**To what extent was buying on margin the primary cause of Black Tuesday in the New York Stock Exchange on 10/29/1929?**

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**Section A:**

The task of this investigation is to determine the primary cause of Black Tuesday in the New York Stock Exchange in 1929. The primary method will be comparing and contrasting evidence from sources such as business historian Maury Klein’s *Rainbow’s End: The Crash of 1929* and economics professor Gene Smiley’s *Margin Purchases, Brokers' Loans and the Bull Market of the Twenties*. Klein and Smiley provide insight into margin purchases and easy credit, as well as Federal Reserve policies, as possible causes driving the crash.

This origin of this book is that it was written in 2001 by Maury Klein, a Professor Emeritus of History at the University of Rhode Island who specializes in American business history. The value of the origins is that since Klein specializes in business history, he can give educated insight on possible causes of the crash by drawing parallels with other historical economic crashes. The limitation of the origins is that because the University of Rhode Island is liberal, Klein's analysis reflects liberal economics and with it an opposition to governmental intervention in the economy.

The purpose of this book is to defend the notion that a host of varying factors, not simply causes nested within the stock market, prompted the crash of 1929. The value of the purpose is that since Klein defends various non-monetary factors, he poses strong arguments for commonly overlooked possible causes. The limitation of the purpose is that since Klein is defending other factors, there is minimal focus on the effect of forces within the stock market.

The content of this book is an assertion of how causes of the crash were not solely economically oriented, as supported by multiple perspectives. The value of the content is that since Klein cites many contemporary and historical sources to support his claims, the writing is relatively moderate and unbiased. The limitation of the content is that since Klein asserts the crash cannot be explained by economics or observable forces but should instead be justified by levels of market optimism, he focuses on more marginal factors such as sports, religion, or other aspects of culture and society which hardly relate to the crash.

The origin of this article is that it was written in 1988 by Gene Smiley, a Professor Emeritus of Economics at Marquette University who was also past President of the Economic and Business Historical Society. The value of the origins is that Smiley's past position as president of the Economic and Business Historical Society, a moderate organization, allows him to take a holistic view on the crash of 1929. The limitation of the origins is that since Smiley specializes more in economics and less in history, he lacks the historical context to successfully analyze the complex forces driving the market in 1929.

The purpose of this article is to reevaluate the widely accepted view that margin purchases and brokers’ loans caused Black Tuesday. The value of the purpose is that since the article is reevaluating, it considers and builds off of existing strong arguments. The limitation of the purpose is that since Smiley structures his argument around evaluation of prior interpretations, he brings in little new evidence to support his claims.

The content of this article is the discrediting of the claim that margin purchases and brokers’ loans caused Black Tuesday, as seen through study of inner scope accounts from the crash. The value of the content is that because a lot of inner scope material is cited, there is plenty of direct evidence regarding the situation. The limitation of the content is that because Smiley focuses on refuting the effect of margin purchases and brokers’ loans, other possible factors and their relations to the crash are omitted, while the extent to which margin purchases and brokers’ loans were influenced by these causes is then oversimplified.

**Section B:**

After World War I, the United States plunged into a post-war recession which lasted until the end of the 1910s. The “Roaring Twenties” was fueled by the rising ideal of consumerism, which caused overconfidence in the national economy. Easy credit and the proliferation of margin purchases allowed many to get rich quickly, but also corroded the stability of the market. Such deficiencies were overlooked until October 1929, when the New York Stock Exchange went into one of the most vicious economic downward spirals in history, with the Dow having dropped 25% by the end of Black Tuesday. There is uncertainty surrounding the causes of this crash due to the lack of statistical correlation between any one factor and this downturn. Additionally, the emergence of multiple new patterns in the market during the 1920s makes it impossible to isolate a single variable as the sole cause. To a high extent, Black Tuesday was caused by the prevalence of buying on margin, but more primarily it was caused by the presence of easy credit.

The extent to which buying on margin caused Black Tuesday was high due to unwise speculation. There were no set margin requirements prior to the crash – they were determined by individual brokerages and banks (Rappoport 272). This allowed for the existence of extremely low margins requirements, some being as low as 10% from the mid-twenties to 1929 (Smiley 133). A New York Stock Exchange questionnaire found margins averaging around 40% by early 1929 (Rappoport 274). This suggests that most purchases were not backed by real money, making the loan structure dangerous once investors and bankers start defaulting on each other. Margin purchases were very common – for example, the number of stockbrokers in the US rose from 29,609 in 1920 to 70,950 by 1930 (Wecter 3). This aided the development of the economy, but also rooted instability into the structure. At the same time, rapid growth occurred in loans from private investors, corporations, and foreign banks – bankers’ loans from nonbank sources were 25-30% from 1922 to 1925 and became 78% by October 1929 (White 75) (Smiley 137). Furthermore, investment trusts from 40 in 1921 to over 750 in 1929 (White 69). These increases demonstrate the extent to which margin purchases have grown over the course of the 1920s. New listings on the New York Stock Exchange rose from 58 million shares in 1925 to 102 million in 1928 (Klein Rainbow 146). The increasing volume of stocks being issued and exchanged provided more opportunities for speculators to buy on margin, further destabilizing the market. Also, margin transactions went quickly, allowing inexperienced speculators to borrow considerable sums of money (Smiley 130). This accounts for many of the defaults and failures during the crash which intensified Black Tuesday. An estimated 90% of market transactions in the 1920s were such gambling ventures, not permanent transactions (Wecter 5). Thus, the debt structure constructed by the system of loans resulting from margin purchases allowed fluctuations in the market to easily trigger Black Tuesday.

The presence of easy credit led to Black Tuesday in the crash of 1929 to a major extent because it promoted margin purchases. In 1927, an outflow of $500 million in gold led New York city banks to withdraw from the call loan market, to be replaced by corporations, individuals, and foreigners lured by high interest rates (Klein Rainbow 328). This was made possible by a market eager for easy credit as well as enough brokers and bankers to provide it. Additionally, even though the Federal Reserve ordered banks to not lend money for speculative purposes in February 1929, private bankers led by Charles Mitchell unlocked millions for speculation in response (Wecter 5). This illustrates how there was always a ready source of easy credit for speculators, regardless of governmental controls. The Dow Jones Industrial Average went from 158.54 in January 1926 to 308.85 in March 1929, finally peaking at 386.1 in September 1929 (James 133). This promoted investors to use easy credit for margin purchases in hopes of monetary gain. However, easy credit often proved problematic – for example, collateral was often sold before all equity had disappeared (Rappoport 272). This highlights how extreme speculation caused by easy credit leads to lack of confidence on part of the lender, which in turn prompts unexpected calls. On September 20, 1929, Clarence Hatry’s business and financial empire collapsed in Britain, and the New York market responded with a 2.14% drop (James 133). This demonstrates how the debt structure supported by foreign loans due to easy credit was highly susceptible to collapse when triggered by unexpected events. Hence, easy credit promoted margin purchases, which crafted the loan structure leading to the crash.

Actions by the Federal Reserve were a cause of Black Tuesday to a moderate extent. In 1924, the Federal Reserve had 3 objectives: promote high levels of business activity and employment while keeping prices stable, curb speculative use of credit without making it scarcer for business and agricultural purposes, and assist in the reconstruction of monetary stability abroad (Klein Rainbow 78) (Anderson 57). The Board believed economic use of credit was to facilitate production and orderly marketing of goods, not to finance speculative holding of excessive securities (Anderson 33). Thus, the Federal Reserve did not add onto the problem of margin purchases due to easy credit in the early 1920s, and hence was not a contributing factor to the crash initially. However, in 1927 the New York reserve bank initiated an easy money policy to encourage domestic business and strengthen European exchanges (Klein Review 326). Because the Federal Reserve promoted easy credit policies, it could be held accountable for causing Black Tuesday to a considerable extent. Uncertainty regarding the market then led to a policy of “watchful waiting”, and only in 1928 was there a contractionary policy, with restraint through sales of securities and open market sales (Anderson 58). Historians such as Gene Smiley question whether these low margin requirements fostered the boom – because if so, the boom should have happened in years prior to 1929, not at the time of the crash. However, the Reserve’s easy money policies in earlier years had planted instability in the market which facilitated the 1929 crash. There was a rise in the discount rate from 3.5% to 5% in January of 1928, and another rise to 6% in August (White 74) (White 80). The rise in rates before the imminent crash eased the consequences, but the Federal Reserve was widely blamed for not tightening credit fast enough (Klein Review 327). This means the reluctant policymaking by the Federal Reserve failed to effectively curb speculation and hence contributed to Black Tuesday.

To a low extent, overproduction helped lead to Black Tuesday. American manufacturing production jumped by 24% from 1923 to 1929, demonstrating huge increases in the amount of goods being produced in the 1920s (Hillstrom 9). However, most notable was overproduction in the agricultural sector caused by technological improvements – for example, world wheat production increased 80% in 1926-1930 while world rye production averaged 42% more in 1921-1929 than in 1912-1920 (Gray 66) (Gray 64). Such increases illustrate the great extent to which farmers became more productive on a global scale. In the United States, agricultural overproduction caused for an export surplus totaling $2.7 billion for four years in the 1920s, higher than any time period prior to 1914 (Klein Review 329). As agriculture was one of the biggest sectors in the American economy, such a surplus lowered farm prices and resulted in an agricultural recession in the early 1920s. However, the agricultural sector began to recover over the decade, and overproduction hence bears little relation to the stock market crash in 1929. And even so, 2.5 million farming tenants were not subject to heavy land taxes or mortgage indebtedness (Gray 63). This demonstrates how even though overproduction, namely agriculturally, hurt the economy, its results were greatly limited and were also distant enough from the crash of 1929 to have significant effect in stimulating Black Tuesday.

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