

Causes of the Great Depression

Unit 4

Objective & Agenda for 11/20/15

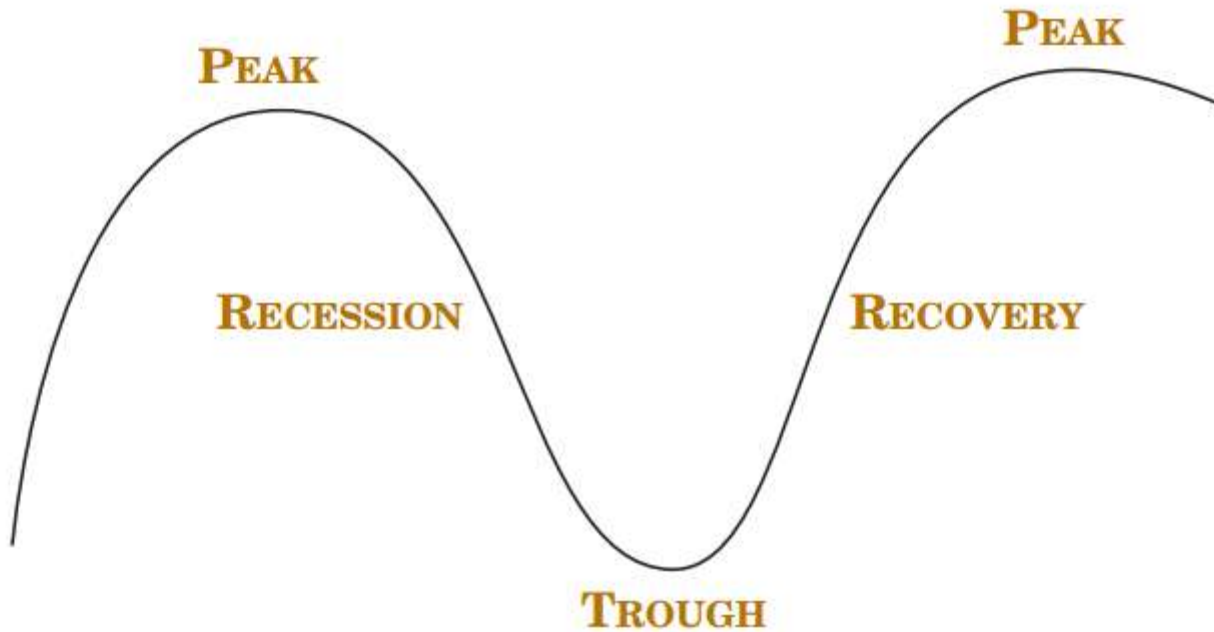
Objective

- SWBAT analyze how the actions and policies of the US Government contributed to the Great Depression

Agenda

- Do Now
- Notes on the Causes
 - Occupations Activity
- What Would You Do Discussion?
- "BUST"
 - Video: America the Story of US
 - Discussion Questions

What is a Business Cycle?



- *Demand for durable goods falls*
- *Demand for investment goods falls*
- *Workers who make those goods are laid off*
- *Because these workers now have less income, they spend less- and demand falls further*
- *Demand for durable goods revives*
- *Demand for investment goods revives*
- *Workers are rehired*

Except...

- In the 1920s the demand continued to fall, business activities continued to decline and unemployment rates continued to rise.

Bank Failures

- Federal Reserve System had been established in 1913, to prevent bank failures by lending reserves to banks that were experiencing unusually high cash withdrawals.
- On the eve of the Depression, the first concern of the 12 regional Federal Reserve banks should have been the overall health of the financial system.
 - But the regional presidents, formerly commercial bankers hesitated to lend to banks in their districts that they considered unsound.
 - As a result, many banks were allowed to fail, and the failures caused fear among account holders in sound banks, prompting them to panic and withdraw their funds.

Bank Failures continued...

- The Federal Reserve System raised interest rates in late 1931:
 - Discouraged business borrowing
 - Contracted the money supply
- Banks kept some of their reserves in the form of bonds
 - When interest rates rise, the prices of bonds fell
 - Banks then held assets that have declined in value, yielding less revenue when banks sell them to raise funds to pay depositors.
- The problem the Federal Reserve Banks faced is that they were obliged to follow the rules of the gold standard
 - Gold began to flow out of the US as a result of financial instability in foreign countries, and the reserve banks raised the interest rates that their member banks had to pay to borrow reserves
 - Encouraged foreign governments and individuals to buy American bonds, rather than exchanging their dollars for American gold
 - Raised interest rates throughout the economy, which discouraged spending by American businesses.

US Prosperity in the 1920s

- US Prosperity in the 1920s was based on the sale of house and automobiles
- Consumers for the first time could buy houses and cars on the installment plan- this led to job growth
 - Jobs for workers who built homes and cars
 - Jobs for workers who built the furniture and appliances that went into new homes
 - Jobs for workers who produced the steel and other materials that were used to produce cars.
 - Jobs for business firms who built new plants and bought new equipment to produce what consumers wanted
 - Jobs for workers who built and paved roads for the new automobiles
 - Jobs for workers in electric plants and water and sewage facilities to service the new households
- The prosperity of workers in all these industries allowed them to spend a lot of money, thus providing income to other workers—income which they in turn spent to buy other goods and services.
 - Economists call the spread of such new spending a *multiplier effect*
 - One person's spending becomes income to another person, who in turn can spend more and add to the income of others.

US Prosperity in the 1920s

- Multiplier Effect in Reverse

- US Business activity began to slow down by the late 1920s
- The US economy entered a mild recession
 - Sales of homes and cars began to fall
 - What happened to all of the jobs that were created due to cars and homes?

Direct Causes of the Great Depression

- 1. Stock Market Crash of 1929:
 - Although the workings of the New York Stock Exchange can be quite complex, one simple principle governs the price of stock. When investors believe a stock is a good value they are willing to pay more for a share and its value rises. When traders believe the value of a security will fall, they cannot sell it at as high of a price. If all investors try to sell their shares at once and no one is willing to buy, the value of the market shrinks.
 - On October 24, 1929, "**BLACK THURSDAY**," this massive sell-a-thon began. By the late afternoon, wealthy financiers like J.P. Morgan pooled their resources and began to buy stocks in the hopes of reversing the trend.
 - But the bottom fell out of the market on Tuesday, October 29. A record 16 million shares were exchanged for smaller and smaller values as the day progressed. For some stocks, no buyers could be found at any price. By the end of the day, panic had erupted, and the next few weeks continued the downward spiral. In a matter of ten short weeks the value of the entire market was cut in half. Suicide and despair swept the investing classes of America.



Direct Causes of the Great Depression

NUMBER OF U.S. BANKS CLOSING TEMPORARILY OR PERMANENTLY, 1920-1933

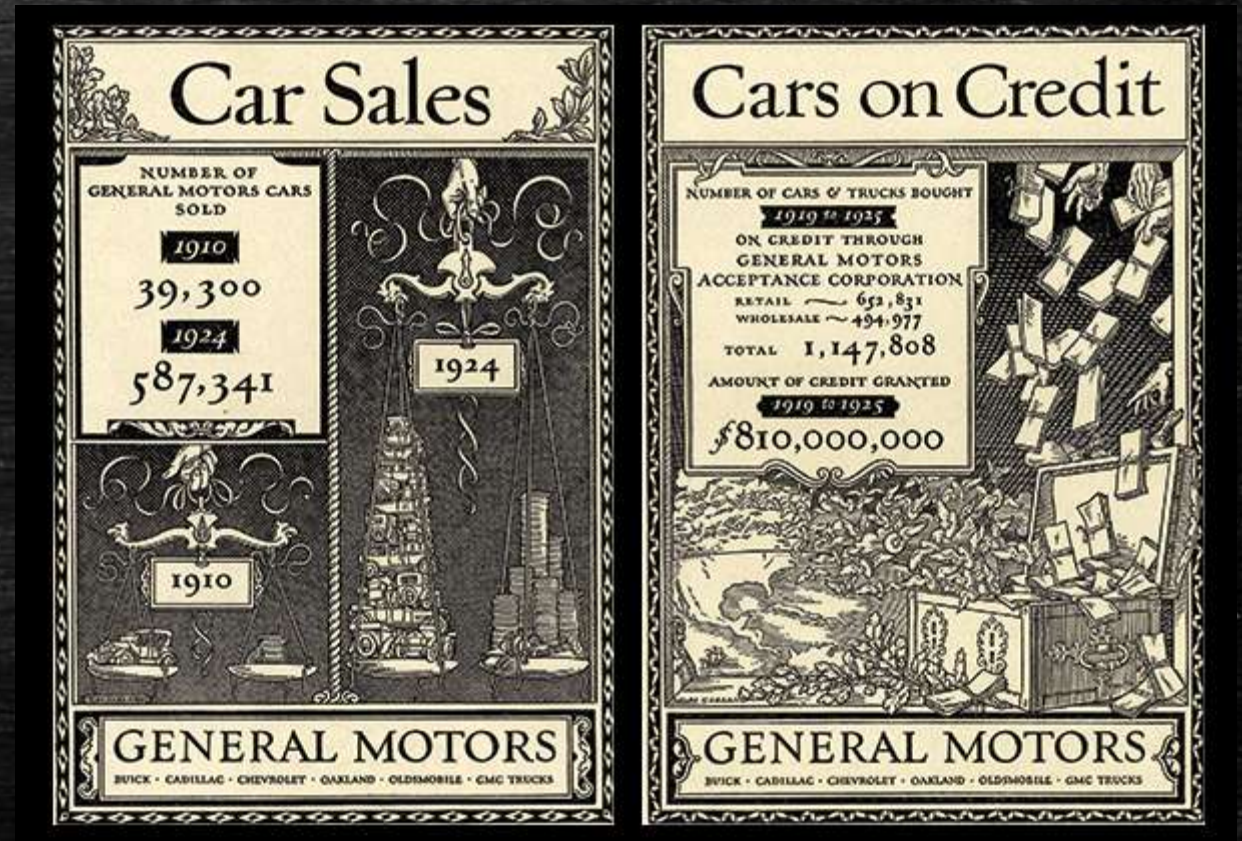
Year	Number of Bank Closings
1920	168
1921	505
1922	367
1923	646
1924	775
1925	618
1926	976
1927	669
1928	499
1929	659
1930	1,352
1931	2,294
1932	1,456
1933	4,004

▪ 2. Bank Failures

- Throughout the 1930s over 9,000 banks failed. Bank deposits were uninsured and thus as banks failed people simply lost their savings. Surviving banks, unsure of the economic situation and concerned for their own survival, stopped being as willing to create new loans. This exacerbated the situation leading to less and less expenditures.

Direct Causes of the Great Depression

- 3. Reduction in Purchasing Across the Board
 - With the stock market crash and the fears of further economic woes, individuals from all classes stopped purchasing items. This then led to a reduction in the number of items produced and thus a reduction in the workforce. As people lost their jobs, they were unable to keep up with paying for items they had bought through installment plans and their items were repossessed. More and more inventory began to accumulate. The unemployment rate rose above 25% which meant, of course, even less spending to help alleviate the economic situation.

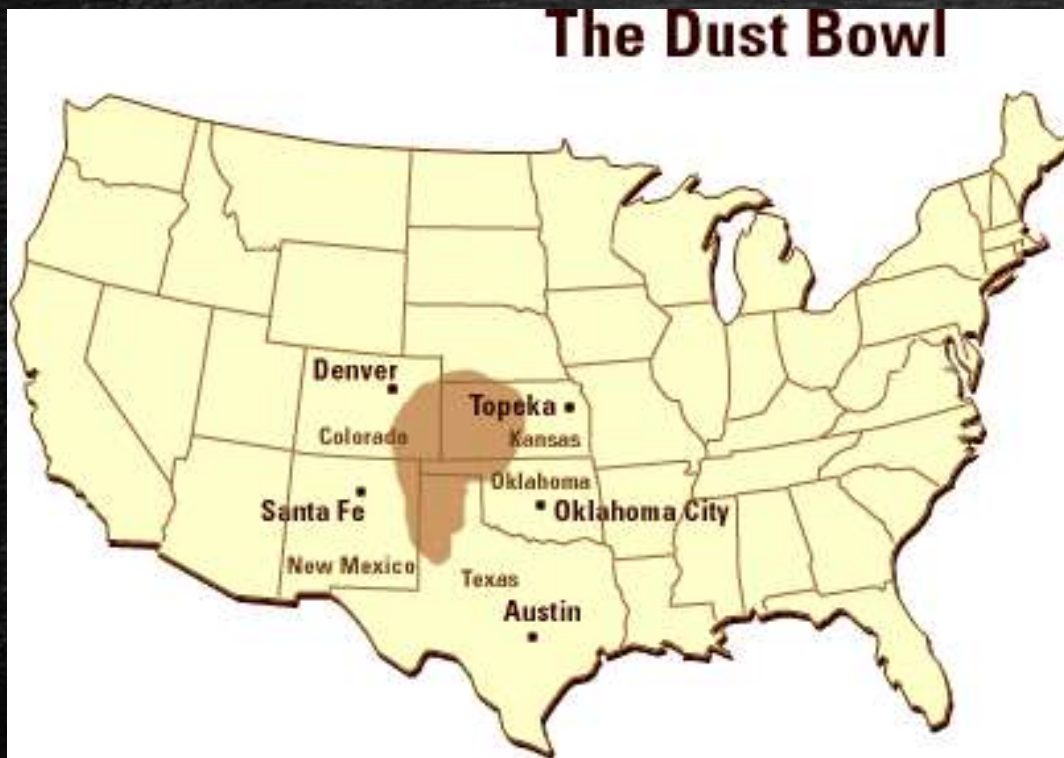


Direct Causes of the Great Depression

- 4. American Economic Policy with Europe
 - As businesses began failing, the government created the Smoot-Hawley Tariff in 1930 to help protect American companies. This charged a high tax for imports thereby leading to less trade between America and foreign countries along with some economic retaliation



Direct Causes of the Great Depression



- 5. Drought Conditions
 - While not a direct cause of the Great Depression, the drought that occurred in the Mississippi Valley in 1930 was of such proportions that many could not even pay their taxes or other debts and had to sell their farms for no profit to themselves. The area was nicknamed "The Dust Bowl." This was the topic of John Steinbeck's *The Grapes of Wrath*.