

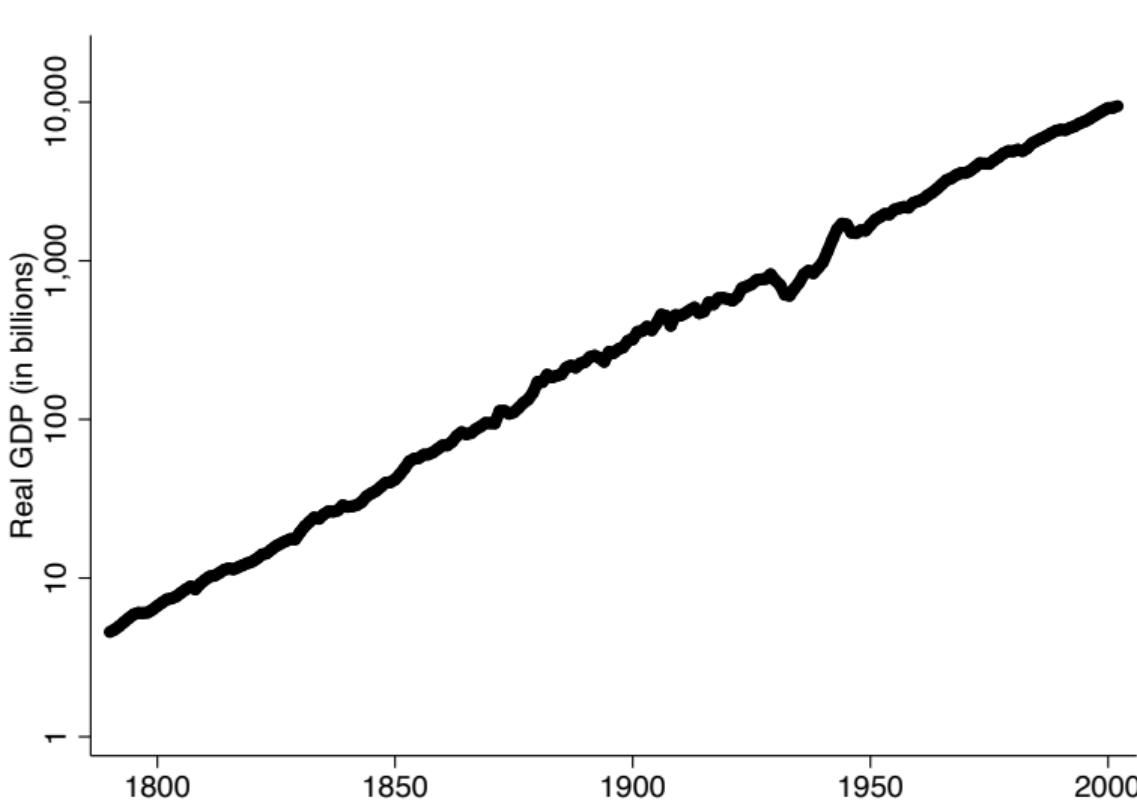
11. The Great Depression

Econ 373: US Economic History

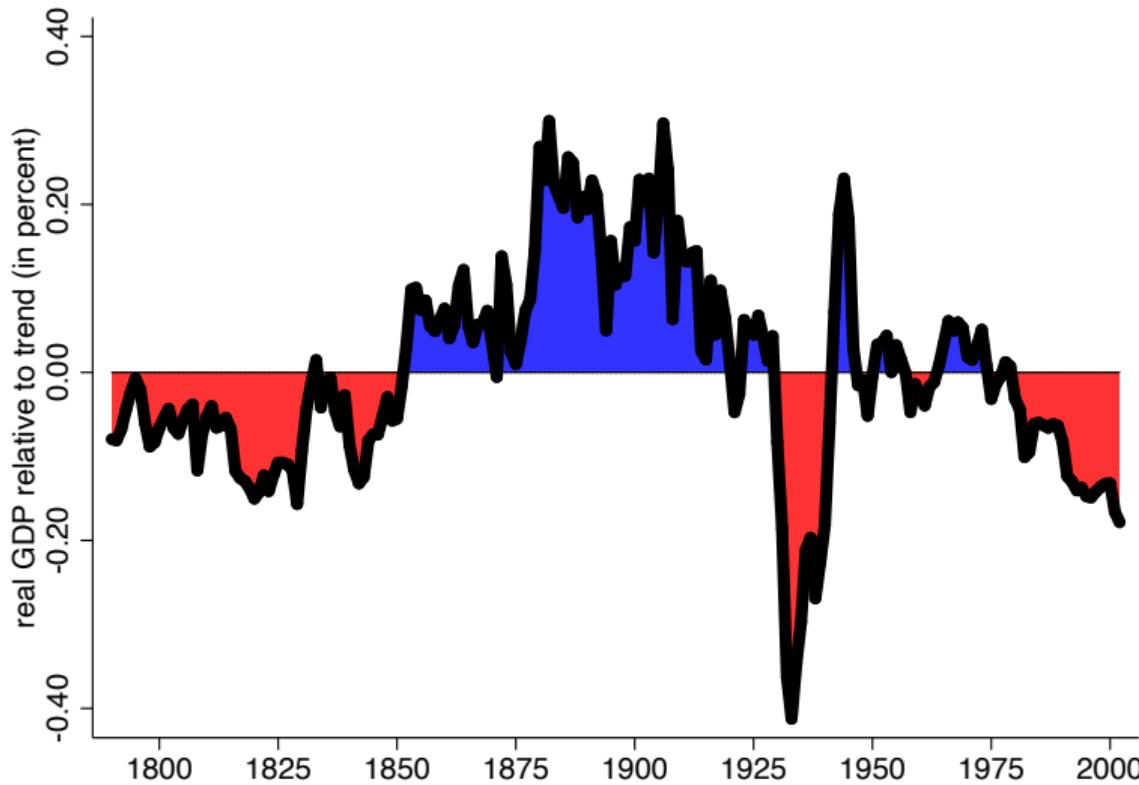
Taylor Jaworski

Fall 2023

Economic growth is a theme of US history and this course

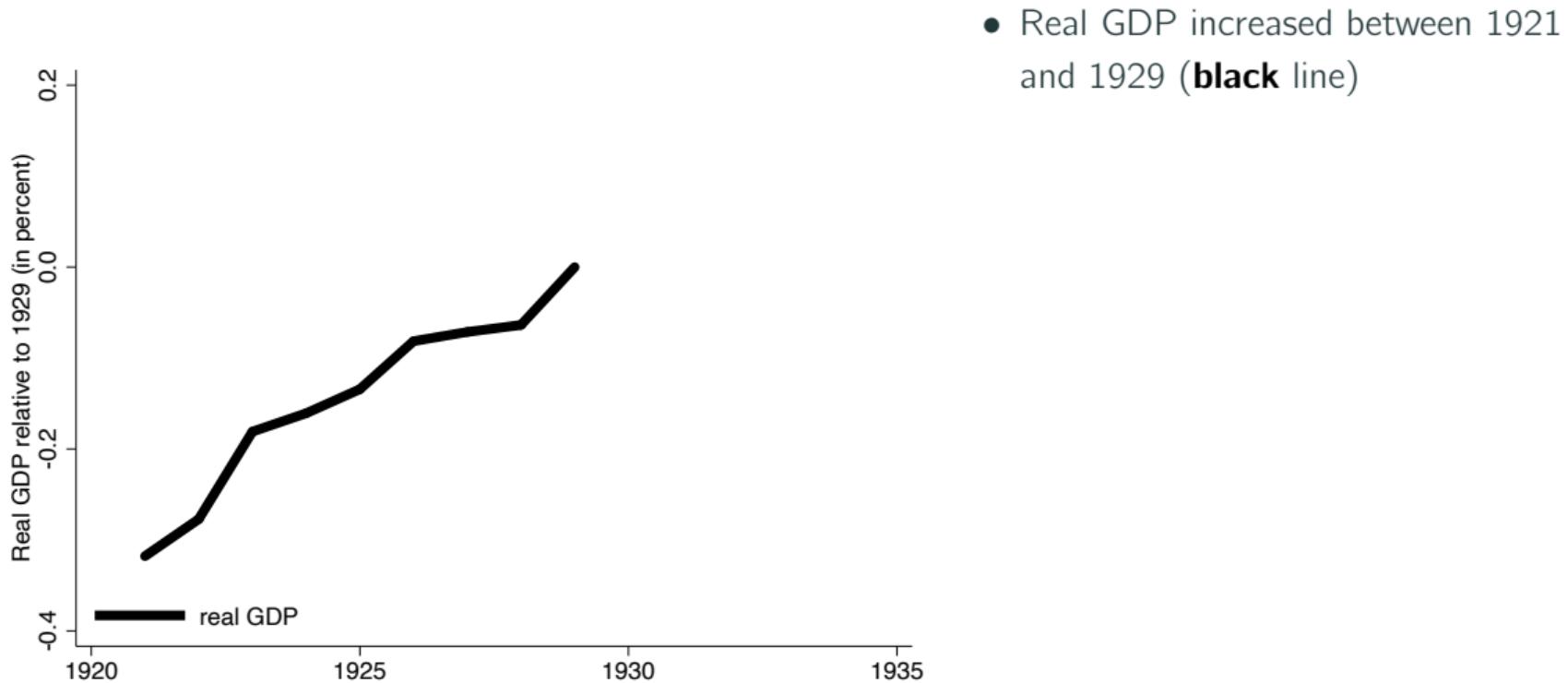


Business cycle **expansions** and **contractions** are also common

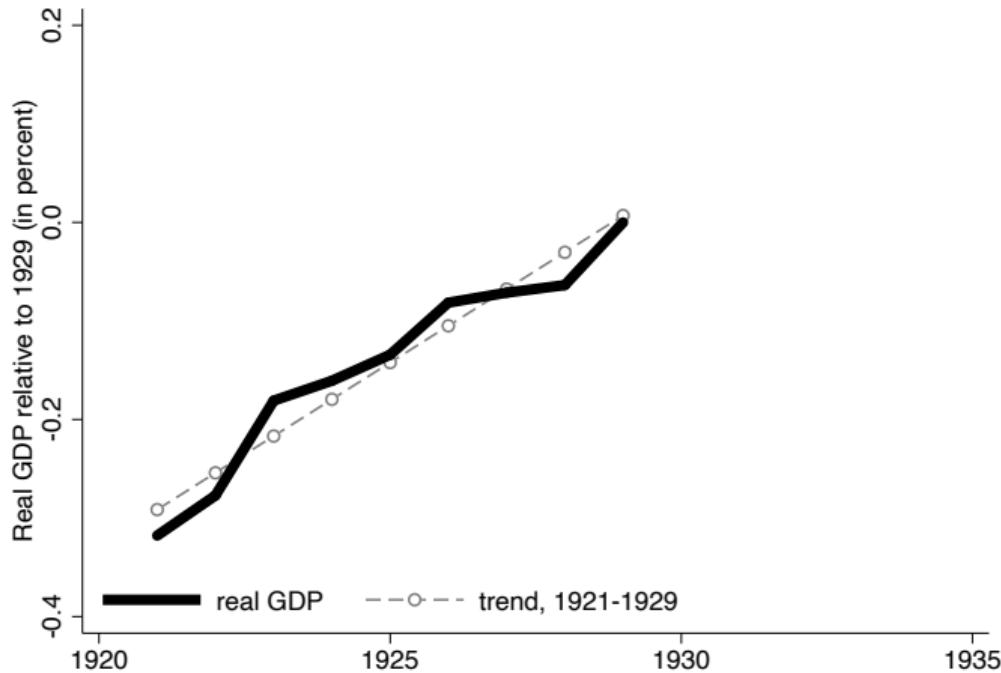


The **Great Depression** was the most significant downturn of the 20thC

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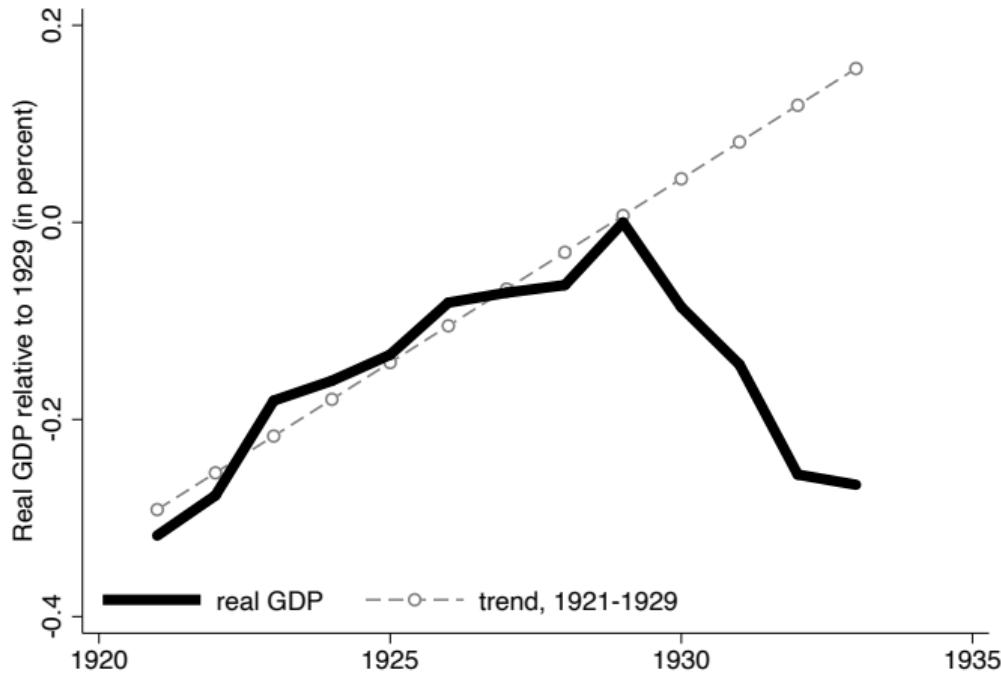


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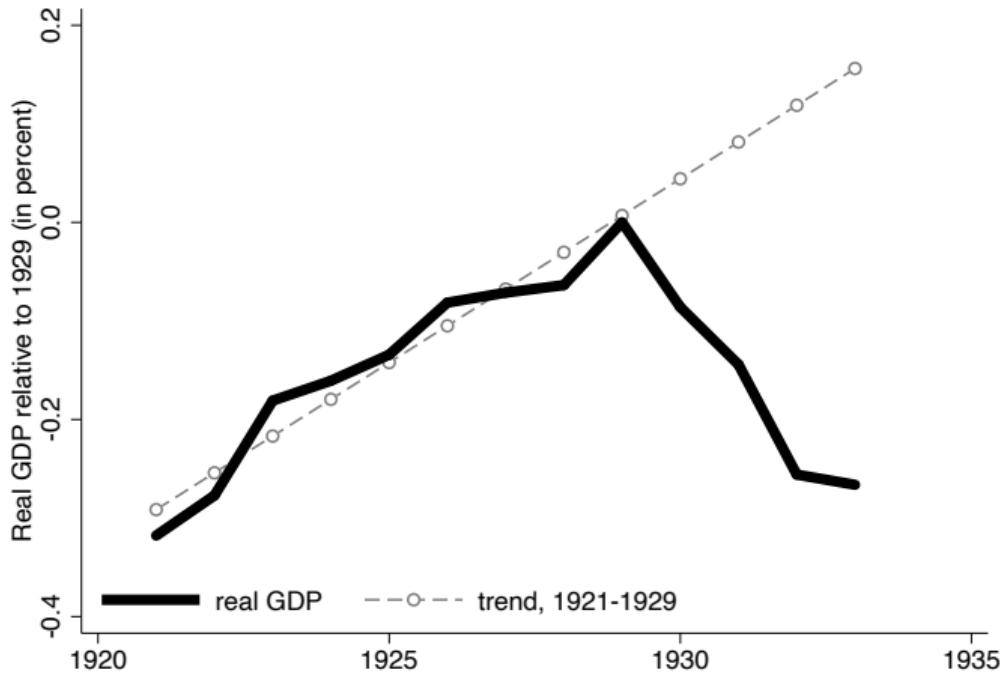
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- The **gray** line shows the linear trend over this period
- From 1929 to 1933 real GDP decreased by 25 percent
- The gap between the **black** and **gray** lines is missed “potential”

The **Great Depression** was the most significant downturn of the 20thC

- Unemployment increased from below 5 percent in 1929 to above 25 percent in 1933 and total **employment** decreased from nearly 9 million to just above five million



The **Great Depression** was the most significant downturn of the 20thC

- Unemployment increased from below 5 percent in 1929 to above 25 percent in 1933 and total employment decreased from nearly 9 million to just above five million
- In addition, **industrial production** and the **Standard & Poor's index** decreased substantially



Questions about the **US economy in the 1930s**

- What **caused** the Great Depression?
- What was the **government response** to the Great Depression?
- When and why did the economy **recover** from the Great Depression?
- Why did the Great Depression **last so long**?
- What were the **lasting effects** of the Great Depression?

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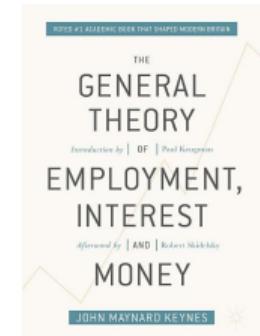
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The **causes** of the Great Depression

- We will contrast two broad explanations for business cycle fluctuations and use these to understand the 1930s Great Depression in the United States:

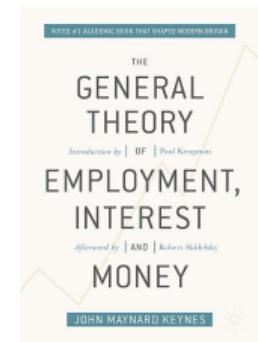
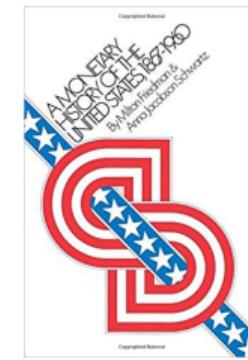
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The **causes** of the Great Depression

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 1. **Aggregate demand**—associated with John Maynard Keynes
 2. **Monetary policy**—associated with Milton Friedman and Anna Schwartz



Aggregate demand explanations for the Great Depression

- Let's start with the identity between aggregate supply (GNP) and aggregate demand:

$$GNP = C + I + (X - M) + G$$

- And then rewrite this formulation in changes as:

$$\Delta GNP = \text{multiplier} \times (\Delta C + \Delta I + \Delta(X - M) + \Delta G)$$

- From the expression above we can turn to **empirical evidence** on the sources of the decrease in aggregate demand during the Great Depression

Aggregate demand: **consumption**

- Between 1929 and 1933 **consumption expenditures** decreased from \$77 billion to \$46 billion (or in real terms to \$59 billion, 23 percent!)
- Income for **farmers**—a group that accounted for roughly 1/4 of US population at the time—decreased by 30 percent from \$6.2 billion in 1929 to \$4.3 billion in 1930
 - due to increased production from 1929 to 1930 and shrinking domestic and overseas markets that led to a collapse of farm prices
- The economist Peter Temin summarized the role of the consumption decline as:
[T]he fall in consumption was unusually large in 1929.... Goods that could not be sold were not produced. The fall in aggregate demand spread throughout the economy. And as the fall of 1930 wore on and business did not recover...businessmen lost the confidence that underlies private investment. The economy continued to decline.

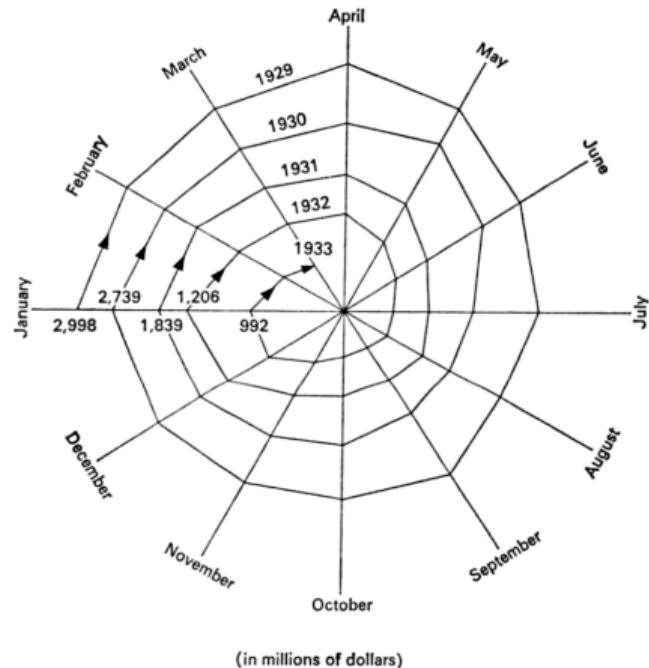
Aggregate demand: **investment**

- Gross domestic private investment, which reached its peak in 1926, was at \$16.2 billion in 1929 and decreased further to \$1.0 billion in 1932
 - changes in investment during the early years are quantitatively sufficient to explain the entire change in aggregate demand from 1929 to 1933
- Decomposing gross domestic private investment, a large portion of the total change can be explained by the decline in residential construction, which had stalled since 1926
- Keynes wrote:

I attribute the slump of 1930 primarily to the deterrent effects on investment of the long period of clear money which preceded the collapse itself. But the collapse having occurred, it greatly aggravated matters, especially in the United States, by causing disinvestment in working capital.

Aggregate demand: **net exports**

- In 1928, the **Smoot-Hawley Tariff Act** precipitated a worldwide trade war
 - duties imposed on sugar, wheat, textiles, etc
 - average ad valorem tariff rates on all goods increased from 25 percent to 50 percent
- US net exports were \$1 billion in 1928 and decreased to \$33 million in 1936
 - and world trade collapsed
- US balance of payments shifted from deficit to surplus, US prices fell less than other countries



Aggregate demand: **government spending**

- From 1929 to 1931 the federal government increased spending, e.g.,
 - \$500 million for public buildings
 - \$150 million for rivers and harbors
 - \$75 million for roads
 - \$60 million to start Boulder Dam
 - \$160 million income tax decrease
- The federal deficit increased in 1932 due to decreased receipts and increased spending
- In 1932 federal government fiscal policy turned from [counter-cyclical](#) to [pro-cyclical](#), e.g., large tax increase passed on June 6

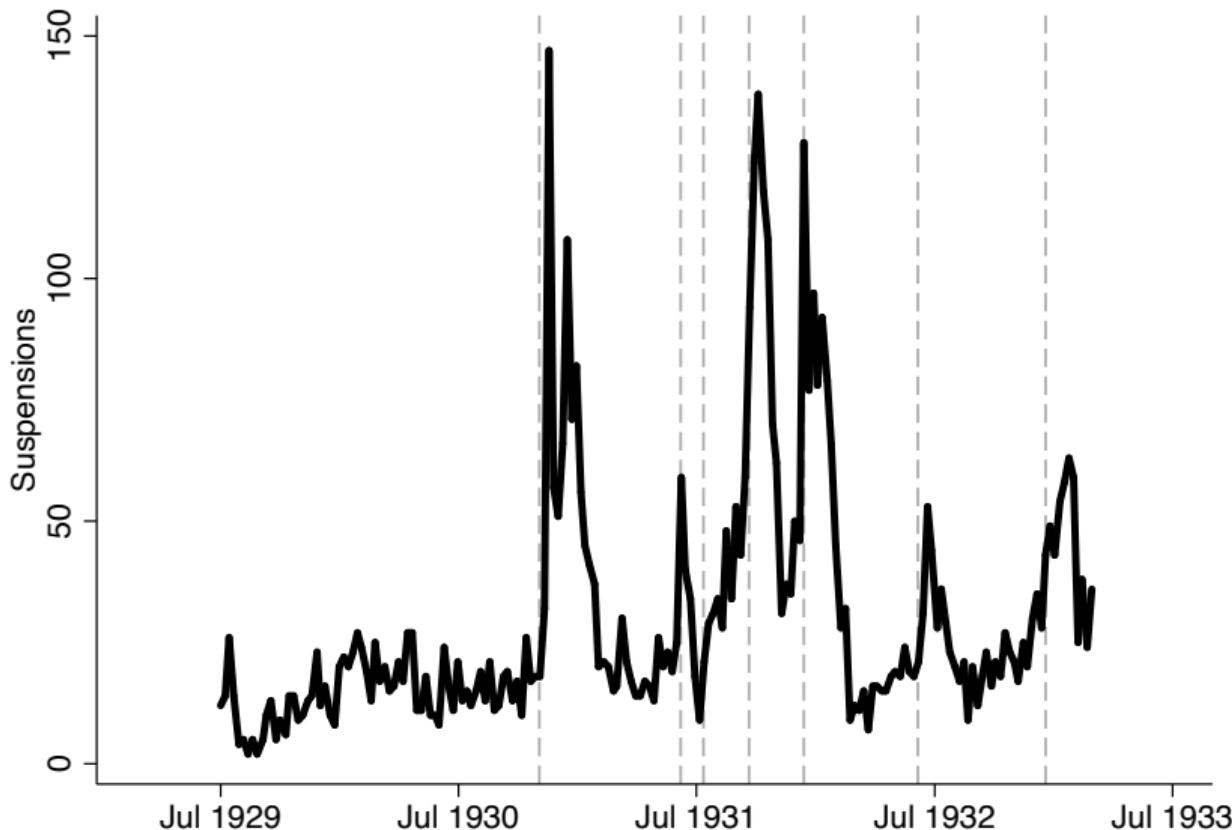
The Friedman and Schwartz view: **monetary shocks**

- Friedman and Schwartz emphasized the role of **five** shocks to the financial system:
 - The Great Crash (Oct 1929)
 - First Banking Crisis (Oct 1930 to Feb 1931)
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- **Bank failures** increased in the wake of each shock, this decreased public confidence in the banking system and helped turn recession to depression

Bank suspensions during the Great Depression



The economics of **bank runs**

- Let's model the banking crises during the Depression as simple game between two depositors, each has deposited D with a bank
- The bank has invested the deposits in a long-term project and can only return $2 \times r$ to depositors in the short-run, where $D > r > D/2$
- The bank will return $2 \times R$ in the long run if the investment is allowed to reach maturity, where $R > D$
- The game is played over two time periods, in the short-run before the investment matures and in the long-run after the investment matures

The economics of **bank runs**

Date 1

	withdraw	don't
withdraw	r, r	$D, 2r - D$
don't	$2r - D, D$	next stage

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Date 2

	withdraw	don't
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don't	$D, 2R - D$	R, R

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Combining Date 1 and Date 2

withdraw don't

withdraw
don't

r, r	$D, 2r - D$
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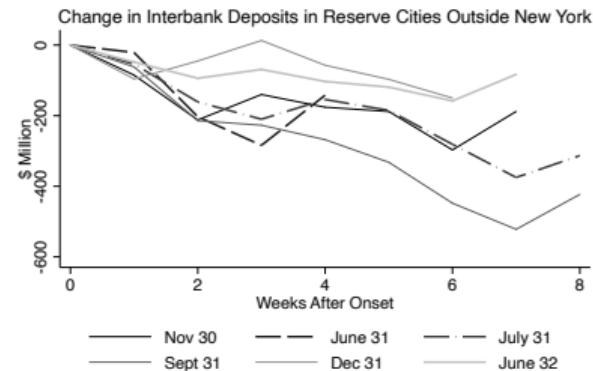
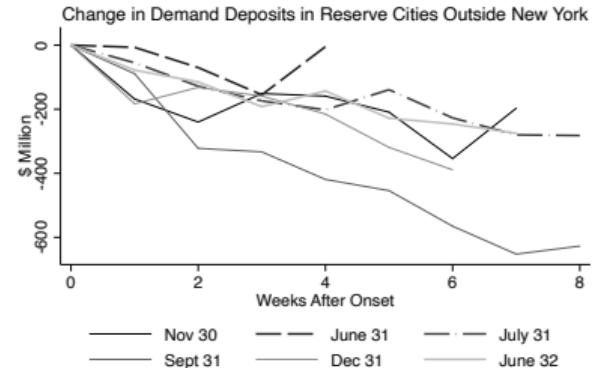
	withdraw	don't
withdraw	r, r	$D, 2r - D$
don't	$2r - D, D$	R, R

The economics of **bank runs**

- There are two pure-strategy Nash equilibria:
 - (1) both investors withdraw and each receives a payoff of r (in date 1)
 - (2) both investors do not withdraw (in date 1) and each receives a payoff of R (in date 2)
- The outcome in (1) is a bank run: if each investor believes the other will withdraw, the best response is to withdraw even though both investors are better off waiting
- The outcome in (1) is inefficient, the outcome (2) is efficient; the model does not predict which outcome will occur but shows that bank runs can emerge in equilibrium

Amplification through interbank lending

- Banking panics induced withdrawal of deposits from Federal Reserve member banks
- These correspondent banks subsequently curtailed lending to businesses in response
- As a result, interbank amplification reduced commercial bank lending by 15 percent



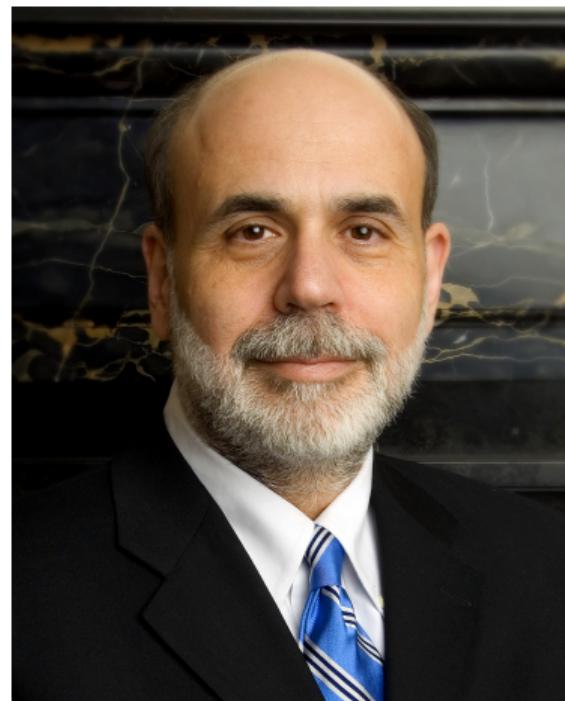
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 - ▷ Final Banking Crisis (Oct 1932 to Mar 1933)
- ▷ Bank failures increased in the wake of each shock, this decreased public confidence in the banking system and helped turn recession to depression
- Finally, the **Federal Reserve's contractionary policy** exacerbated the crisis (F&S called the policy "inept") and the monetary system was allowed to collapse

Lessons from contractionary policy

Let me end my talk by abusing slightly my status as an official representative of the Federal Reserve. I would like to say to Milton and Anna: Regarding the Great Depression. You're right, we did it. We're very sorry. But thanks to you, we won't do it again.

—Ben Bernanke (November 8, 2002)



Lessons from contractionary policy

THE WALL STREET JOURNAL.

ECONOMY | U.S. ECONOMY

Fed Unveils Major Expansion of Market Intervention

Central bank will begin lending operations to unclog corporate and municipal debt markets

English Edition | March 24, 2020 | Print Edition | Video

Monday's dramatic Federal Reserve announcements, explained

They include big new lending programs — but state and local governments are left out of the party.

By Matthew Yglesias | matty@vox.com | Mar 23, 2020, 11:00am EDT

TheUpshot

The Fed's Message: The Money-Printing Presses Are Fired Up and Ready to Go

Its actions Monday show it will do anything necessary to address a glaring shortage of dollars across the economy.



By Neil Irwin

March 23, 2020

Economics

Fed Unleashes Unprecedented Measures to Shore Up Reeling Economy

By Christopher Condon, Craig Torniai, Matthew Boesky, and Michael McKee

March 23, 2020, 6:00 AM MDT Updated on March 23, 2020, 10:34 AM MDT

The New York Times



By Ben Casselman

March 23, 2020

Whatever It Takes: How the Fed Aims to Rescue the Economy

The central bank is using tactics from the last financial crisis and deploying new ones to keep money flowing. Here are the basics.

Taking stock of the **causes** of the Great Depression

- Aggregate demand-based explanations:

- Consumption: ✓ Investment: ✓ Net exports: ✗ Government spending: ✗
- There is evidence that decreases in consumption and investment played an important role
- The evidence for net exports and government spending playing a direct role is more limited, although these policy choices probably exacerbated the crisis after 1930

- Monetary explanations

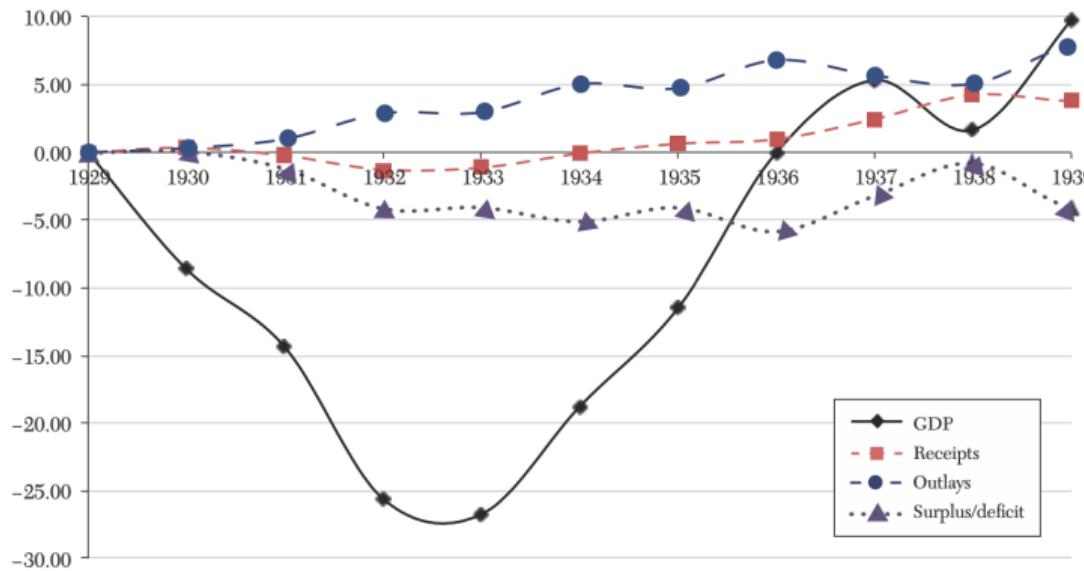
- Monetary shocks: ✓ Bank runs: ✓ Federal Reserve policy: ✓
- Monetary shocks were large and negatively affected balance sheets of households and firms
- Runs, failures, and suspensions decreased confidence in the banking system and helped propagate monetary shocks throughout the financial and real economy
- Federal Reserve policy was bad, but possibly explained by goal of defending gold standard

Questions about the **US economy in the 1930s**

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The **government response** to the Great Depression

- Following the economic downturn, especially with the election of Franklin D. Roosevelt in 1932, the federal government undertook the largest peacetime increase government intervention in the economy in US history



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- Following the economic downturn, especially with the election of Franklin D. Roosevelt in 1932, the federal government undertook the largest peacetime increase government intervention in the economy in US history
- During the 1930s, New Deal policies took a variety of actions:
 - address problems of unemployment and poverty
 - establish the farm grant and loan programs
 - subsidize households and businesses with low-interest or guaranteed loans
 - regulate the financial sector and provide old-age insurance
 - strengthen unions and establish a minimum wage

An overview of New Deal programs

Program	Description	Percentage of total grants, fiscal years 1934–40
Total grants	\$34.5 billion in nominal dollars; roughly \$586.5 billion in 2013 dollars.	
<i>Relief grants</i>		
Federal Emergency Relief Administration (FERA)	Provided direct and work relief payments based on gaps between household income and an income maintenance budget. Hourly work relief payments about half of payments under PWA. July 1933 through June 1935 with a phase out period to March 1937. Work relief that paid similar wages to Public Works Administration from November 1933 through March 1934.	47.9 8.9
Civil Works Administration (CWA)		2.3
Work Projects Administration (WPA)	Provided work relief with limits on monthly hours and hourly wage payments of roughly half of Public Works Administration payments. Started in July 1935.	24.3
Social Security Administration Public Assistance (SSAPA)	Matching grants to states to help fund public-assistance payments for aid to dependent children, old age assistance, and aid to the blind. Testing of first payments based on when states passed enabling legislation after national law passed in 1935.	3.3
Civilian Conservation Corps (CCC)	Work for young men, who were often moved to other states to work on various projects. Paid \$1 per day with most of pay sent to parents. July 1933 through the 1930s. About 1 percent went to small to CCC for Native Americans.	6.8
<i>Veterans' grants</i>		
Veterans' Administration (VA)	Provided a wide array of pensions, disability payments, provision of housing and medical care, and life insurance payments. Preceded New Deal.	20.9 10.5
Veterans' Bonus Payments for Adjusted Service Certificates (ASCC)	Payments in cash or repayments of loans based on World War I Adjusted Service Certificates beginning in June 1936.	10.1
<i>Public works grants</i>		
Public Roads Administration (PRA)	Provided grants for highway building and took over control of prior highway matching grant programs. Started in June 1933.	17.5 4.7
Public Works Administration, Nonfederal (PWANF)	Provided grants to build public works to subnational governments for projects specific to their area. Started in June 1933.	3.8
Public Works Administration, Federal (PWAF)	Built national public-works projects. Started in June 1933.	2.1
Housing Public Works Administration (PWAH)	Grants to build low-income housing projects. June 1933 through 1938 with phasout afterward.	0.4
Public Buildings Administration (PBA)	Grants for building federal buildings. Formal agency created in 1933.	0.8
Bureau of Reclamation (BR)	Provided long-term no-interest loans for irrigation works. Repayments delayed enough many treat them as grants rather than loans. Preceded New Deal.	1.1
Rivers and Harbors under Army Corps of Engineers (ACE)	Built and maintained projects to control floods and aid navigation and use of rivers and harbors. Preceded New Deal.	4.0
Tennessee Valley Authority (TVA)	Corporation created to build and then operate dams for flood control and electricity. By late 1900s became a retailer of electricity to houses and businesses. Created in 1933 but given control of Wilson Dam, which had been built in 1920s.	0.7
Miscellaneous	Includes maintenance of forests, building forest roads, aid to hydroelectric power, and wildlife restoration.	0.3
<i>Farm grants</i>		
Agricultural Adjustment Act (AAA)	Payments to farmers to reduce acreage from production and raise prices in 1933. Started in July 1933. After declared unconstitutional in 1935 was reenacted as means to conserve on soil and prevent erosion.	12.4 10.7
Farm Security Administration (PSA)	Payments to help low-income farmers and tenants. Took over some of responsibilities of FERA. Began in fiscal 1935.	0.9

Program	Description	Percentage of total grants, fiscal years 1934–40
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Home Owners' Loan Corporation (HOLC)	Purchase of nonfarm mortgages from lenders that were in trouble through no fault of the homeowner. The loans were then refinanced at better terms. Loans made from late 1933 through early 1935. The HOLC also made loans and investments to Savings and Loans, which accounted for 7.8 percent of its activity.	26.1
Reconstruction Finance Corporation (RFC)	Made loans to banks, industry, local governments for relief, and to help many New Deal and later war programs in their early stages. Started in February 1932.	21.4
Commodity Credit Corporation (CCC)	Nonrecourse loans for farmers in which farmer repaid the loan in cash when price exceeded a reserve level or repaid the loan with the crop when the market price was below. Started in 1933.	12.6
Public Works Administration (PWA)	Loans to help subnational governments build local public works. Usually tied to PWA nonfederal grants as part of a package. Started in fiscal 1933.	3.9
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Public Roads Administration (PRA)	Provided grants for highway building and took over control of prior highway matching grant programs. Started in June 1933.	4.7
Public Works Administration, Nonfederal (PWANF)	Provided grants to build public-works to educational governments for projects specific to their area. Started in June 1933.	3.8
Public Works Administration, Federal (PWAF)	Built national public-works projects. Started in June 1933.	2.1
Housing, Public Works Administration (PWAH)	Grants to build low-income housing projects, June 1933 through 1938 with phantom afterward.	0.4
Public Buildings Administration (PBA)	Grants for building federal buildings. Formal agency created in 1933.	0.8
Bureau of Reclamation (BR)	Provided long-term no-interest loans for irrigation works. Repayments delayed enough many treat them as grants rather than loans. Preceded New Deal.	1.1
Rivers and Harbors under Army Corps of Engineers (ACE)	Built and maintained projects to control floods and aid navigation and use of rivers and harbors. Preceded New Deal.	4.0
Tennessee Valley Authority (TVA)	Corporation created to build and then operate dams for flood control and electricity. By late 1930s became a retailer of electricity to homes and businesses. Created in 1933 but given control of Wilson Dam, which had been built in 1920s.	0.7
Miscellaneous	Includes maintenance of forest, building forest roads, aid to hydroelectric power, and wildlife restoration.	0.3
Farm grants		12.4
Agricultural Adjustment Act (AAA)	Payments to farmers to reduce acreage from production and raise prices in 1933. Started in July 1933. After declared unconstitutional in 1936 was reenacted as means to conserve on soil and prevent erosion.	10.7
Farm Security Administration (FSA)	Payments to help low-income farmers and tenants. Took over some of responsibilities of FERA. Began in fiscal 1935.	0.9

Program	Description	Percentage of total grants, fiscal years 1934–40
Loans total	\$13.1 Billion in nominal dollars, roughly 222.7 billion in year 2013 dollars.	
Farm Credit Administration (FCA)	Programs for loans for mortgages, production credit, emergency crop and seed loans, and farm owner relief. Started in July 1933 and took over administration of earlier programs. The latter programs included seed money for Federal Land Banks to offer mortgages through associations of farmers, emergency crop and feed loans provided on an ad hoc basis by Congress.	29.5
Home Owners' Loan Corporation (HOLC)	Purchase of nonfarm mortgages from lenders that were in trouble through no fault of the borrower. The loans were then refinanced at better terms. Loans made from late 1933 through early 1935. The HOLC also made loans and investments to Savings and Loans, which accounted for 7.5 percent of its activity.	26.1
Reconstruction Finance Corporation (RFC)	Made loans to banks, industry, local governments for relief, and to help many New Deal and later war programs in their early stages. Started in February 1932.	21.4
Commodity Credit Corporation (CCC)	Nonrecourse loans for farmers in which farmer repaid the loan in cash when price exceeded a reserve level or repaid the loan with the crop when the market price was below. Started in 1933.	12.6
Public Works Administration (PWA)	Loans to help educational governments build local public works. Usually tied to PWA nonfederal grants as part of a package. Started in fiscal 1933.	3.9
Farm Security Administration (FSAL)	Loan programs for low-income farmers, started in fiscal 1936.	2.6
Rural Electrification Administration (REA)	Loans to cooperatives to bring electric power lines to farms, started in 1935.	0.9

Relief grants account for nearly 50 percent of total spending

An overview of **New Deal** programs

Program	Description	Percentage of total grants, fiscal years 1934–40
Total grants	\$34.5 billion in nominal dollars; roughly \$586.5 billion in 2013 dollars.	
Relief grants		
Federal Emergency Relief Administration (FERA)	Provided direct and work relief payments based on gaps between household income and an income maintenance budget. Hourly work relief payments about half of payments under PWA. July 1933 through June 1935 with a phase out period to March 1937. Work relief that paid similar wages to Public Works Administration from November 1933 through March 1934.	47.9 8.9
Civil Works Administration (CWA)		2.3
Work Projects Administration (WPA)	Provided work relief with limits on monthly hours and hourly wage payments of roughly half of Public Works Administration payments. Started in July 1935.	24.3
Social Security Administration Public Assistance (SSAPA)	Matching grants to states to help fund public-assistance payments for aid to dependent children, old age assistance, and aid to the blind. Timing of first payments based on when states passed enabling legislation after national law passed in 1935.	3.3
Civilian Conservation Corps (CCC)	Work relief for young men, who were often moved to other states to work on various projects. Paid \$1 per day with most of pay sent to parents. July 1933 through the 1900s. About 1 percent went to small to CCC for Native Americans.	6.8
Veterans' grants		20.9
Veterans' Administration (VA)	Provided a wide array of pensions, disability payments, provision of housing and medical care, and life insurance payments. Preceded New Deal.	10.5
Veterans' Bonus Payments for Adjusted Service Certificates (ASCC)	Payments in cash or repayments of loans based on World War I Adjusted Service Certificates beginning in June 1936.	10.1
Public works grants		27.5
Public Roads Administration (PRA)	Provided grants for highway building and took over control of prior highway matching grant programs. Started in June 1933.	4.7
Public Works Administration, Nonfederal (PWANF)	Provided grants to build public-works to educational governments for projects specific to their area. Started in June 1933.	3.8
Public Works Administration, Federal (PWAF)	Built national public-works projects. Started in June 1933.	2.1
Housing, Public Works Administration (PWHA)	Grants to build low-income housing projects, June 1933 through 1938 with phantom afterward.	0.4
Public Buildings Administration (PBA)	Grants for building federal buildings. Formal agency created in 1933.	0.8
Bureau of Reclamation (BR)	Provided long-term no-interest loans for irrigation works. Repayments delayed enough many treat them as grants rather than loans. Preceded New Deal.	1.1
Rivers and Harbors under Army Corps of Engineers (ACE)	Built and maintained projects to control floods and aid navigation and use of rivers and harbors. Preceded New Deal.	4.0
Tennessee Valley Authority (TVA)	Corporation created to build and then operate dams for flood control and electricity. By late 1900s became a retailer of electricity to houses and businesses. Created in 1933 but given control of Wilson Dam, which had been built in 1920s.	0.7
Miscellaneous	Includes maintenance of forest, building forest roads, aid to hydroelectric power, and wildlife restoration.	0.3
Farm grants		12.4
Agricultural Adjustment Act (AAA)	Payments to farmers to reduce acreage from production and raise prices in 1933. Started in July 1933. After declared unconstitutional in 1935 was reenacted as means to conserve on soil and prevent erosion.	10.7
Farm Security Administration (FSA)	Payments to help low-income farmers and tenants. Took over some of responsibilities of FERA. Began in fiscal 1935.	0.9

Program	Description	Percentage of total grants, fiscal years 1934–40
Loans total	\$13.1 Billion in nominal dollars, roughly 222.7 billion in year 2013 dollars.	
Farm Credit Administration (FCA)	Programs for loans for mortgages, production credit, emergency crop and seed loans, and farm owner relief. Started in July 1933 and took over administration of earlier programs. The later programs included seed money for Federal Land Banks to offer mortgages through associations of farmers, emergency crop and feed loans provided on an ad hoc basis by Congress.	29.5
Home Owners' Loan Corporation (HOLC)	Purchase of nonfarm mortgages from lenders that were in trouble through no fault of the borrower. The loans were then refinanced at better terms. Loans made from late 1933 through early 1935. The HOLC also made loans and investments to Savings and Loans, which accounted for 7.5 percent of its activity.	26.1
Reconstruction Finance Corporation (RFC)	Made loans to banks, industry, local governments for relief, and to help many New Deal and later war programs in their early stages. Started in February 1932.	21.4
Commodity Credit Corporation (CCC)	Nonrecourse loans for farmers in which farmer repaid the loan in cash when price exceeded a reserve level or repaid the loan with the crop when the market price was below. Started in 1933.	12.6
Public Works Administration (PWA)	Loans to help subnational governments build local public works. Usually tied to PWA nonfederal grants as part of a package. Started in fiscal 1933.	3.9
Farm Security Administration (FSAL)	Loan programs for low-income farmers, started in fiscal 1936.	2.6
Rural Electrification Administration (REA)	Loans to cooperatives to bring electric power lines to farms, started in 1935.	0.9

Veterans' grants account for 21 percent of total spending



An overview of **New Deal** programs

Program	Description	Percentage of total grants, fiscal years 1934–40	Program	Description	Percentage of total grants, fiscal years 1934–40
Total grants	\$34.5 billion in nominal dollars; roughly \$586.5 billion in 2013 dollars.		Total loans	\$13.1 Billion in nominal dollars, roughly 222.7 billion in year 2013 dollars.	Percentage of total loans, fiscal years 1934–39
<i>Relief grants</i>			Farm Credit Administration (FCA)	Programs for loans for mortgages, production credit, emergency crop and seed relief, and farm-delinquency relief. Started in July 1933 and took over administration of earlier programs. The programs included seed money for Federal Land Banks to offer mortgages through associations of farmers, emergency crop and feed loans provided on an ad hoc basis by Congress.	29.5
Federal Emergency Relief Administration (FERA)	Provided direct and work relief payments based on gaps between household income and an income maintenance budget. Hourly work relief payments about half of payments under PWA. July 1933 through June 1935 with a phase out period to March 1937. Work relief that paid similar wages to Public Works Administration from November 1933 through March 1934.	47.9	Home Owners' Loan Corporation (HOLC)	Purchase of nonfarm mortgages from lenders that were in trouble through no fault of the borrower. The loans were then refinanced at better terms. Loans made from late 1933 through early 1935. The HOLC also made loans and investments to Savings and Loans, which accounted for 7.5 percent of its activity.	26.1
Civil Works Administration (CWA)	Work relief with limits on monthly hours and hourly wage payments of roughly half of Public Works Administration payments. Started in July 1935.	2.3	Reconstruction Finance Corporation (RFC)	Made loans to banks, industry, local governments for relief, and to help many New Deal and later war programs in their early stages. Started in February 1933.	21.4
Work Projects Administration (WPA)	Provided work relief with limits on monthly hours and hourly wage payments of roughly half of Public Works Administration payments. Started in July 1935.	24.3	Commodity Credit Corporation (CCC)	Nonrecourse loans for farmers in which farmer repaid the loan in cash when price exceeded a reserve level or repaid the loan with the crop when the market price was below. Started in 1933.	12.6
Social Security Administration Public Assistance (SSAPA)	Matching grants to states to help fund public-assistance payments for aid to dependent children, old age assistance, and aid to the blind. Testing of first payments based on when states passed enabling legislation after national law passed in 1935.	3.3	Public Works Administration (PWA)	Loans to help subnational governments build local public works. Usually tied to PWA nonfederal grants as part of a package. Started in 1933.	3.9
Civilian Conservation Corps (CCC)	Work relief for young men, who were often moved to other states to work on various projects. Paid \$1 per day with most of pay sent to parents. July 1933 through the 1960s. About 1 percent went to small to CCC for Native Americans.	6.8	Farm Security Administration (FSA)	Loan programs for low-income farmers, started in fiscal 1936.	2.6
Veterans' grants			Rural Electrification Administration (REA)	Loans to cooperatives to bring electric power lines to farms, started in 1935.	0.9
Veterans' Administration (VA)	Provided a wide array of pensions, disability payments, provision of housing and medical care, and life insurance payments. Preceded New Deal.	10.8			
Veterans' Bonus Payments for Adjusted Service Certificates (ASCC)	Payments in cash or repayments of loans based on World War I Adjusted Service Certificates beginning in June 1936.	10.1			
Public works grants					
Public Roads Administration (PRA)	Provided grants for highway building and took over control of prior highway matching grant programs. Started in June 1933.	17.8			
Public Works Administration, Nonfederal (PWANP)	Provided grants to build public-works to subnational governments for projects specific to their area. Started in June 1933.	4.7			
Public Works Administration, Federal (PWAf)	Built national public-works projects. Started in June 1933.	3.8			
Housing, Public Works Administration (PWAH)	Grants to build low-income housing projects. June 1933 through 1935 with phasout afterward.	2.1			
Public Buildings Administration (PBA)	Grants for building federal buildings. Formal agency created in 1933.	0.4			
Bureau of Reclamation (BR)	Provided long-term no-interest loans for irrigation works. Repayments delayed enough many treat them as grants rather than loans. Preceded New Deal.	0.8			
Rivers and Harbors under Army Corps of Engineers (ACE)	Built and maintained projects to control floods and aid navigation and use of rivers and harbors. Preceded New Deal.	1.1			
Tennessee Valley Authority (TVA)	Corporation created to build and then operate dams for flood control and electricity. By late 1930s became a retailer of electricity to houses and businesses. Created in 1933 but given control of Wilson Dam, which had been built in 1920s.	4.0			
Miscellaneous	Includes maintenance of forests, building forest roads, aid to hydroelectric power, and wildlife restoration.	0.7			
<i>Farm grants</i>					
Agricultural Adjustment Act (AAA)	Payments to farmers to remove acreage from production and raise prices in 1933. Started in July 1933. After declared unconstitutional in 1935 was reenacted as means to conserve on soil and prevent erosion.	0.3			
Farm Security Administration (FSA)	Payments to help low-income farmers and tenants. Took over some of responsibilities of FERA. Began in fiscal 1935.	12.4			
		10.7			

Public works grants account for 18 percent of total spending



An overview of **New Deal** programs

Program	Description	Percentage of total grants, fiscal years 1934–40	Program	Description	Percentage of total grants, fiscal years 1934–40
Total grants	\$34.5 billion in nominal dollars; roughly \$586.5 billion in 2013 dollars.		Loans total	\$13.1 billion in nominal dollars, roughly 222.7 billion in 2013.	Percentage of total loans, fiscal years 1934–39
<i>Relief grants</i>			Farm Credit Administration (FCA)	Programs for loans for mortgages, production credit emergency crop and seed loans, and farm owner relief. Started in July 1933 and took over administration of earlier programs. The later programs included seed money for Federal Land Banks to offer mortgages through associations of farmers, emergency crop and feed loans provided on an ad hoc basis by Congress.	29.5
Federal Emergency Relief Administration (FERA)	Provided direct and work relief payments based on gaps between household income and an income maintenance budget. Hourly work relief payments about half of payments under PWA, July 1933 through June 1935 with a phase out period to March 1937. Work relief that paid similar wages to Public Works Administration from November 1933 through March 1934.	47.9 8.9	Home Owners' Loan Corporation (HOLC)	Purchase of nonfarm mortgages from lenders that were in trouble through no fault of the borrower. The loans were then refinanced at better terms. Loans made from late 1933 through early 1935. The HOLC also made loans and investments to Savings and Loans, which accounted for 7.8 percent of its activity.	26.1
Civil Works Administration (CWA)		2.3	Reconstruction Finance Corporation (RFC)	Made loans to banks, industry, local governments for relief, and to help many New Deal and later war programs in their early stages. Started in February 1932.	21.4
Work Projects Administration (WPA)	Provided work relief with limits on monthly hours and hourly wage payments of roughly half of Public Works Administration payments. Started in July 1935.	24.3	Commodity Credit Corporation (CCC)	Nonrecourse loans for farmers in which farmer repaid the loan in cash when price exceeded a reserve level or repaid the loan with the crop when the market price was below. Started in 1933.	12.6
Social Security Administration Public Assistance (SSAPA)	Matching grants to states to help fund public-assistance payments for aid to dependent children, old age assistance, and aid to the blind. Timing of first payments based on when states passed enabling legislation after national law passed in 1935.	3.3	Public Works Administration (PWA)	Loans to help subnational governments build local public works. Usually tied to PWA nonfederal grants as part of a package. Started in fiscal 1933.	3.9
Civilian Conservation Corps (CCC)	Work relief for young men, who often moved to other states to work on various projects. Paid \$1 per day with most of pay sent to parents. July 1933 through the 1930s. About 1 percent went to CCC for Native Americans.	6.8	Farm Security Administration (FSA)	Loan programs for low-income farmers, started in fiscal 1936.	2.6
Veterans' grants			Rural Electrification Administration (REA)	Loans to cooperatives to bring electric power lines to farms, started in 1935.	0.9
Veterans' Administration (VA)	Provided a wide array of pensions, disability payments, provision of housing and medical care, and life insurance payments. Preceded New Deal.	20.9 10.5			
Veterans' Bonus Payments for Adjusted Service Certificates (ASCC)	Payments in cash or repayments of loans based on World War I Adjusted Service Certificates beginning in June 1936.	10.1			
Public works grants					
Public Roads Administration (PRA)	Provided grants for highway building and took over control of prior highway matching grant programs. Started in June 1933.	17.5 4.7			
Public Works Administration, Nonfederal (PWANF)	Provided grants to build public works to subnational governments for projects specific to their area. Started in June 1933.	3.8			
Public Works Administration, Federal (PWAF)	Built national public-works projects. Started in June 1933.	2.1			
Housing, Public Works Administration (PWAH)	Grants to build low-income housing projects, June 1933 through 1938 with phantom afterward.	0.4			
Public Buildings Administration (PBA)	Grants for building federal buildings. Formal agency created in 1933.	0.8			
Bureau of Reclamation (BR)	Provided long-term no-interest loans for irrigation works. Repayments delayed enough many treat them as grants rather than loans. Preceded New Deal.	1.1			
Rivers and Harbors under Army Corps of Engineers (ACE)	Built and maintained projects to control floods and aid navigation and use of rivers and harbors. Preceded New Deal.	4.0			
Tennessee Valley Authority (TVA)	Corporation created to build and then operate dams for flood control and electricity. By late 1930s became a retailer of electricity to houses and businesses. Created in 1933 but given control of Wilson Dam, which had been built in 1920s.	0.7			
Miscellaneous	Includes maintenance of forest, building forest roads, aid to hydroelectric power, and wildlife restoration.	0.3			
<i>Farm grants</i>					
Agricultural Adjustment Act (AAA)	Payments to farmers to encourage farms production and raise prices in 1933. Started in July 1933. After declared unconstitutional in 1935 was reenacted as means to conserve on soil and prevent erosion.	12.4 10.7			
Farm Security Administration (FSA)	Payments to help low-income farmers and tenants. Took over some of responsibilities of FERA. Began in fiscal 1935.	0.9			

Farm grants account for 12 percent of total spending



An overview of **New Deal** programs

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Total grants	\$34.5 billion in nominal dollars; roughly \$586.5 billion in 2013 dollars.	
Relief grants		
Federal Emergency Relief Administration (FERA)	Provided direct and work relief payments based on gaps between household income and an income maintenance budget. Hourly work relief payments about half of payments under PWA. July 1933 through June 1935 with a phase out period to March 1937. Work relief that paid similar wages to Public Works Administration from November 1933 through March 1934.	47.9 8.9
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Veterans' grants		
Veterans' Administration (VA)	Provided a wide array of pensions, disability payments, provision of housing and medical care, and life insurance payments. Preceded New Deal.	20.9 10.5
Veterans' Bonus Payments for Adjusted Service Certificates (ASCC)	Payments in cash or repayments of loans based on World War I Adjusted Service Certificates beginning in June 1936.	10.1
Public works grants		
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Farm grants		
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Farm Security Administration (PSA)	Payments to help low-income farmers and tenants. Took over some of responsibilities of FERA. Began in fiscal 1935.	0.9

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Public Works Administration (PWA)	Loans to help subnational governments build local public works. Usually tied to PWA nonfederal grants as part of a package. Started in fiscal 1933.	3.9
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Rural Electrification Administration (REA)	Loans to cooperatives to bring electric power lines to farms, started in 1935.	0.9

Loans to farmers, businesses, and homeowners were sizeable



The effect of the New Deal

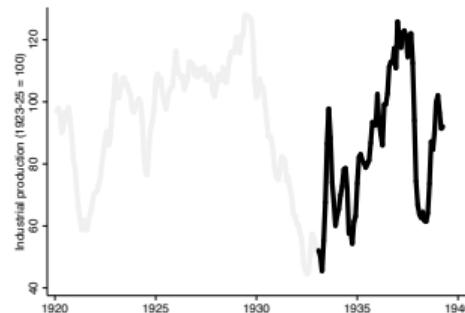
- **Public works and relief grants:**
 - increased income with a multiplier of around one
 - increased durable goods consumption
 - reduced mortality and crime rates
- **Farm grants** incentivized farmers to take land out of production and helped farmers receiving the payments, likely did not help non-owners
- The **mortgage purchase and refinance program** kept a large share of people in their homes, bailed out mortgage lenders
- The provision of **financing** stimulated activity in banking but prevented the maintenance and rebuilding of capital in railroads

Questions about the **US economy in the 1930s**

- ▷ What caused the Great Depression?
- ▷ What was the government response to the Great Depression?
- When and why did the economy **recover** from the Great Depression?
- ▷ Why did the Great Depression last so long?
- ▷ What were the lasting effects of the Great Depression?

Recovery from the Great Depression

- Recovery from the Great Depression lasted a long time and did not come with the New Deal, based on the **stock market**, **employment**, or **industrial production**



- Importantly, aggregate economic data mask heterogeneity in the Great Depression by **geography**, **occupation**, **skill**, etc—recovery was long and longer still for some groups!

Recovery from the Great Depression

- **Fiscal policy:**
 - Federal fiscal policy was expansionary from 1933 onward, but this was partially offset by contractionary policies at the state and local levels
- **Monetary policy:**
 - stability was restored to the banking system and the money supply started to grow
- **The international financial system:**
 - currency depreciation starting in the early 1930s benefited the initiating countries and would have been better if they had been more widespread and coordinated
 - beginning with the UK going off the gold standard in 1931 and the United States doing the same in 1933 (by an executive order issued by FDR)

Recovery from the Great Depression

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- Monetary policy: ✓
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Questions about the **US economy in the 1930s**

- ▷ What caused the Great Depression?
- ▷ What was the government response to the Great Depression?
- ▷ When and why did the economy recover from the Great Depression?
- Why did the Great Depression **last so long?**
- ▷ What were the lasting effects of the Great Depression?

The **length** of the Great Depression

- **Sticky wage theory:** monetary contraction and nominal wage rigidity decrease output
- **Cartelization theory:** cartelization and unionization decrease labor market efficiency
 - wedge between marginal rate of substitution and marginal product of labor
- **Investment friction theory:** monetary contraction increases capital market frictions and decreases investment (and output)
 - wedge between intertemporal marginal rate of substitution and marginal product of capital
- Different types of economists place more or less emphasis on these different explanations

Questions about the **US economy in the 1930s**

- ▷ What caused the Great Depression?
- ▷ What was the government response to the Great Depression?
- ▷ When and why did the economy recover from the Great Depression?
- ▷ Why did the Great Depression last so long?
- What were the **lasting effects** of the Great Depression?

The **lasting effects** of the Great Depression

- Taking a step back, the 1930s were most technologically progressive decade of 20thC

	TFP	Output/Hour
1901–1919	1.08	1.71
1919–1929	2.02	2.27
1929–1941	2.31	2.35
1941–1948	1.29	1.71
1948–1973	1.90	2.88
1973–1989	0.34	1.34
1989–2000	0.78	1.92

The **lasting effects** of the Great Depression

- Taking a step back, the 1930s were **most technologically progressive decade of 20thC**
 - labor productivity increased 2.35% per year

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- Taking a step back, the 1930s were **most technologically progressive decade of 20thC**
 - labor productivity increased 2.35% per year
- More strikingly, the **efficiency of the entire economy**—not just labor productivity—increased
 - total factor productivity increased by 2.31%

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The **lasting effects** of the Great Depression

- Taking a step back, the 1930s were **most technologically progressive decade of 20thC**
 - labor productivity increased 2.35% per year
- More strikingly, the **efficiency of the entire economy**—not just labor productivity—increased
 - total factor productivity increased by 2.31%
- Gains occurred in several areas
 - chemical processes, e.g., sugar, mining
 - thermal efficiency, e.g., electricity
 - conveyor belts and factory layouts
 - materials, e.g., plastics, metal, wood

	TFP	Output/Hour
1901–1919	1.08	1.71
1919–1929	2.02	2.27
1929–1941	2.31	2.35
1941–1948	1.29	1.71
1948–1973	1.90	2.88
1973–1989	0.34	1.34
1989–2000	0.78	1.92

The **lasting effects** of the Great Depression

- Taking a step back, the 1930s were **most technologically progressive decade of 20thC**
 - labor productivity increased 2.35% per year
- More strikingly, the **efficiency of the entire economy**—not just labor productivity—increased
 - total factor productivity increased by 2.31%
- Gains occurred in several areas
 - chemical processes, e.g., sugar, mining
 - thermal efficiency, e.g., electricity
 - **conveyor belts** and **factory layouts**
 - materials, e.g., plastics, metal, wood



The **lasting effects** of the Great Depression

- Going forward, technological progress during the 1930s laid the foundation for the postwar Golden Age—this is the argument of the economist [Alexander Field](#)
 - A few general explanations for technological progress include: capital investment, disembodied technical change, structural change, and general-purpose technology
- The New Deal (and subsequently mobilization for World War II) permanently changed the role of government in the economy and in American society
 - The economist [John Wallis](#) documents the growth of federal government at expense of local governments, emphasizes greater “capacity” of federal government
 - The economist [Robert Higgs](#) focuses on the increasing size and regulatory oversight exercised by federal authorities, emphasizes “public choice” problems
 - A few general explanations for the government growth include: modernization, public goods, the welfare state, political and economic redistribution, ideology, and crisis

Summing up the 1930s

- The Great Depression was likely the **caused** by the interaction between consumption and investment downturns and trouble in the financial system
- As a **response**, the New Deal did not obviously speed recovery—recovery took a long time!—but did ameliorate some of the worst suffering and its legacy continues to today
- The economy **recovered** when the banking sector was stabilized and monetary policy turned expansionary, aided by the United States going off the gold standard
- And **technological changes** that occurred during the 1930s laid the foundation for many of the subsequent advances in the US economy, particularly in the postwar Golden Age
- Next, we'll turn to the 1940s and mobilization for **World War II** in the United States