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# A Deceptive Economy

In 1928, after eight years of conservative Republican leadership, a generally contented American public stayed the course and elected a third such president. Overall, life in the United States had been good for many Americans, as the nation's prosperity hit a stride that many people could not imagine ending. Some had even come to believe that the U.S. economy had fallen into an endless groove of permanent growth. The new president certainly seemed to think so. While still the Republican candidate, Herbert Hoover, who had served the Coolidge administration as secretary of commerce, gave a speech in August touting the great strides already made by a national economy on the rise: "We in America today are nearer to the final triumph over poverty than ever before in the history of any land. The poorhouse is vanishing from among us."

In the fall of 1928 such words seemed to ring true. The 1920s had hummed with growth, expansion, and prosperity.

Consumer confidence had never seemed higher. Throughout the decade, great prosperity had become the watchword.

## BOOM TIME FOR INDUSTRY AND INVESTORS

Economic progress seemed everywhere, as Americans emerged from the self-imposed rationing and sacrifice of World War I and went on a buying spree. Millions of people across the country bought their first everything—their first automobile, washing machine, camera, radio, refrigerator. These products came off America's assembly lines in an endless stream. As early as 1916 the number of cars produced annually in domestic plants topped 1 million. When the decade opened, in 1920, there were more than 8 million cars registered in the United States. By the end of the decade that number had mushroomed to 23 million. America's industrial output knew no bounds. More people were at work in U.S. factories and production plants than ever before, producing more goods than ever before. The U.S. economy was sometimes compared to an economic miracle.

Consumers in the United States were not the only ones to experience good times. U.S. investors had also had a field day. Overseas, U.S. investments nearly doubled from $3.98 billion in 1919 to $7.5 billion by 1929. The New York Stock Exchange, which served for many as the truest indicator of the nation's economic pulse, enjoyed phenomenal growth, especially after 1923. Stock purchases on the Exchange increased four-fold between 1923 and 1930. And stock sales were only outstripped by the rise in stock prices.

Americans had binged on stock investments during the 1920s. Altogether, investment in the stock market and in bonds rose sharper than any other economic indicator during the decade, faster, in fact, than the actual production or sales of manufactured goods.

## Buying on Margin

It is no wonder. During the 1920s a would-be investor could make his or her stock purchases largely on credit. Under the rules in place for the New York Stock Exchange, investors could purchase stock through a practice called "buying on margin." It worked this way: An investor intent on purchasing $1,000 worth of stock at $10 per share could pay his broker (the person through whom the investor made his or her actual stock purchases) just one-tenth of the needed investment capital, or $100. The broker was all too happy to "loan" the investor the other $900, make the $1,000 investment, and wait for the profits to roll in.

With many stocks increasing in value during the 1920s at an average rate of 25 percent annually, that initial investment of $1,000 might have accrued to a value of $1,250 after being invested for a year. Then the investor might order his broker to sell his shares, pay the broker a fee of $100, and pocket the remaining $150, plus the initial investment of $1,000. Through this speculative system, everybody could win. The investor made money, the broker made money, the money invested in the market made someone money, and the economy continued to hum along. Year after year during America's "Roaring Twenties," the gambles paid off. Suddenly regular folks, not just the wealthy, were making money by playing the stock market and each investment seemed to represent a sure thing.

## Soaring Stock Prices

Profits were there for the taking, it seemed. Certainly the New York Stock Exchange reflected this reality. In 1923 the market value of the Exchange's stock stood at $4 billion; it increased to $67 billion in just six years. It was not a flawless system, of course. There were losses on the market prior to 1929. Sometimes a given stock would tumble in value, the broker would have to call in his investment, causing the original investor to cash out short, and resulting in a loss. It was a gamble for the broker, as well. If a stock dropped, he might find himself overextended with “margin” loans to his investment clients, leaving him ruined.

Many were eager to ride the wave, however. Sometimes stock prices soared unbelievably. Take, for example, one company, Radio Corporation of America (RCA), part of an industry that was experiencing true growth at the time. In early 1928—the year of Hoover’s election—RCA stock stood at $85 a share. By March 3 a share was worth $91.50. A week later, on March 10, it was worth $107 when the stock market opened, then closed that day at $120.50. Just two days later it had risen to $138.50. On March 13 it hit $160. By May it had reached the mile marker of $200. By November, with the election of Hoover over Democrat challenger Alfred Smith, RCA stock again doubled to $400, nearly five times its worth less than a year earlier. After a 70-point tumble in December, the stock recovered and began a slower rise, reaching $500 by mid-summer of 1929. At that point each share was split into five shares. Each was worth $101 by early September, and soon reached $114. Within just 18 months RCA stock had increased in value by a whopping 600 percent!

Only the most cautious investor could look at such increases and not be tempted to put money into stocks during the 1920s. The year 1928 presented additional stock miracles, including Chrysler, with a share of its stock increasing from $63 to $132—more than double. But the wave of investment was about to crest, and even collapse.

## CORPORATE PROFITS

What was behind this drive in stock values during the 1920s? One answer is clear—corporate profits. Between 1916 and 1925 the profits gleaned by America’s largest manufacturing companies amounted to an annual average of $730 million. That figure nearly doubled, to $1.4 billion, in the period from 1926 to the latter months of 1929! During 1929 alone corporate profits were actually three times what they had been in 1920. The stock prices simply reflected this ever-increasing level of corporate profit. Just as corporate profits tripled during the 1920s, so stock prices tripled during those same years.

Another reason why stock prices rose so significantly during the decade was that banks and brokerage companies were encouraging stock investment through their practice of "buying on margin." A typical stock purchase in the 1920s involved a broker or bank loan of half the stock's value. Such loans climbed from $1 billion in 1920 to $6 billion in 1928. Through this practice 1.5 million families became stock market investors, almost doubling the previous number and creating the largest number of investors to that point in U.S. history. Furthermore trading was constant and heavy, with 236 million shares traded in 1923, compared to 1.1 billion shares in 1928.

Finally, the stock market took on the appeal of a legitimate "get rich quick" scheme. Americans wanted to get in on the boom that the market seemed to represent. They listened to important movers-and-shakers in the corporate world, such as the director of General Motors and chairman of the Democratic Party, John J. Raskob. In 1928 he said the stock boom would continue for years, and that wealth was within the reach of nearly anyone who saved some money regularly to invest in the market. Writing an article for the *Ladies Home Journal* ("Everybody Ought to Be Rich"), Raskob stated, notes historian Dixon Wecter: "If a man saves fifteen dollars a week and invests in common stocks, at the end of twenty years he will have at least $80,000 and an income from investments of around $400 a month. He will be rich."


An unlucky Wall Street speculator, Walter Thornton of New York, offers to sell his car for way below its purchase price after the stock market crash of October 1929.

For hundreds of thousands of Americans, the formula for easy money and financial security was just too appealing to pass up.

## THE STOCK MARKET CRASH

Reality caught up with the U.S. stock market in the autumn of 1929, when the giant bubble of speculation finally began to burst. In part, the timing was caused by Great Britain, where interest rates were raised to lure back investors who had abandoned British markets for the greener pastures of the U.S. stock market. Suddenly, foreign investors and an astute cadre of U.S. speculators saw the writing on the wall and began dumping their U.S. stocks.

The first significant shudder in the market was felt in September 1929, when stock prices fell without warning, only to recover as quickly as they had fallen. On October 21 another drop occurred. On October 23, a Wednesday, 6 million shares were sold, representing a withdrawal from the market of $4 billion in investment. Electric stock tickers were so pressed with information that traders across the country were reading numbers nearly two hours old.

### Black Thursday, Black Tuesday

The next day, October 24, would be remembered as "Black Thursday," with orders to sell off stock spreading across the index. By noon nearly 13 million shares had been traded, setting a new record; the value of the market decreased by $9 billion. Stock tickers ran four hours behind. The day ended on an up tick, reducing the day's losses to approximately one-third of the previous day. Following the drop on Black Thursday the investment firm of J. P. Morgan and Company, with support from other large banks, hurriedly bought up as many stocks as they could just to restore public confidence in the market.

It was all for nothing. On October 29, 1929, a day recalled even today as "Black Tuesday," the market collapsed. That day 16 million shares were traded, and the industrial stock index dropped 43 points, destroying nearly all the gains made by the market during the previous 12 months. Multiple stocks lost almost all their value. For three weeks following "Black Tuesday," the market continued to free-fall. By the middle of November, the market had lost about one-third of its value, an amount representing $26 billion, or 40 percent of all stock that had existed on the Exchange just a month earlier.

## Wall Street Suicides

The once powerful stockbrokers of New York were losing their silk shirts. Some, their livelihoods gone and their wealth evaporating, chose to end it all by leaping out of their office windows. One was the head of the Union Cigar Company, whose company's stock had dropped from $115 a share to $2. He took a dive from a ledge above the streets of New York City. Another jumper, this one in Milwaukee, left a suicide note that read, notes historian Robin Doak: "My body should go to science, my soul to Andrew W. Mellon [Hoover's Secretary of the Treasury], and sympathy to my creditors." A dark joke soon began to spread of hotel clerks questioning guests as they signed in for a room: "For sleeping or jumping?"

One of the most famous jumps was reported by Winston Churchill, who was to become Prime Minister of Great Britain in 1940. Churchill was staying at the Savoy-Plaza Hotel in New York the day after "Black Tuesday," and was awakened by a crowd on the street below. He wrote later: "Under my very window a gentleman cast himself down fifteen storeys and was dashed to pieces, causing a wild commotion and the arrival of the fire brigade."

Actually, Wall Street suicides became part of the myth of the Great Depression. New York City's chief medical officer reported on November 13, 1929, that just 44 suicides had taken place during the previous month, which included "Black Tuesday," a lower number than the 53 suicides reported during the same period a year earlier.

### Crash Followed by Depression

Within another month, further stock slides represented a market loss of 50 percent of the value of stocks on the market back in September. And the decline continued over the next three years. The industrial index—a measure of performance of leading industrial shares—which was pegged at 452 in September 1929, hit bottom in July 1932 at 58.

But, when the stock market began to tumble off in late October 1929, it was not the cause of the long-term economic depression that followed. Instead, it was a symptom of the nation's less-than-healthy economy. In the first place, the vast majority of Americans were not invested in the market. Historians and economists estimate that just 3 million Americans—approximately 2.5 percent of the population—owned any stock at all. Thus, according to historian David M. Kennedy, "the Crash in itself had little direct or immediate economic effect on the typical American." The same would not be true, of course, of the Great Depression that was soon to engulf not just the United States, but most of the industrialized world.

## CAUSES OF THE DEPRESSION

Several important circumstances, some of which were not within the scope of the U.S. government's control, were responsible for the Great Depression that spread across the United States and throughout the western industrialized nations after 1929.

A significant portion of the economic growth in the United States during the 1920s had been in two industries: construction and automobile sales. By the late 1920s both these industries were declining. Construction expenditures fell between 1926 and 1929, from $11 billion to $9 billion. Car sales were also down, dropping by one-third throughout 1929 until the Crash. Americans had now bought their Fords, Parkards, Studebakers, and Pierce-Arrows, and most were more than happy to hang on to them as long as pos-

## Signs of Disaster

For many Americans, the stock market collapse in October 1929 was a shock. So many had considered the economy to be "bullet proof," experiencing a boom that might continue without end. But reality caught up with the nation that fateful fall. Yet, for some people, the collapse came as no surprise—a few Americans had seen it coming.

Some of them were in positions of power. One such was Smith Wildman Brookhart, a Republican senator from Iowa who was elected in 1920 and again in 1926. Brookhart was considered an "Insurgent Republican," because he was often critical of the economic politics of Republican presidents Harding and Coolidge. During a Senate hearing in 1928 Brookhart stated to "expert witness" Joseph Stagg Lawrence, a Princeton University economist, his opinion that the United States was "headed for the greatest panic in the history of the world," notes historian David A. Horowitz. Professor Lawrence dismissed Brookhart's claims as "the curious emissions of a provincial mind."

Among the others who spotted signs of coming disaster was a Minnesota senator, Henrik Shipstead, who noted before the Crash that 3,500 small banks had closed their doors across the country between 1920 and 1925. Herbert Hoover also saw it coming, and sold off most of his stock long before the bottom fell out of the market.

sible, ultimately cutting the nation's market for new automobiles. With drops in building and automobiles, dozens of "feeder" industries were impacted, including electronics, rubber, lumber, cement, and steel.

## Poverty and Credit

A second cause of the Depression related to how good the "good times" of the 1920s had really been for the majority of Americans. It appears the economy was vibrant in many ways, but the wealth of the era was not evenly distributed to everyone. Even as late as 1929 more than 50 percent of U.S. families were living at or below the poverty line. This meant that they were too poor to buy the consumer goods that were, in part, fueling the economic boom. There were profits in major sectors of the economy, for farmers, industrial workers, and others, but the level of those profits did not generate enough income to create adequate markets. For example, between 1923 and 1929, manufacturing output per U.S. worker increased by 32 percent, yet during those same years real wages only increased by 8 percent. U.S. workers were more productive, but they were unable to afford the goods they were producing. Had manufacturers paid their workers better, those workers would have had greater purchasing power, which would have fed the economy.

Perhaps related to this is the third cause of the Depression—the level of the nation's credit structure. So many of those who were buying from the abundance of U.S. consumer goods being produced did so on credit. Unable to pay cash for the things they saw advertised, many were driven to make purchases on credit, through revolving credit plans, installment plans, and other newly created means. A family's parlor might feature a radio, vacuum sweeper, and nice furniture, but this did not mean they were able to afford such things. Farmers too were deeply in debt, with their lands mortgaged to the hilt, but with farm prices too low to allow them to pay off those debts. With so many small banks in small towns loaning farmers money, they became shaky institutions, as their customers were sometimes unable to pay or simply defaulted on their loans. In addition, some of the larger U.S. banks were incautiously investing in the stock market or otherwise giving out their own bad loans.

## The International Situation

The fourth and fifth causes of the Great Depression in America were related more directly to the country's international economic situation. While U.S. companies had produced an abundance of goods during World War I, when European powers needed everything from tents to trucks, the demand for U.S. goods fell off dramatically after the war. Postwar Europeans rebuilt their own industries and reclaimed their farm fields, so they did not need to rely on U.S. goods and food. Tariffs were commonplace among the industrialized nations of the West, which limited trade between them. Some tariff rates were as high as they had ever been, keeping U.S. goods out of foreign markets and limiting the sale of U.S. products.

Lastly, an important factor leading to the Depression was the international debt structure. During the war European nations had borrowed billions from the U.S. Treasury to help pay for their war effort. Those Allied nations, particularly Britain and France, had intended to repay their own debts by extracting reparations, or war damages, from the defeated Central Powers, especially Germany. But Germany and Austria emerged from the war with their economies in shambles, and their governments unable to pay. If the war's losers could not pay the war's winners, U.S. bankers were left holding the bag. In addition, U.S. banking houses loaned Germany a further $1.2 billion between 1924 and 1930, in an effort to help the country recover from the war and become a viable trading partner for the future.

## Rich and Poor

All this meant that the booming prosperity of America's "Roaring Twenties" had represented a warped or lopsided economy. The production of consumer goods was always running ahead of the average person's ability to buy them. In fact, the U.S. economy of the 1920s represented an extremely uneven distribution of wealth. In 1929 the top 0.1 percent of U.S. households had a combined income equal to that of the bottom 42 percent of U.S. households, who numbered 11.5 million families. That same 0.1 percent of wealthy Americans also owned one out of every three dollars held as savings. Approximately 80 percent of families in the United States had no money saved at all. Similarly, 71 percent of U.S. families had annual incomes of $2,500 or less (equivalent to about $32,000 today).

The U.S. economy of the 1920s had appeared, if one did not look behind the stage set, booming, progressive, and pointing endlessly upward. But by 1929 the bubble had burst, and the nation found itself engulfed in the deepest economic collapse in its history. Yet 1929 was only the beginning. Over the next four years, the nation's economy continued to slide downward into a hole that seemed to have no bottom.