

Making of the Modern World 15

Lecture #5: Global Depression and
the Creation of the Welfare State

What I want you to know today

- And now for something completely different: the Great Depression
- First, a brief film clip: *Grapes of Wrath* (1940)
- Individuals found themselves controlled by forces they couldn't understand, often w/o concrete sense of who or what was responsible.
- Economic depression helped to delegitimize a belief in the obvious “technical” superiority of liberalism.
 - Belief that:
 - Our system doesn't lead to prosperity.
 - Individuals can face hardship through no fault of their own.
- Pain of depression helped to lead to rise of welfare state.

European Origins of the Great Depression

- Austria/Germany borrow money from USA to pay war debts to France and England
- France, England pay debts owed to USA for WWI
- System dependent on flow of cash from USA
 - Economies interdependent
- Investors begin to pull out in 1928

Agricultural Surplus and the Great Depression

- Overproduction in 1920s
- Strongest harvests in 1925, 1929
- Wheat lowest price in 400 years
 - Farm income drops
 - less demand for manufactured goods
 - inventory surpluses
- The Dust Bowl in the 1930s

Black Thursday (October 24, 1929)

- Stock purchases on margin (3%)
- Hints of slowdown in Europe
 - investors begin to sell
- Snowball effect
 - life savings lost
- Black Thursday
 - suicides

US Economic Collapse

- Inventory surplus leads to layoffs
- Layoffs lead to decreased demand, businesses fail
- Federal Reserve does not manage crisis well
 - Fails to lend adequately
 - Raises interest rates
- 1932 industrial production $\frac{1}{2}$ of 1929 levels
- 44% of US banks out of business
 - Deposits lost

Debt-Deflation

1. Debt liquidation and distress selling.
2. Contraction of the money supply as bank loans are paid off.
3. A fall in the level of asset prices.
4. A still greater fall in the net worth of businesses, precipitating bankruptcies.
5. A fall in profits.
6. A reduction in output, in trade and in employment.
7. Pessimism and loss of confidence.
8. Hoarding of money.
9. A fall in nominal interest rates and a rise in deflation-adjusted interest rates.

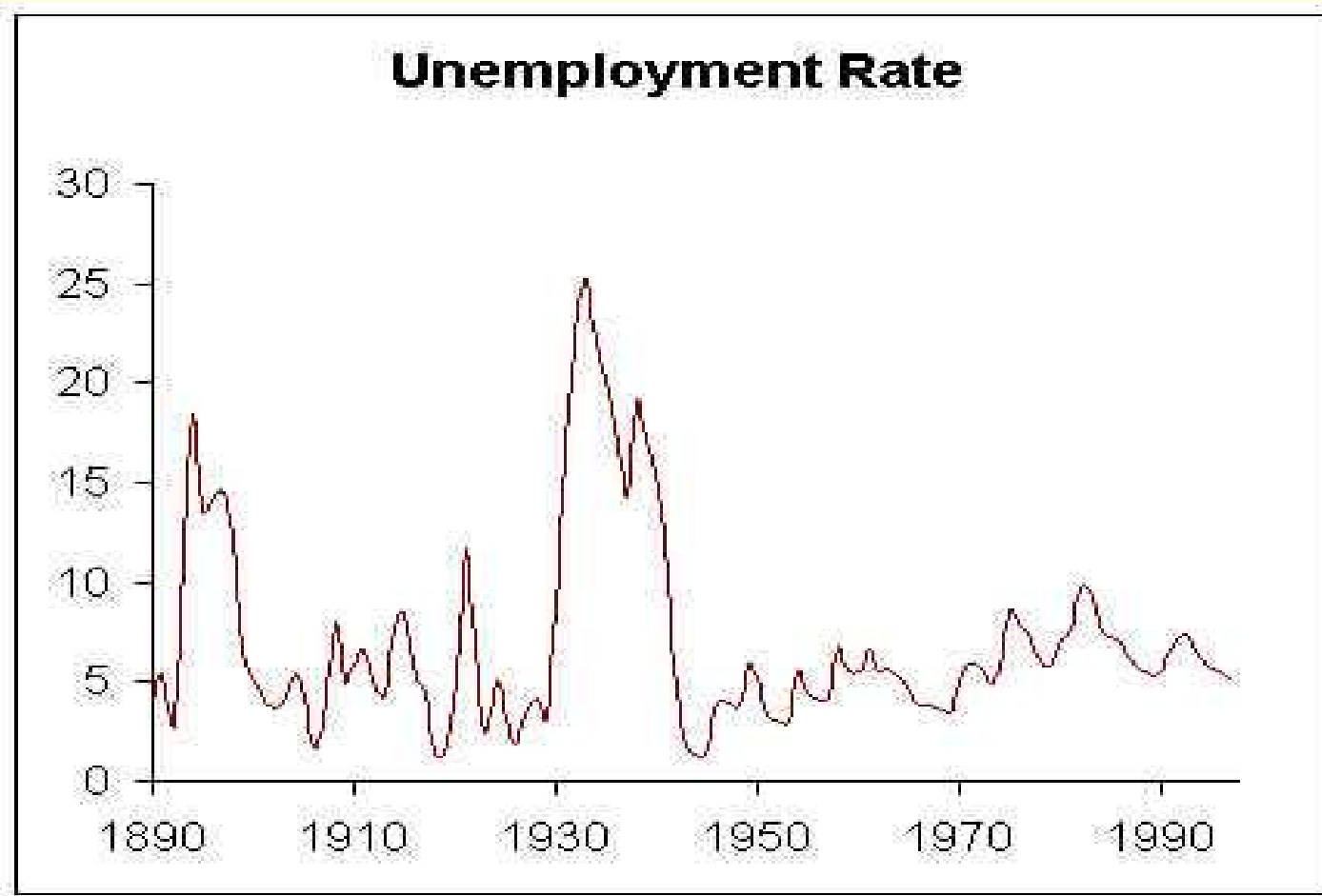
Poor Mother and Children, California



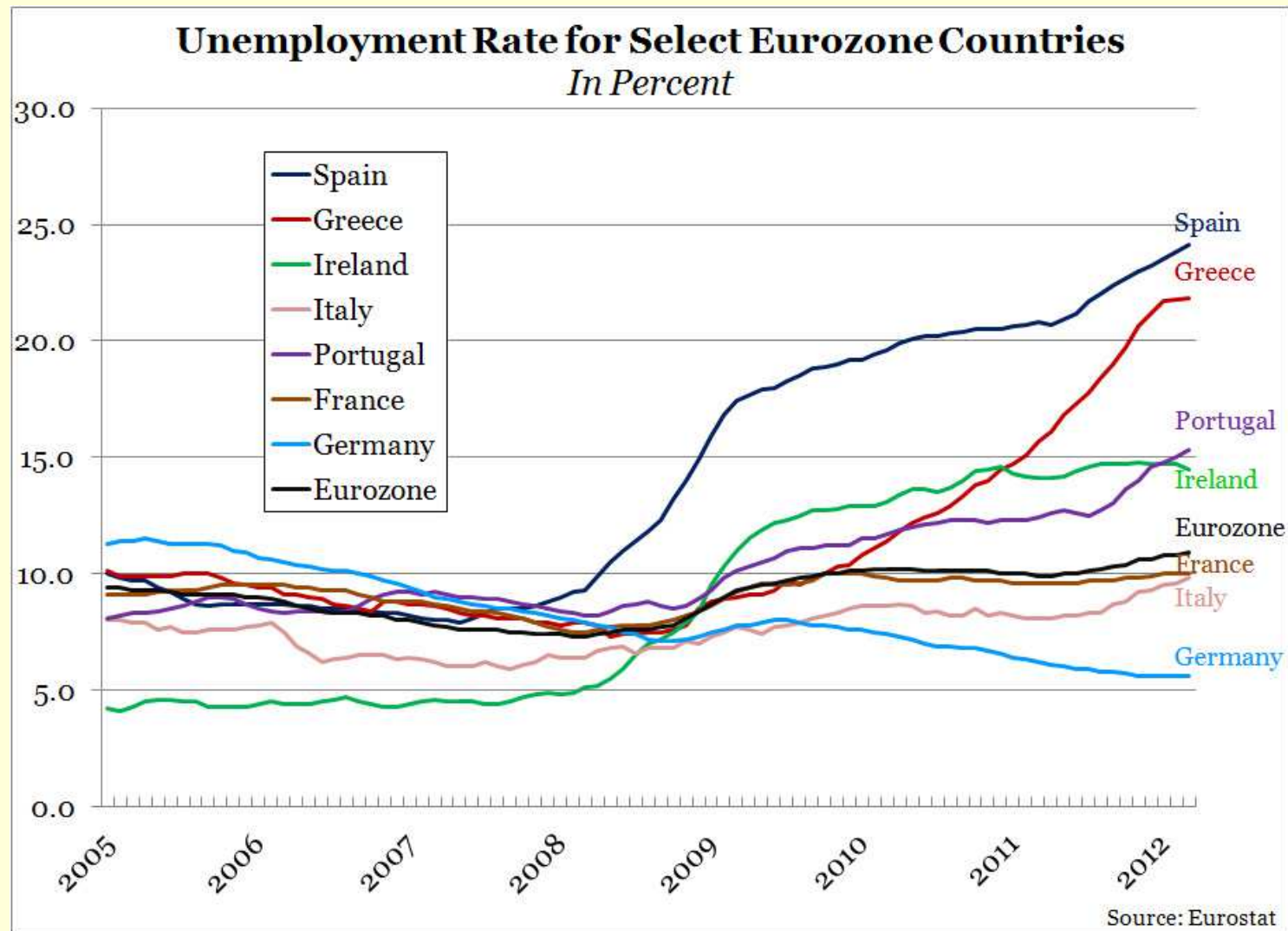
World Economic Collapse

- Hardest hit: countries dependent on export of manufactured goods for essentials
 - Japan
- Single-export countries
 - South America

Unemployment during the Great Depression



Unemployment in the Eurozone Today



Initial Government Attempts to Increase Demand

- Brazil
 - surplus of coffee beans set on fire, used to build highways
- USA: “planned scarcity”
 - Vegetables, fruits and animals destroyed
 - Steinbeck’s *The Grapes of Wrath*

Advice to Hoover

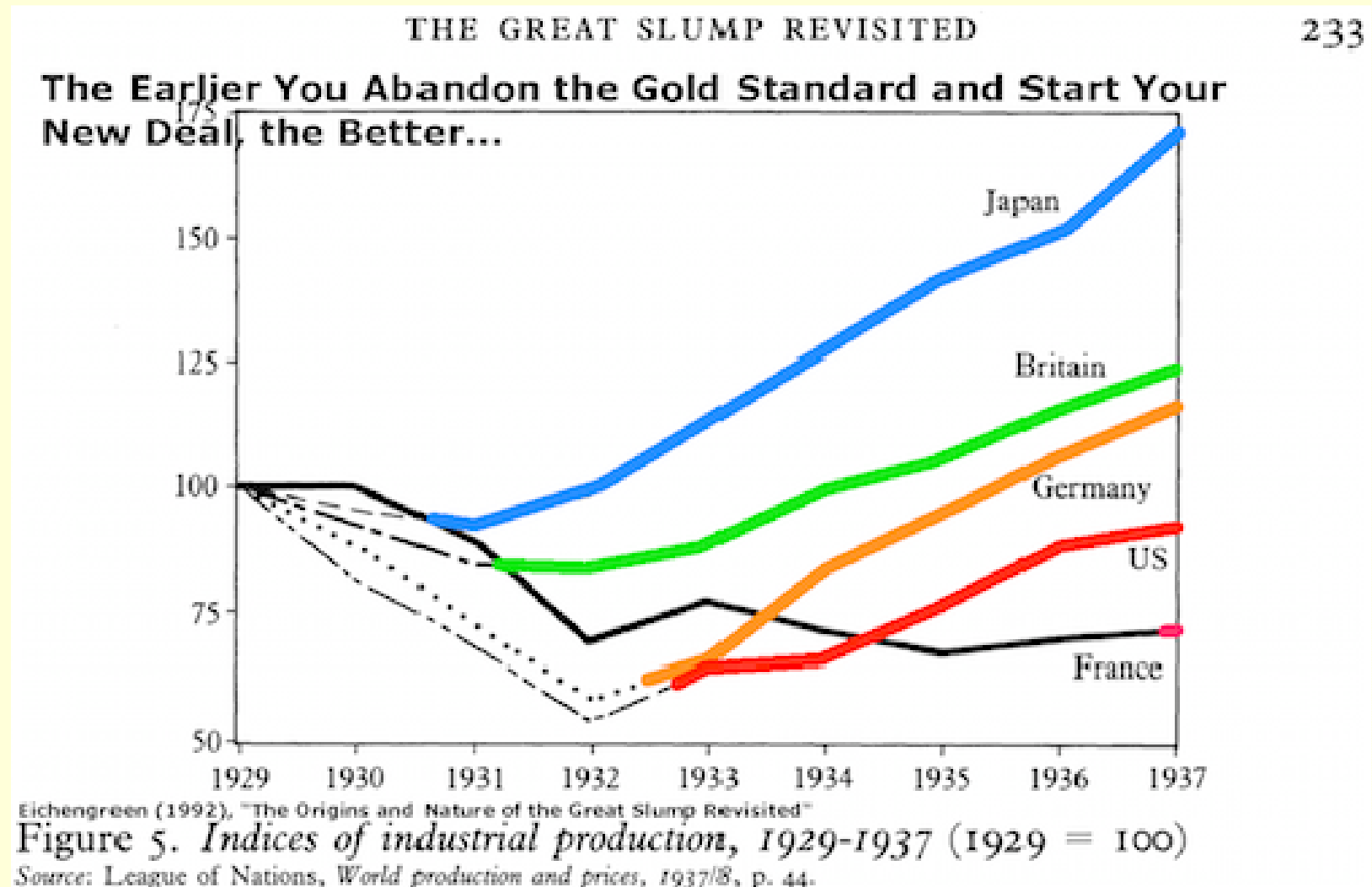
- “The government must keep its hands off and let the slump liquidate itself. Liquidate labor, liquidate stocks, liquidate the farms, liquidate real estate. When the people get an inflation brainstorm, the only way to get it out of their blood is to let it collapse. A panic is not altogether a bad thing. It will purge the rottenness out of the system. High costs of living and high living will come down. People will work harder, live a more moral life. Values will be adjusted, and enterprising people will pick up the wrecks from less competent people.”

-Treasury Secretary Andrew W. Mellon

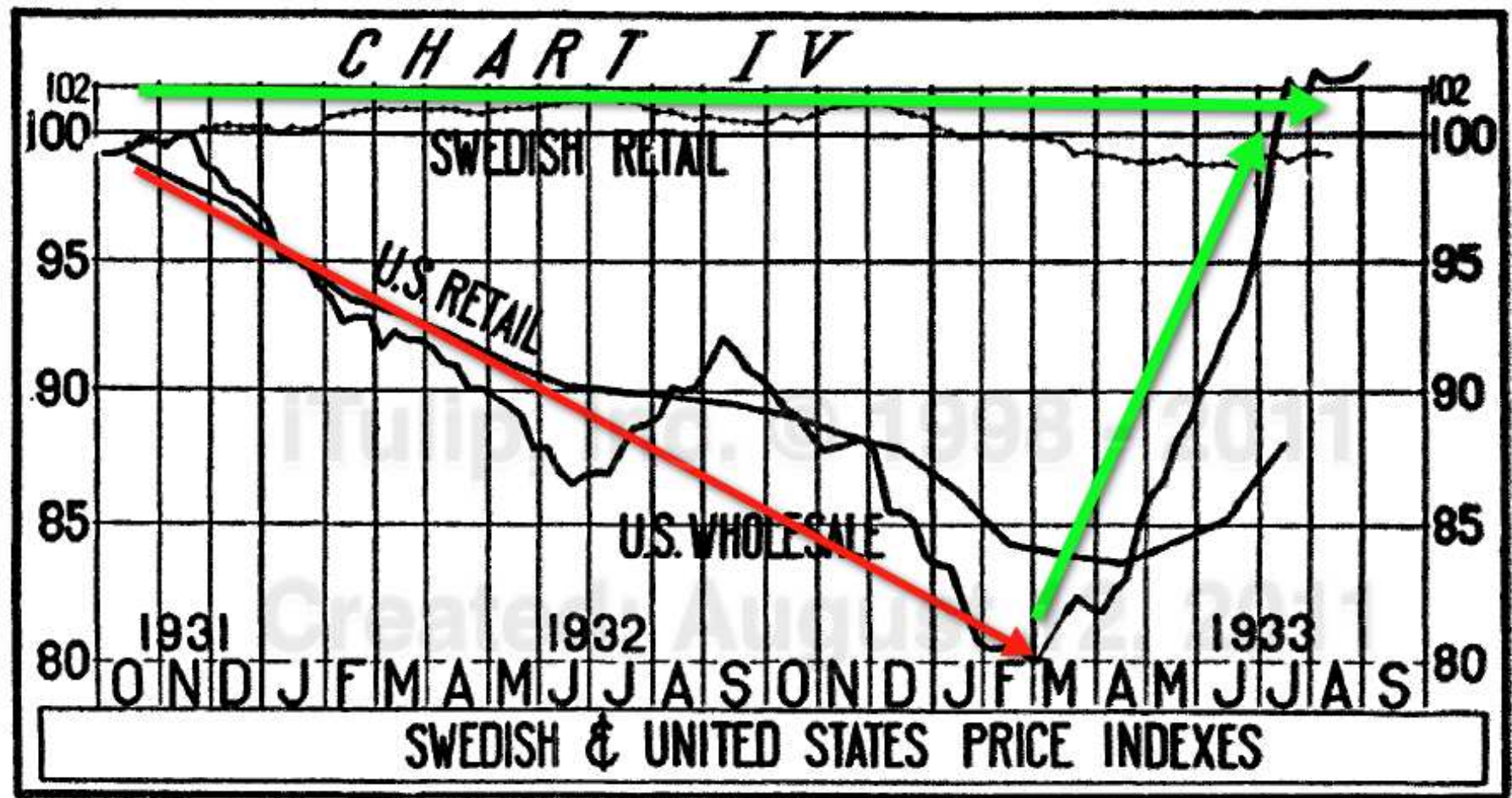
New US Strategies

- *Laissez-faire*, “planned scarcity” approaches fail
- John Maynard Keynes, economist
 - Stimulate economy by lowering interest rates
 - Government spending to compensate for private deleveraging
 - encouraging investment, employment
 - Leave the gold standard – release from “golden fetters”
- The New Deal of Franklin Delano Roosevelt
- WWII Spending

Golden Fetters



Golden Fetters



Franklin Delano Roosevelt



FDR

The Welfare State

- The pain of the 1930s helped to create a constituency for active government involvement in citizen's economic affairs to ameliorate economic downturns and misfortune.
 - Old age pensions
 - Health care
 - Food stamps and aid to children
 - Unemployment insurance
 - Work place regulations
- Liberal economics would be “softened” but too far?

Social Security Act of 1936

