

The Great Depression was a worldwide event:

- By 1929, unemployment increases worldwide

American Farmers Face Problems First



Farm overproduction during WWI

- Govt subsidized crops (paid higher prices for grain and wheat)
- Farmers
 borrowed money
 to enlarge and
 modernize farms

After wartime subsidies were cut

With the same
 payments needing to
 be made month to
 month → farm
 foreclosures
 increased



There are 4 causes of the Great Depression

- 1. Overproduction
- 2. Banking and Monetary Policies
 - 3. Stock Market Actions
 - 4. Political Decisions

1. Overproduction



High availability of consumer goods

- Electric appliances, automobiles

Americans feel they deserve to reward themselves following WWI



Availability leads to a high demand for goods

 Companies begin to produce more and more to attempt to meet growing consumer demand



The continued uneven distribution of wealth didn't stop the poor and middle class from being able to possess "luxury items", such as cars and radios

Reality:



-Real under-consumption is creating a "bubble":

Although people wanted the items, they didn't have enough cash to buy everything they wanted → bought "on credit"

-Uneven distribution of wealth and income

Wages were not keeping up with prices of goods

- Solution: buy "on credit"
- By end of 1920s 60% of cars and 80% of radios were bought on installment credit

Choose Your Christmas Phonograph Today And Save An Extra 5 Per Cent!

Here you are sure of finding an upright or console "Nightingale" that best harmonizes with your musical taste and with your carefully selected home furnishings. And—today—double Gold Bond Dividends save you an extra 5% on these close to one-half prices.

New \$100.00 "Nightingale" Models!

§49.75

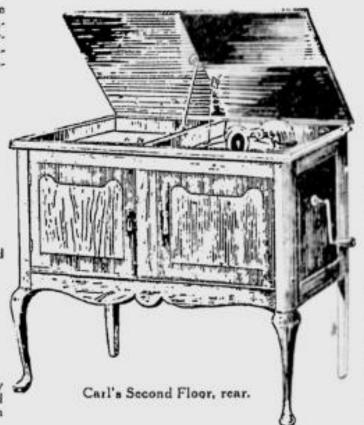
New \$150.00 "Nightingale" Models!

§69.75

You can have one delivered to your home or held for Christmas delivery by paying.

Only \$1 Down!

The balance can then be paid in six small monthly payments. \$10.00 worth of records may be added to the purchase price without any additional down payment.



2. Banking and Monetary Policies



The Federal Reserve Board

Federal Reserve Act (1907) in response to the banking crisis

- Meant to be protective "Watchdog" of economy by managing the money supply
- Set the interest rates for loans issued by banks

ECONOMIC CYCLE



EARLY UPSWING PHASE

- Increasing confidence
- *Healthy economic growth *Inflation remains low
- MARKETS :
- *Short rates at neutral
- *Bond stable
- *Stock market strong
- *Commodities strong
- Property prices picking up

RECOVERY PHASE

- *Stimulatory economic policies
- *Confidence picks up
- *Inflation falling

MARKETS :

- *Short rates low or falling
- *Bond yields bottoming
- *Stock market rising
- *Commodities rising
- *Property prices bottoming

LATE UPSWING PHASE

- *Boom mentality
- *Inflation gradually picks up
- Policy becomes restrictive

MARKETS :

- *Short rates rising
- *Bond yields rise
- *Stock market topping out
- *Commodities rising strongly
- *Property prices rising strongly

ECONOMY SLOWS/ENTERS RECESSION

- Confidence suddenly drops
- *Inflation continues to rise
- *Inventory correction begins

MARKETS :

- *Short rates peaks
- *Bond yields tops out
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- Stock market starts falling
- Commodities starts falling
- Property prices tops out

RECESSION

- *Confidence weak
- Inflation peaks
- Production falling

MARKETS:

- *Short rates drops
- *Bond yields drops
- ·Stock market bottoming
- Commodities weak
- *Property prices weak





In 1920s: "The Fed" set interest rates very low

- To encourage people to take out loans to try to stimulate the economy
- More consumers → higher profit → companies can afford to produce more → leads to a surplus of goods

1929: Fed worried growth was too rapid

 Raise interest rates and tighten supply of money → consumers responded

3. Stock Market Actions





The Stock Market was/is an indicator of national prosperity

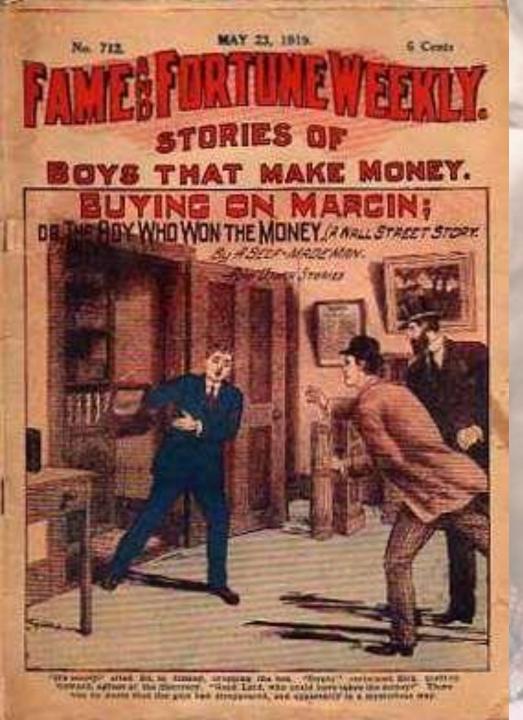
Buying "on margin"

Just like one could buy goods on credit, it was easy to borrow money to invest in the stock market

– "Margin investing" or "buying on margin"

Small investors more likely to invest in stock market in large numbers because the "margin requirement" was only 10%

 - \$1000 worth of stock could be bought with 10% down and you pay the rest with your dividends



1920s: business is "booming"

- Stock prices rising
- Growing profits

Speculation:

stockbrokers predict which stocks will do well

Causes prices to rise

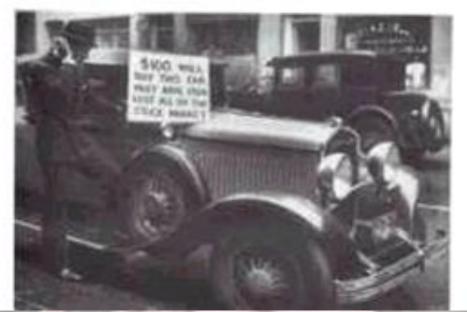
What went wrong?

Banks began to loan money to stock buyers/brokers

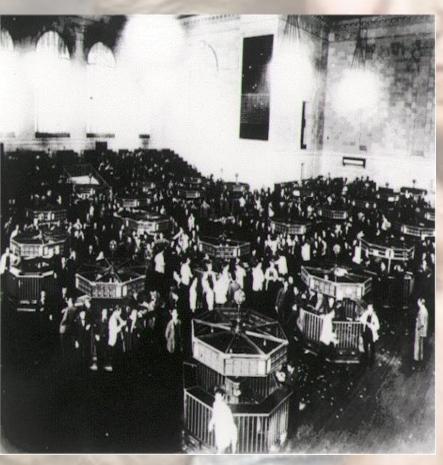
Allowed to use their stock as "collateral" for defaulted loans

What does this mean for banks if the stock loses value?





The Crash



- Stock prices decline in September
- 24 October "Black Thursday"
- 28 October "Black Monday"
- 29 October 1929 "Black
 Tuesday", prices collapsed
 completely and a share selling
 frenzy occurred
- Over 16m shares sold
- Losses exceeded \$26 billion

Some historians say it was a symptom of more than a cause of the GD

The Federal Reserve Could Have Intervened

The Fed was established (in part) to prevent banks from closing

However, The Fed had previously lowered the reserve requirement of cash to be held by banks
Many banks didn't have enough cash to match amount of money in customer accounts



Bad Banking Practices

- -Loss of confidence in stocks led to loss of confidence in security of money being held by banks
- -Customers raced to banks to withdraw their savings
- -"Bank Runs" become a regular occurrence





1930

-60 bank failures per month

1930 - 1933

-9,000 bank failures

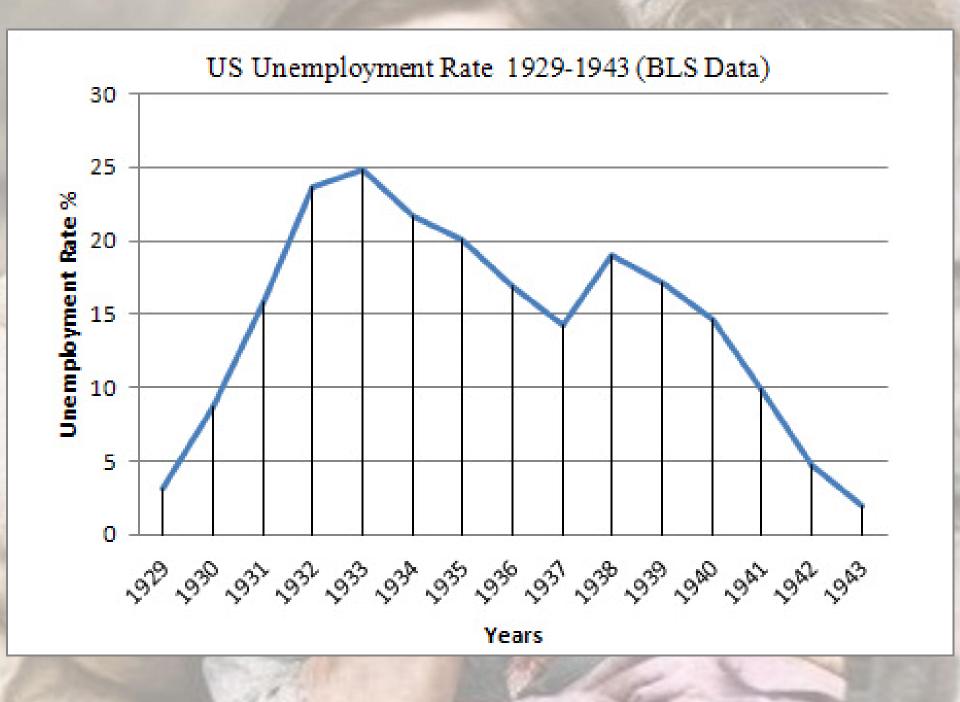
A Downward Spiral:

When banks fail, money just "disappears" from the economy

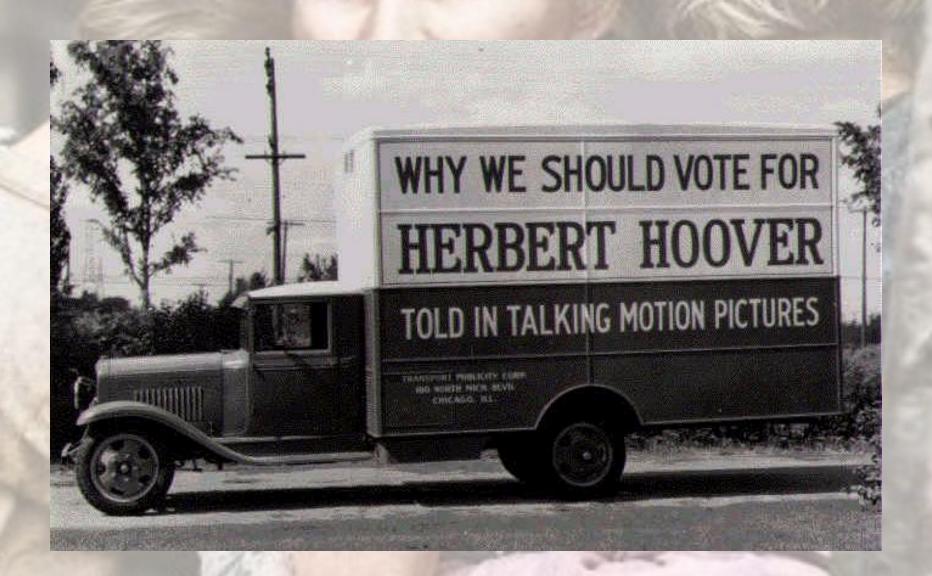
- No insurance for savings deposits → many lost their life savings
- As more banks close → people lose money →
 more fear of banks and more runs

Businesses lose money

Many go bankrupt → close their doors → leaving workers unemployed



4. Political Decisions



The Depression could have been less severe had policy-makers not made certain mistakes



Leaders in govt and business relied on poor advice from economic and political experts





"The sole function of the government is to bring about a condition of affairs favorable to the beneficial development of private enterprise."

-Herbert Hoover (1930)

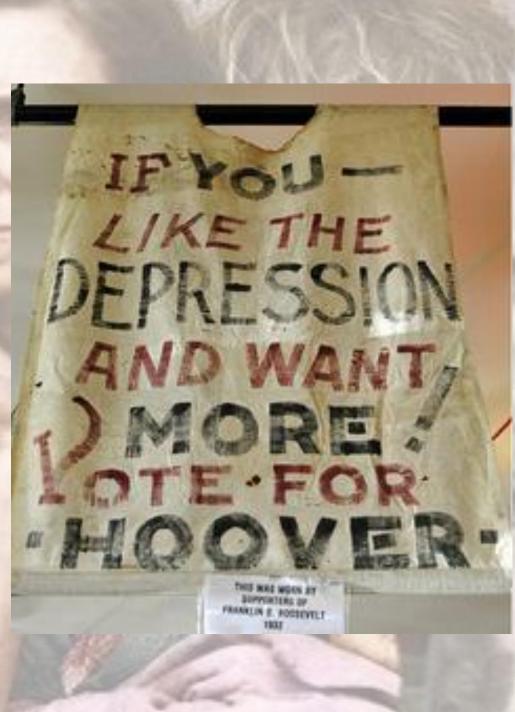


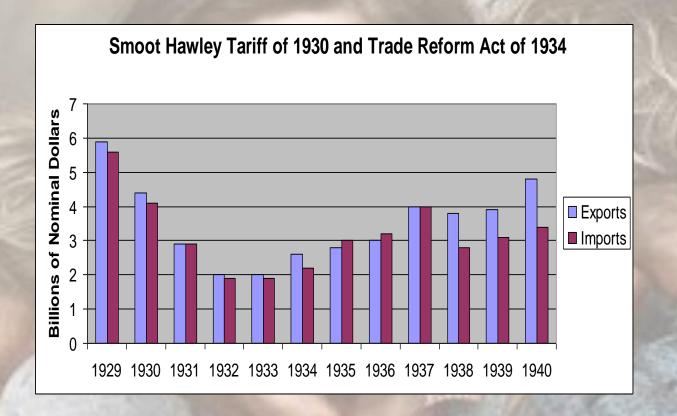
Within a month of "The Crash", Hoover met with key business leaders:

> -Urged them to keep wages high, even though prices and profits were falling

Biggest mistake of Hoover administration was the Hawley-Smoot Tariff Act (1930):

- -Raised most tariffs to 40-48%
- -Believed trade barriers would force Americans to buy American, therefore producing jobs





Leaders ignored that trade is two-way street

• If foreigners can't sell goods in the U.S., they will cut down our exports there