Lecture 18

Crashing Hopes: The Great Depression

In 1929, Yale University economist Irving Fisher stated confidently: "The nation is marching along a permanently high plateau of prosperity." Five days later, the bottom dropped out of the stock market and ushered in the Great Depression, the worst economic downturn in American history. Although Americans often believe that the Crash was the starting point of the Great Depression, many historians point out that it wasn't the sole cause. This lecture examines the roots of the Crash and the effect of the Great Depression on the American public.

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Some questions to keep in mind:

1. **Why were Americans so confident in the stock market in the years leading up to the Great Depression?**
2. **How did the Psychology of Consumption shape the causes and effects of the Crash?**
3. **How did stock market investing change during the 1920s? Who were the main investors and how did they pay for their investments?**
4. **Explain the statement: "By 1929, much of the money that was invested in the stock market did not actually exist."**
5. **Why did Hoover choose the term "depression" for this economic downturn? Why do you think this term has remained part of the American vocabulary ever since?**

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Optimism and Prosperity

When Americans elected Herbert Hoover President in 1928, the mood of the general public was one of optimism and confidence in the United States economy. Most people believed that national prosperity would continue indefinitely. In his acceptance speech for the Republican party nomination for the presidency, Hoover had said:

"We in America today are nearer to the final triumph over poverty than ever before in the history of any land. The poorhouse is vanishing from among us."

Herbert Hoover (1874-1964)

Many Americans shared Hoover's optimism at the beginning of 1929. An editorial in the New Year's edition of the *New York Times* on January 1, 1929, for example, stated:

> "It has been twelve months of unprecedented advance, of wonderful prosperity. If there is any way of judging the future by the past, this new year will be one of felicitation and hopefulness."

That same year, John Jacob Raskob, Chief Executive of General Motors and head of the Democratic National Committee, published an article entitled "Everybody Ought to be Rich" in the *Ladies Home Journal*. Raskob suggested that every American could become wealthy by investing $15 a week in common stocks. He failed to realize, however, that the weekly salary of the average American worker was between $17 and $22, but that's not important: the optimism was there.

A "Bull Market"

For five years prior to 1929, rising prices typified the stock market. During this period, American investors enjoyed an enormous "bull market." (The opposite, a market characterized by falling prices, is called a "bear market.").

Americans invested in the stock market for six reasons during the 1920s:

1. Rising stock dividends.
New investors entering the market, many who viewed it as an easy way to get rich quick, helped inflate stock prices. Economic historians, however, estimate that a relatively small number of Americans--about 4 million--had investments in the market at any one time. Yet, the constant influx of new investors coming in and old investors moving out ensured that new money was always floating around.

2. Increase in personal savings.
Higher wages meant that even average Americans now had surplus money to put into savings or invest in the stock market.

3. Relatively easy money policy.
At this time, banks made money more readily available at lower interest rates to more and more people. Although economists debate the actual influence of this phenomenon on the stock market, it's conceivable that many people took out loans not only to buy cars, but also to buy stock.

4. Companies invested their over-production profits in new production.
From 1925 on, industry was over-producing. In anticipation of eventually selling the surplus, business leaders funneled their profits right back into industry. They invested in factories and new machinery, and hired more workers, which, in turn, fueled even greater overproduction. This increased production gave the companies an aura of financial soundness, which encouraged Americans to buy more stock.

5. Lack of stock market regulation.
At this time, there were no effective legal guidelines on buying and selling stock. Free from such limitations, corporations began printing up more and more common stock. Many investors in the stock market practiced "buying on margin," that is, buying stock on credit. Confident that a given stock's value would rise, an investor put a down payment on the stock, expecting in a few months to pay off the balance of their initial investment while reaping a hefty profit. This investment strategy turned the stock market into a speculative pyramid game, in which most of the money invested in the market didn't actually exist.

6. Psychology of consumption.
We've already discussed this phenomenon in Lecture 15. The Psychology of Consumption fed the optimism of investors and gave them unquestioning faith in prosperity. When the Crash did come, it was even more devastating because of this unquestioned faith.

The Crash

Most economists of the 1920s believed that the stock market--not housing starts, sales of durable goods, or the financial health of banks--was the chief indicator of the fiscal health of the United States. In September of 1929, stock prices began to fluctuate, but market analysts dismissed this as temporary. What many of these analysts did not realize--or refused to admit--however, was that stock prices were totally out of proportion to actual profits. Sales of goods and the construction of factories were falling rapidly while stock values continued to climb. Still, very few were worried; they still accepted Adam Smith's "self-adjusting economy" as dogma and believed the problems would correct themselves.

Historians refer to October 24, 1929 as "Black Thursday." On this day, people began dumping their stocks as quickly as they could. Sell orders inundated market exchanges and the bull market suddenly shifted to a bear market. By that evening, J.P. Morgan and other financiers bought up stock to stop the panic and keep the market afloat. On Friday, October 25, the House of Morgan continued to keep the market stable and it seemed that the panic was over. Yet, many investors began to worry during the weekend. George and Martha and thousands of their friends decided to sell whatever stock they still had as soon as the market opened on Monday. As a result, on Monday, October 28, there was another wave of sell orders. The next day, October 29, 1929, "Black Tuesday," was the beginning of the Great Crash.

"Black Tuesday" was the single most devastating financial day in the history of the New York Stock Exchange. Within the first few hours the stock market was open, prices collapsed and wiped out all the financial gains of the previous year. Since most Americans viewed the stock market as the chief indicator of the health of the American economy, the Great Crash shattered public confidence. Between October 29 and November 13, the day when stock prices hit their lowest point, over $30 billion disappeared from the American economy. This amount was comparable to the total amount of money that the federal government had spent to fight the First World War.

Still, optimism persisted and many leaders declared that the worst was over. J. D. Rockefeller said:

"These are days when many are discouraged. In the 93 years of my life, depressions have come and gone. Prosperity has always returned and will again."

Such optimism, however, did not last long. Popular songs of the day mirrored the transition from optimism to despair. In 1930, people sang "Happy Days Are Here Again" and the national income dropped from $87 billion to $75 billion. In 1931, somewhat more dejectedly, people sang "I've Got Five Dollars" and the nation's income dropped to $59 billion. The song of 1932 was "Brother, Can You Spare a Dime," when the domestic economy fell to $42 billion. Eventually, the American economy bottomed out at $40 billion in 1933.

Former President Coolidge had this insightful observation about the economic health of the United States:

"This country is not in good condition."

The Depression

So as not to alarm the public, President Hoover chose his words carefully when he discussed the state of the economy in 1929. American economists and politicians had referred to previous economic downturns as "Panics," such as the "Panic of 1873" and the "Panic of 1893." Hoover, however, called this latest downturn a "Depression" rather than a "Panic," and the name stuck.

Of course, America was not alone in the Great Depression; it struck all the industrialized nations of the world, including Germany, Britain, and France. Moreover, Germany still had huge reparation payments to make to the Allies in the aftermath of WWI. These reparation payments fueled spiraling inflation in Germany and crippled that nation's economy. The Allies themselves had borrowed money from the United States during the war, were unable to pay it all back during the 1920s, and were now not only broke, but in debt.

Social Problems

These perplexing economic problems in the United States exacerbated a host of social problems, including:

- Unemployment and poverty
- Breakdown of families
- Soaring high school dropout rates (2 to 4 million)
- Homelessness
- Organized protests
- Around the country, the homeless built settlements of cardboard and tar-paper shacks, called "Hoovervilles" in sardonic reference to President Hoover.
- Farmers armed with guns and pitchforks marched on the local banks to prevent foreclosures.
- "The Bonus Expeditionary Force." A group of WWI veterans who had been denied their pensions organized the first march on Washington in protest. In 1932, twenty thousand men set up a tent city, vowing to stay until they got their money. President Hoover overreacted and sent in the army (led by future war heroes Douglas MacArthur and Dwight D. Eisenhower) to break up this peaceful demonstration.

CAUGHT WITHOUT A SPARE

"Bonus Army" WWI Veterans protesting unpaid pensions

CAMP MARKS, WASHINGTON, D. C.

"Bonus Army" WWI Veterans making camp in Washington, D.C., to protest unpaid pensions

A WESTERN LEADER

Handpainted sign on Bonus Army truck states: "We Done a Good Job in France, Now You Do a Good Job in America"

Images of the Depression

There are many stereotypical images of the depression, images enforced by the mass media. These include:

- Bread lines
- Hoboes hopping freight trains
- College grads becoming gas station attendants (or enrolling in graduate school in record numbers)
- Skyrocketing rates of suicide and mental illness
- Former businessmen selling pencils or apples on street corners
- "Okies"--Oklahoma farmers escaping the dust bowl for migrant farm work in California, most vividly portrayed in John Steinbeck's novel *The Grapes of Wrath* (1939)

These stereotypes, many of which have become romanticized in popular culture, only depict the experience of a small number of the American people. The reality of long-term unemployment, the day-to-day despair, was much less dramatic, and thus more dismal. Two basic economic facts soured the lives of average Americans:

1. Unemployment. In his inaugural address, Franklin D. Roosevelt recognized:

"Now let's be frank. You and I know that immediate relief of the unemployed is the immediate need of the hour."

2. Inability to sell goods and services. With so much of the work force unemployed, nobody had money to buy things.

The Great Depression hit farmers especially hard. Many had gone into debt to buy machinery and land, and now could not make their payments. Low crop prices wiped out potential profits. In addition to the usual challenges of agriculture, a great drought took place in 1931 and 1932 in the Midwest and the South and turned much of the trans-Mississippi West into a dust bowl. Nevertheless, if farmers couldn't make a profit selling their products, at least they could still eat, so most stayed put. In contrast to popular images of farmers leaving the land, the 1930s actually had the lowest rate of migration from farms to cities.

Sam Nichols, tenant farmer, Boone County, Arkansas, October 1935

Escapism

One-third of Americans were below the poverty line, yet some industries actually managed to make a profit at the beginning of the 1930s as the public looked for a way to escape. If Americans couldn't find work, at least they could go for a drive, have a cigarette, or go to a movie. Correspondingly, sales of oil, gas, cigarettes, and movie tickets all went up. Humorist Will Rogers remarked,

"We're the first nation in the history of the world to go to the poorhouse in an automobile."

Laying the Blame

The American public found the "Three B's" responsible for the Crash and the Depression:

1. Bankers
2. Brokers
3. Businessmen

However, the Crash was not the immediate cause of the Depression. It alone was not responsible for a decade of worldwide economic catastrophe. But what was responsible for the Depression? And what were the long-term consequences of the Great Depression in the United States? The Depression itself was responsible for a dramatic transformation in the structure of American politics, for a change in Americans' expectations about government, and for a shift in United States foreign policy during the 1930s. These are remarkably important issues, so important, that we'll take them up in Lecture 19: "The Great Depression and the New Deal."