ...I say after eight years of this Administration we have just as much unemployment as when we started.” – U.S. Treasury Secretary Henry Morgenthau, Jr.



# World War II

- The draft and war production brought unemployment down to 7% in 1942 and 1.3% in 1944, but the economy did not expand.
- Harvard economist Robert Barro found that for every dollar spent on the war, the rest of the economy shrank by 20 cents.
- Consumption fell and many products were unavailable because of rationing.





# Recovery at Last



- After the war, Keynesian economists predicted a return to the Depression because of the massive drop in government spending.
- Instead the economy grew at its fastest rate in history.
- Once set free from many New Deal programs, the market ended the Depression.

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