Hi-story lessons.

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24.10.1929

24 October: beginning of the Great Crisis

The great economic crisis was the deepest ever collapse of production and resulted in mass unemployment in most highly developed countries across the globe, particularly in the U.S. and Germany.

Following the period of post-war devastation and inflationary perturbations, the second half of the twenties brought prosperity to the free market. The developed countries of the west repaired their war damaged cities and balanced the economy, while international commerce grew at a swift pace. There was an air of optimism among entrepreneurs. Many respected economists predicted a long-term boom. However, international trade was burdened by a payment imbalance of the main players, and within many of them, particularly in the United States and Germany, there was a dangerous and growing disproportion between the power of monopolies and the weakness of millions of small producers. Optimism of investors was often expressed in stock market speculation with borrowed money, which spelled catastrophe.

On this background, the crash that began in 1929 was particularly shocking. The first symptoms occurred in the stock market. The "Black Thursday" of 24 October 1929 on the New York Stock Exchange brought a huge drop in the stock prices of a great number of companies. Their owners were selling in a panic, magnifying the drop and chaos. Bankruptcies were on the rise and so were cases of owners' suicides. Stock market crisis and reduction of buying power caused the industry to react by limiting production and employment. Unemployment was rising rapidly, which in turn caused reduction in consumer demand, halting of investments and deepening of the crisis. Monopolies maintained prices, but had to limit the scale of production. In agriculture, the crisis impacted not so much production, but prices. Millions of producers were not able to affect the prices, so they increased the supply. This caused a phenomenon known as price scissors, meaning that the drop in the prices of agricultural products was much deeper than industrial products. This divergence led to pauperisation of farmers. At the same time, countries were trying to increase exports, but by limiting imports the overall trade slowed. The economic crisis worsened the state of democracy and increased the numbers of supporters of extreme political solutions – fascism, Nazism, communism or various forms of authoritarianism.

Until the great crisis, the economies of highly developed countries were dominated by free market or monopolistic capitalism. With the exception of the First World War period, government played a limited role in the economy. That role was most significant in Russia and Germany, but in the United States, for example, government almost never acted as a business entity. The great crisis and efforts to overcome it gave birth to a period of state interventionism. The author of the first developed theory of interventionism was a British economist John Maynard Keynes. Indirect forms of interventionism include policy on currency exchange rates, bank interest rates and tax rates, while direct forms are unemployment compensation, public works projects, credit and government orders. The most direct form of government's intervening in the economy was taking over corporations to save them from collapse, known as statism.

Different types of intervention were used in many countries. Generally, two types of intervention policy are recognised. One of them was used in the United States, where from March 1933 Franklin D. Roosevelt's government implemented a crisis mitigation program called "The New Deal". Created by Roosevelt team of advisers called "Brain Trust" postulated that the goal of crisis management policy ought to be increasing consumer demand by creating public works projects and paying unemployment benefits. Funding for the New Deal was to come from progressive taxation. Another source was the devaluation of the U.S. Dollar, which revitalised exports and activated the money supply kept in banks. Roosevelt's policy included an encouragement for businesses to institute minimum wage, which made it very popular. The government also intervened in the agricultural market, buying some crops directly from farmers and paying them compensation for limiting production. Surplus crops were sometime destroyed. The government also supported price dumping, which meant artificial lowering of export prices and equalising losses by government subsidies or by raising prices on the domestic market.

Interventionism in Germany took a different form. Here, the government sought to increase demand for industrial production by placing orders for armaments. This was part of Nazi policy, which aimed at rebuilding Germany's military might while improving the economy and gaining mass public support. The Nazis also implemented public works and economic planning in a four-year cycle. Similar to Italy, the Third Reich implemented corporate style of economic governance, which maintained private ownership while the interests of various industries and trade groups were centrally coordinated by the party and the government. Both Germany and Italy, which suffered from sanctions imposed upon them by the League of Nations, as a consequence of their conquest of Ethiopia, strived for economic self-sufficiency.

As a result of the above interventionist activities, as well as other organic mechanisms for rebuilding the economy (reducing costs, organisational changes, innovation), the crisis began to lessen in 1933 and by 1935-1937 the economy of most developed countries exceeded the pre-crisis levels. This, however, was a whole new phase, in which government intervention became an integral part of capitalist economy.

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References: