1 The Great Depression of 1929

Crisis in the world economy

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1.1 The Western economy in the early 20th century

The 20th century was marked by dramatic upheavals: two world wars – of great severity and destruction – and several economic crises. The "interwar period" (1918–1939) ran from the end of the First World War to the beginning of the Second World War. During these years, two events stand out: the birth of the Soviet Union and the economic crisis of 1929. In this chapter, we will deal with the second of these events.

The outbreak of the First World War upset the international equilibrium of the early years of the 20th century. Until 1914, the political rivalry of the great powers had not generated tensions of such scope and gravity. From that year onwards, events far outstripped the attitudes of politicians and rulers (Casanova 2011). After an acute post-war crisis followed by a short depression in 1920, the industrialised countries of the West benefited from a period of expansion that lasted until 1929 (Aldcroft 1989). Political, social, and economic life had weakened in Europe, and some countries were on the verge of bankruptcy in the early post-war period. Growth during these years was very uneven. Britain suffered through a precarious situation after the deflationary experience of 1925, which led to a return to the gold standard; France endured tremendous instability; and Germany was plagued by terrible hyperinflation. In Spain, economic growth was similar to that experienced in the rest of Europe and coincided with the favourable international environment after the war. However, by 1930, the difference in Spanish GDP per capita compared to the most advanced countries was still considerable (Carreras and Tafunell 2010; Sánchez and Catalán 2013). The fragile foundations of the "Roaring Twenties" were largely overlooked out of ignorance.

The crisis erupted in October 1929 with the collapse of the New York Stock Exchange. The depression spread rapidly around the world. Widespread unemployment affected almost every country and the national economy and trade declined sharply. Traditional liberalism was called into question and there was talk of a "deep crisis of capitalism". The shock was very serious for the capitalist system because in those same years the whole world witnessed the first steps of a collectivist economy taking hold in the Soviet Union (Comín 2011b).

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Between 1929 and 1932, the world experienced one of the worst depressions in history. The existing state of economic science was powerless to solve the problem, and the decisions taken by governments were, on the whole, misguided. Policies tended to be protectionist in nature, designed to insulate national economies from external "contagion". Attempts at international cooperation failed at the London Conference of 1933. Each country avoided "external contamination" and sought to "export its unemployment" through protectionist policies (Parker and Whaples 2013). A case in point is the United States, which imposed very high tariffs. At this juncture, the depression spread very quickly, mainly because of the sheer scale of the US economy compared to the rest of the world. In 1929, 40% of world manufacturing production was located in the United States; its imports represented 12% of the world total, while its exports accounted for 15.8% globally (Matés-Barco 2017a).

The improvement in 1933 had little to do with government recovery programmes, although some instigated ambitious plans to boost their economies. The recovery was very slow and uneven, especially in terms of job creation, to the extent that on the eve of the Second World War there were still a number of countries with very impoverished economies. This precarious situation led to rearmament policies that reactivated the arms industry, a major consumer of industrial raw materials. These actions were not only a danger to world peace, but also a fertile breeding ground for fascism.

1.2 Peace and economic instability in the 1920s

Throughout the 19th century, the European continent experienced significant economic development. Sidney Pollard (1991) has noted that this process can be seen as a general phenomenon that transcends national borders, although it was most prominent in Europe and North America. Economic growth rates were modest and very uneven across countries, but were particularly strong in Britain, France, Germany, Belgium, and the Netherlands. However, the war of 1914–1918 was the dramatic precedent for the Second World War and led to significant stagnation. For all those who witnessed the high number of casualties, or the levels of destruction caused by this event, it was such a shock that it was referred to as the "Great War".

Once peace was achieved, far from alleviating economic problems, it arguably increased them for two main reasons. Firstly, because it led to increasing financial and monetary instability and, secondly, because it stimulated a certain economic nationalism. The best known of the treaties was that of Versailles, which established peace with Germany. Apart from territorial compensation for regions such as Alsace and Lorraine, the treaty allowed France to occupy the Saar Valley coal basin for 15 years and ceded parts of Prussia and part of Upper Silesia – rich in mineral deposits – to Poland. But the most significant aspects, apart from border adjustments, centred on dispossessing Germany of much of its mineral resources (iron, zinc, coal), depriving it of 13% of its arable land, as well as its colonies in Africa and the Pacific. In addition, it had to give up its

navy, most of its merchant fleet, locomotives, wagons, trucks, etc. In short, it was a humiliating and rather onerous surrender, reflected in the famous War Guilt Clause in Article 231, which stated that Germany was responsible for having started the war. Basically, the Allies were attempting to justify the reparations that Germany had to make in compensation for the destruction caused by the war. But the Allies did not take a uniform position, and a Reparations Commission was appointed, which was to report by 1 May 1921. John Maynard Keynes, economic adviser to the British delegation to the peace treaty, warned of disastrous consequences for the whole of Europe if the demands for reparations were maintained. After resigning from the delegation because he did not agree with the measures adopted, he set out his reasoning, ideas, and approaches in a well-known book entitled *The Economic Consequences of the Peace* (Keynes 1919/1991). These ideas were much debated, but the passage of time confirmed his dramatic predictions.

In Western Europe, some countries adopted very restrictive measures, such as protectionist tariffs and import bans on certain products. Others promoted their own exports through subsidies. Britain, an advocate of free trade, neglected this practice by maintaining and increasing the tariffs it had already put in place during the war in order to achieve its funding. Even the United States imposed very restrictive protectionist legislation, enacting laws such as the Emergency Tariff Act (1921), which banned imports of German dyes; the Fordney–McCumber Tariff Act (1922), with one of the highest tariff levels in American tariff history; and the Smoot–Hawley Tariff (1930), which even exceeded the rates of the 1922 law and provoked a chain reaction from other countries, which responded by increasing their tariffs against American products. Ultimately, the practice of such exaggerated economic nationalism, embodied in countless protectionist provisions, led to a slowdown in production and the establishment of lower than desired income levels (Hynes, Jacks, and O'Rourke 2012).

But it was not only economic nationalism that caused the collapse of the international economy; financial and monetary disturbances also played a major role, with the problem of war reparations as a backdrop. At the end of the war, the debts of the Allied bloc countries amounted to more than $20 billion, which had been lent mainly by the United States and Great Britain. American leaders viewed the loans as simple commercial transactions, but they encountered European reluctance to repay these obligations. As this controversy manifested itself in all its crudeness, the issue of reparations emerged, as Britain and France demanded that Germany pay them not only for civilian damages, but also as compensation to cover the full cost of the war. The Reparations Commission estimated that Germany would have to pay 132 billion gold marks (about $3 billion), more than twice its national income. The precarious state of the international economy, coupled with the pressure on Germany to make the payments, resulted in uncontrolled inflation, leading to a disastrous situation in November 1923, when one US dollar was worth 4.2 trillion German marks (Holtfrerich 1986). A mark was worth less than the paper it was printed on.

Hyperinflation not only occurred in Germany but also spread to other nations such as Bulgaria, Austria, and France itself. This led the League of Nations to adopt stabilisation measures that achieved their objectives by 1926. Although disputed, Keynes' predictions about the crisis in the international economy seemed to be coming true. To turn the situation around, an international loan of some 800 million marks was granted to Germany, in addition to lower annual reparation payments. This loan, mostly from the United States, enabled Germany to resume paying reparations and to obtain the foreign exchange it needed to modernise its industry.

Periods of war have a strong influence on economic activity. The post-war depression was quite severe, but very brief. It was followed by a longer period of expansion lasting until 1929, at least in the United States, which can be considered the peak of American and world prosperity. The American economy benefited from the thrust that the exigencies of war imposed on industrial production, both between 1914 and 1919 and between 1939 and 1945. The United States emerged stronger from the First World War. In the years that followed, it became the leading exporter of goods and services, as well as the leading investor of capital in other countries.

In the meantime, Europe had to rebuild itself from its ruins. To help in this task, in 1919, the American government created the American Relief Administration (ARA) to provide economic aid to certain central European countries threatened by crisis and famine. In 1929, aid from the ARA totalled 1.415 billion dollars in foreign currency (29%), loans (63%), and grants (8%). The loans were never to be repaid because of the 1929 crisis. The situation in Europe, although challenging because of reconstruction needs, was not critical. The main problem lay in the difficulty of transforming a wartime economy into a peacetime one. The mass demobilisation of soldiers from the army could lead to a sharp rise in unemployment, but the forced savings accumulated during the war made it possible to finance the purchase of consumer goods to rebuild the household economy. The strong demand for consumer goods, especially in Great Britain, made it possible to hire this huge mass of demilitarised young men. The demand for capital and intermediate goods also increased as a result of the inflationary expansion process.

In 1920 and 1921, the data show the severity of the crisis: the manufacturing industry shrank by 30% in Britain and 24% in the United States, and prices fell by about 37%. The depression was deep but short lived and is evidenced by the decline in demand for consumer durables. Several factors played a role in the fall in economic activity. On the one hand, the normalisation of international trade and the supply of raw materials and, on the other, restrictive monetary policies played an important role in this trend. The instability of 1920 is the prototype of a crisis of reconversion from a wartime to a peacetime economy. France also suffered serious imbalances, although they were not as deep as in Britain and the United States. Reconstruction boosted demand for capital goods and stemmed the depression. Budgetary and financial policy contributed to the maintenance of aggregate demand, as equilibrium was assured by advances from

the Bank of France. Between 1922 and 1929, there was a period of expansion, although there were differences among countries. Two minor recessions in 1924 and 1927 softened this economic upswing. The 1920s saw international monetary reconstruction within the framework of the famous gold exchange standard, the failure of which in 1930 played a major role in the world crisis.

Inflation inflicted deep wounds on European society, especially in Germany and Britain. The dire situation of the Germans, especially the middle class, wage earners, and workers, led to the inclination of these groups towards extremist politicians. It is symptomatic that the national socialists (Nazis) and the communists increased their parliamentary representation in the Reichstag in the 1924 elections. German hyperinflation followed the upswing in foreign exchange rates, which was faster than the rise in prices. In a second stage, rising prices took the lead, but foreign currencies (dollar, pound, franc) gradually replaced the mark as a means of domestic payment. German production increased until the beginning of 1923, so the government launched a stabilisation policy and created the *Rentenbank* and the *Rentenmark*. The *Rentenmark* was a currency guaranteed by the national wealth, endowed with legal tender status and with the same value as the pre-war gold mark. One *Rentenmark* was exchanged for 1 trillion paper marks. The operation generated confidence in the German currency and made it possible to obtain credit in 1924, which facilitated the inflow of foreign capital. In the Treaty of Versailles, the Reparations Commission had set at £6 billion the compensation Germany was to pay for the damage caused during the war. France was counting on these payments to rebuild its devastated regions and balance the budget. Germany, with its soaring hyperinflation, could not meet these debts, so France occupied the Ruhr region in January 1923. The Commission, chaired by the American Dawes, established that Germany would have to pay between £50 million and £150 million, with the first disbursement to be made thanks to an international loan of £40 million.

Great Britain suffered a similar situation, as economic problems became particularly acute in the post-war period. The British had to deal with the readjustment of their economy, which was overly dependent on international trade, while unemployment rose to over 25% in the years following the Great Depression of 1929. The economic policy adopted by its rulers was not the most appropriate, and the initiative to return to the gold standard, taken in 1925 by the then Chancellor of the Exchequer, Winston Churchill, was very harmful. The repercussions of this measure were especially serious in the world of labour. Wages fell considerably, especially in the coal mines, prompting miners to call a general strike, which they tried to enforce in May 1926. It was supported by about 40% of unionised workers, and although it was a short-lived conflict, it left a trail of social confrontation that made it difficult to resolve the serious national and international problems afflicting the British economy.

The British textile industry experienced a decline that resulted in the abandonment of exports to traditional markets. In 1907, Britain exported almost 90% of its total production, but by 1929 it had fallen to 73.7%, and by 1935 it

accounted for only 57.6%. Between 1913 and 1937, the Far Eastern markets (Hong Kong, China, India, Japan) saw a 90% drop in the arrival of British textile products. This decline was due to the development of synthetic fibres and competition from Japanese products. The same was true of coal and iron and steel. Between 1900 and 1937, coal exports fell from 19.5% to 16.5%, and steel exports fell from 13.2% in 1913 to 8.3% in 1937.

Inflation in France was not as high as in Germany but lasted until 1926. The price swings and the tremendous ups and downs are indicative of its economic instability. Between 1914 and 1926, one pound sterling went from 25.22 francs to 240 francs, and one dollar went from 5.18 to 49.22 francs. The Poincaré government achieved a significant decline in inflation and the French economy improved from 1926 onwards, thanks to international expansionary conditions and the devaluation of the currency, which boosted exports. Although the rate of industrial production declined in these years, the increase in manufactured goods was evident (Parejo and Sudrià 2012).

The United States experienced strong economic expansion until 1929. From 1922 onwards, there was spectacular development in construction, electricity, and the automobile industry. The latter increased its production (33%) and led to an expansion of oil exploration, steel, rubber, and infrastructure construction, such as roads. The manufacture of electrical appliances boosted the production of electricity. Unemployment fell to just 2% of the labour force and the total output of manufactured goods increased by nearly 50%.

The trend of international investment at this stage shows a lack of rationality. Britain, France, and the United States were at the forefront of foreign investment. New York emerged as the new financial centre and investment behaviour was extremely risky. American lenders flooded Europe and much of the world with unsafe and speculative investments. In essence, the United States lent capital to Europe so that Europeans would "buy" American products. It was a way of financing exports using a practice the British had employed extensively in the 19th century. The difference was that American companies and bankers forced this lending activity. These operations, by increasing the income and consumption of foreign countries – increasingly dependent on a continuous source of foreign exchange – made the outbreak of an unsustainable situation inevitable.

Nevertheless, most of Europe experienced relative progress and, from 1924 onwards, the "Roaring Twenties" wore the face of optimism and economic prosperity. Much of the reparations for war damage had been paid, and this made it easier to solve the more immediate problems. However, the foundation of that prosperity was so fragile that 1929 showed most starkly how the progress of recent years had been but a mirage.

1.3 The 1929 crisis and its effects on the world economy

Until 1929, none of the economic crises in previous history had been as far-reaching as the one that occurred in that year. Above all, the "crash of 1929" is significant for its broad global impact, which was facilitated by the importance

of the United States in the international economy. The exceptions were nations that, because of their precariousness or economic situation, were cut off from the capitalist system. In any case, the crisis did not begin at the same time in all countries, nor did it have the same magnitude, nor was its duration identical. As Morilla Critz (1991) points out, there are two basic truths that allow us to understand the shocks suffered by the international economy: 1) "the seeds of the crisis were scattered in many places"; and 2) "that from a certain moment (which we place in 1929), a chain reaction was set in motion, which amplified and spread the crisis from one sector to another, and from one part of the world to another".

1.3.1 The crisis from the perspective of economic theory

The unfolding of the 1929 crisis has been well described by many scholars, but the analysis of the causes remains a matter of discussion and debate (Kindleberger 1991; Galbraith 1993; Marichal 2010). The complexity lies in explaining the severity, depth, and extent of the subsequent economic depression. History has shown how the capitalist system exhibits cyclical behaviour, which has been described differently according to the respective schools of economic thought (Barber 1974; Barnett 2017).

First, there is the instability school, which characterises capitalism as an essentially unstable system. Malthus, Marx, and Keynes have been its leading exponents. Thomas Malthus (1766–1834) developed his theories on crises, underconsumption, and defended protectionism (Fernández-Delgado 2003). For his part, Karl Marx (1818–1883) pointed out the internal contradictions of capitalism, due to the difficulty of controlling the market and chronic underconsumption, which would lead to its destruction. At the same time, Marx harshly criticised the Malthusian theory of population as a superficial plagiarism of authors such as Daniel Defoe (1660–1731) and Benjamin Franklin (1706–1790). On the other hand, in *Capital* – in contrast to Malthus – he defended the scientific and technological advances that would allow for exponential population growth (Martín-Muñoz 2003; Perdices de Blas 2003; Rodríguez-Braun 2006). In the 20th century, John Maynard Keynes (1883–1946) outlined a theory of stabilising intervention by the state, in order to avoid falls in effective demand (Galindo-Martín 2003; Wapshott 2016).

Second, the stability school assumes that the market is able to cope with the different crises that the system undergoes and is capable of returning to equilibrium. Neoclassical economists are part of this group and have not been very interested in the analysis of cycles. Galbraith (1993), in his well-known book on the 1929 crisis, notes the reassuring statements of the economists of the time, who stubbornly ignored the serious situation that arose, even months after the crisis had affected most of the world's population (Landreth and Colander 2006; Roncaglia 2017).

The third school places the cycle at the centre of its theory. The economist Joseph Alois Schumpeter (1883–1950) was its most prominent figure. Of

Austrian origin but based in the United States, where he was a professor from 1932 at Harvard University, he described the theory of the long development cycle inspired by the economist Kondratieff. Another economist, Kuznets, disseminated his theory of the infrastructure cycle (15–20 years), which accompanied the long cycle related to technological systems requiring major investments (locomotives with railways, automobiles with roads, electricity with dams, etc.). There are also financial cycles in which investment "euphoria" alternates with "panic" with the sale of shares (Galbraith 2011; Rothbard 2006/2012; Vegara 2019).

1.3.2 The causes of the 1929 crash

The United States emerged from the First World War in a favoured position, or at least in a stronger position than in 1914. In economic terms, it had shifted from being a debtor to a creditor and had expanded its sphere of influence in international markets, while Europe was very slowly trying to recover. The balance of trade was extremely favourable, the population was growing markedly, technological advances were very substantial, and the many markets were yielding to the momentum of American exports.

However, serious economic problems, some of them of a structural nature, inherited from the 19th century, had been identified for years before the outbreak of the crisis. For example, there was a lack of interest in reinvesting in industrial activities, which led to an imbalance in this sector and an unfavourable trend in agricultural prices. Between 1920 and 1921, the country suffered an acute and brief economic crisis, which was reflected in the harsh living conditions of a large part of the population. Despite the difficulties, recovery was noticeable in the following years. The gap left by industrial investment was filled by channelling substantial amounts into speculation on the New York Stock Exchange. This speculative fever was evident throughout the 1920s. In these years, it experienced a spectacular rise that, at times, provoked an atmosphere of unbridled speculation and closed one of the most extraordinary speculative periods. The share price index rose from 100 in 1926 to 216 in 1929.

Until March 1928, the rise in share prices was not excessive and remained in line with profits. From then on, a speculative boom phase ensued. Galbraith (1993) has pointed to the influence of certain large companies on this trend. Some businessmen painted a glowing picture and heralded a period of economic upswing and enormous profits. On 12 June 1928, there was a first warning with the sale of more than 5 million shares and an overall loss of 23 points in the value of the shares. From July onwards, the stock market experienced further rises and the election campaign for the US presidency focused on announcements of prosperity and welfare. During the summer of that year, American banks and investors began to restrict purchases of German and other bonds. The aim was to invest their funds through the New York Stock Exchange, which began to soar. After the election of Republican candidate Herbert Hoover, the stock market experienced a further rise. In his *Memoirs*

(Hoover 1952/2016), recalling these fateful years, he called speculation a crime worse than murder and one for which men should be "reviled and punished".

The rise in the stock market did not correspond to increased productivity but was rather the result of an excessive process of speculation, by not only large corporations but also small and medium-sized investors. The investment fever stemmed from an exaggerated eagerness to achieve capital growth and was not based on the attraction that good dividends from a profitable company could offer. Thus, a spiral of acquisitions was unleashed, leading to a permanent upward spiral.

In these months of speculative rises, many people of modest means rushed to buy stocks by borrowing money. New York banks were lending short term at 12% interest, when they were borrowing from the Federal Reserve at 5%. Even currency dealers were lending to their clients against the securities they were buying. Purchases of shares were often made for only 10% of the value being purchased, i.e., brokers advanced buyers 90% of the value of the shares and were obliged to borrow money to do so. More specifically, the loans obtained by the brokers rose from around 3.2 billion in 1925 to nearly 7 billion dollars in 1929 (Table 1.1). This is sufficiently illustrative of the effervescence in business (Eichengreen and Mitchener 2003).

But speculation was doomed to failure if stock prices did not correlate with production and profits. And it was indeed the United States that was beginning to experience a certain degree of stagnation and regression. The US gross national product began to decline gradually and steadily in the early months of 1929. A sector as dynamic and expanding as automobile manufacturing began to falter. In March, production reached 622,000 vehicles, while six months later it was down to 416,000. In other words, production in this key industry fell by almost 40%.

For its part, Europe – at the end of the summer of 1929 – was beginning to feel the decline in American investment abroad. Even Germany, the second epicentre of the conflict, was already in serious difficulties by the end of 1928. The economies of many countries deteriorated alarmingly until 1933, with a particular contraction of international trade and the industrial sector. The bomb had been primed; all that remained was for it to detonate.

Table 1.1 Credits to stockbrokers, by origin, 1927–1929 (in millions of dollars)

Date	*New York banks*	*Foreign banks of New York*	*Other*	*TOTAL*
31 December 1927	1,550	1,050	1,830	4,430
30 June 1928	1,080	960	2,860	4,900
31 December 1928	1,640	915	3,885	6,440
30 June 1929	1,360	665	5,045	7,070
4 October 1929	1,095	790	6,640	8,525
31 December 1929	1,200	460	2,450	4,110

Source: Prepared by author with data from Kindleberger (1985, 131).

This scenario was unsustainable in the short term, but the monetary authorities neither understood nor wished to remedy this situation. Galbraith (1993) has shown how the great leaders and economists of the time were unaware of the seriousness of the economic situation. From the chairman of the Federal Reserve to prestigious economists at Harvard University, they spoke of the excellent health of American industry and the irrelevance of broker's loans. At the same time, they argued that nothing could "stop stock prices from rising" and showed that the position "of the markets is satisfactory" and that the value of stocks "has a healthy base given the prosperity" of the United States. For these "learned economists", stock prices "had reached a permanent value" (Table 1.2).

The crisis manifested itself essentially in the United States. Its severity and duration have been among the most spectacular in the capitalist system. When analysing the causes of the crisis, it is relatively easy to list them, although it is more difficult to try to elucidate the importance of each one of them. The bibliography on the subject is immense and the explanations of its origin are endless, but they can be summarised into five key points.

First, the existing imbalance in the international monetary system. The gold standard had been reintroduced in the 1920s, but under conditions that were not in keeping with the economic needs of the time (Bernanke 1983). The United States had changed its role from debtor to net creditor, without observing the "rules of the game" for the proper functioning of the gold standard, as well as not allowing net transfers from Europe. This set of actions caused the system to be unsound and its functioning to run into serious difficulties.

The second issue refers to the structural changes that occurred in the 1920s, especially the decrease in the flexibility of the product market. The rise of monopolies became increasingly evident, and the labour factor began to decline markedly. The return to equilibrium became increasingly difficult.

Third, the role of the New York Stock Exchange must be recalled. Its role has sometimes been exaggerated as both the trigger and the main cause of the crisis. In the United States, in the preceding months, a decline in investment,

Table 1.2 New York Stock Exchange (1913–1929): stock price index (1935–1936 = 100)

Years	*General index*	*Industrial values*	*Railways*	*Public services*
1913	71		240	90
1921	58		164	
1924		63	204	92
1925	95	80	238	111
1926	106	90	265	
1927 (June)		103	316	135
1927 (December)			336	
1928 (June)		134	336	173
1929 (September)	238	195	446	375

Source: Prepared by author with data from Morilla Critz (1991, 119).

production, and income had begun to be detected. At the same time, prices were falling. In Germany, this trend had been discernible a year earlier. Stock market crises had been frequent before and after 1929 and of even greater proportions, but none caused such a severe economic crisis.

The fourth issue that determined the significance of the crisis was the restrictive monetary policy of both the United States and Germany. This led to financial panic, chain bankruptcies and deflation, all due to the absence of international lenders.

Finally, the crisis was transmitted to the rest of the world through the lack of coordination, falling prices, and the mechanisms of the gold standard (Eichengreen 1992; Wolf 2010). At the same time, misinterpreted fiscal orthodoxy and protectionism aggravated the situation. Declining revenues inclined governments to reduce expenditures and increase taxes, right in the middle of the crisis, in order to achieve a balanced budget. Moreover, from 1931, all countries increased their levels of protection, making trade more difficult. The economic policies that had been pursued in previous years with positive results had completely opposite effects. The protectionism introduced in most countries led to a decline in exports and a fall in income.

The brake on the situation occurred in October 1929, but despite its brutality it came in stages. The crisis manifested itself on 24 October – "Black Thursday" – when nearly 13 million securities were offered with almost no demand. The banks intervened in order to halt the fall and briefly managed to restore confidence. By the end of Black Thursday, share prices had fallen by between 12 and 25 points. On Monday, 28 October, the collapse began without any possibility of rescue. On that day, a total of 9,250,000 shares went on sale. Industrial assets were down 49 points and bankers were unwilling to buy any more securities. On 29 October – "Black Tuesday" – the panic triggered a new spate of stock market sell-offs (33 million shares), causing a terrible fall in the value of shares (Table 1.3).

The Dow-Jones index of the New York Stock Exchange between September 1929 and January 1933 shows that the values of 30 companies fell from an average of \$364.90 to \$62.70 per share; the 20 government debt securities dropped from \$141.90 to \$28; and the stock prices of 20 railway companies declined from \$180 to \$28.10. Between October 1929 and July 1933 – the

Table 1.3 Share prices in selected markets from September to December 1929 (monthly indices calculated on different bases)

1929	*Belgium*	*Canada*	*France*	*Germany*	*Netherlands*	*Sweden*	*Switzerland*	*UK*	*USA*
September		316	526	125			239		216
October	98	255	496		113	162		135	194
November	92	209	465		98		212		145
December	79	210	469	107	100		215		

Source: Data taken from Kindleberger (1985, 141).

bottom of the depression – the total value of traded capital fell by $74 billion. In the latter year, the national income of the United States did not reach $40 billion.

Despite the catastrophe, a few days after these events, voices were still being heard, claiming that "the present stock market and business recession is not a precursor sign of a depression". Or that it was unlikely that there would be a repetition of a situation as serious as that of 1920–1921. And even that the "recovery will take place in the spring [of 1930] and consolidate in the autumn". The absence of perspective suggested that the industry was on the road to recovery. These statements show the lack of awareness of the seriousness of the problem, among both political leaders and the "brainy economists" of the time, as well as the inability to find appropriate solutions to emerge from the crisis (Roncaglia 2015).

The stock market crash was not the cause of the Great Depression, but it was the starting pistol that signalled the race towards declining output and rising unemployment. The fragmentation of the banking structure was one of the weaknesses of the US economy. Not only was easy access to credit a problem, but also the mistakes made by the authorities in monetary policy, especially the actions of the Federal Reserve, which Galbraith (1993) describes as "a body of starling incompetence".

After many decades and numerous studies on the subject, there is no unanimity as to the most determinant causes of the depression. For some, they were mainly monetarist; for others, they lay in the fall in consumption and investment and how this spread throughout the economy. In recent years, new arguments have been put forward: the instability of agriculture, the First World War and the implementation of peace treaties, the breakdown of the gold standard, or the disruption of trade and the nationalist policies of the entire decade (Crafts and Fearon 2013).

In any case, it is of great interest to reflect on the causes of the 1929 crisis and the subsequent depression. In this way, the economic policies applied by the different governments in order to achieve recovery can be appreciated with greater precision. The main difficulty lies in assessing the relative importance of each of them and differentiating between the stock market crash of 1929 and the depression that followed. Distinguishing between the causes of one and the other is not easy. It is clear that in the preceding months the importance of the problem was not grasped, and even the severity of the depression that followed was not even minimally perceived. As early as 1934, the complexity of the phenomenon and the impossibility of explaining it with a single reason were already being pondered. The influences were manifold and varied: political unrest, structural weaknesses, and nationalist mentality (Wandscheneider 2013).

One of the reasons most often used to explain the collapse of the New York Stock Exchange is the exorbitant rise in stock prices. It has already been said that the boom in securities could not last indefinitely. Speculation decoupled from economic activity, that is, from production and profits, brings its own

ruin. The lessons of speculation are recurrent – it had already occurred in 18th-century England and 19th-century France – and provide clear evidence of its harmful aspects. One might then ask about the reasons that led to the long and enormous speculation of the years 1927–1929. It was the result of monetary inflation caused by the policy of cheap money and easy credit granted by the Federal Reserve. This conduct was one of the most serious mistakes made by any banking organisation in the last century (Almunia et al. 2010). US authorities were overwhelmed by the pace and momentum of events. The speed of the circulation of money and the expectations of speculators swept away everything in their path.

It is clear that some causes did have a greater impact. For example, the excessive fragmentation of the banking structure, which was one of the weaknesses of the US economy (Galbraith 1993). Furthermore, the organisational structure of US firms was conducive to unbalanced and abusive practices. The development of holding companies and trusts encouraged intense speculation. Such companies owned bundles of shares and bonds and had a vested interest in skyrocketing share prices. Meanwhile, dishonest business practices were rampant, involving shady deals, swindles, and fraudulent schemes. High-profile personalities from politics, finance, industry, and even the cinema, through their popular influence, played a key role in these regrettable actions. In this course of events, the small and medium-sized investor was swept along by an excessive desire for profit and failed to see the deceitful deals that were right before their eyes. Maurice Niveau (1989) has emphasised how financial and banking structures, large capitalist interests, and mass psychology were cumulative causes of excessive speculation and high inflation. Moreover, as we have seen, the monetary authorities proved incapable of acting to prevent the crisis.

1.3.3 The impact of the crisis in Europe

The complexity of the crisis, the extent of its repercussions, and the diversity of situations make it difficult to analyse in detail the multiple causes of the depression. Recent research has shown the error of liberal orthodoxy. Economic science provided few solutions and excessive conservatism prevented the adoption of economic policies in line with the situation.

Conjunctural factors played an important role. Bank failures resulted in corporate insolvency and compromised the creditworthiness and confidence of depositors. This, in turn, led to the hoarding of gold and banknotes, which paralysed investment. In addition, falling prices, especially agricultural prices, reduced the buying potential of producers and sellers. In this climate, unease, misgivings, and pessimism took hold of the population, which curbed its appetite for consumerism. Faced with low consumption and rising unemployment, producers and sellers did not renew their inventories, did not modernise their technology, and put the brakes on any kind of investment. This progressive reduction generated a multiplier mechanism that paralysed investment and increased the inflationary trend.

In terms of structural factors, what stands out is the growing importance of the US economy in the rest of the world, which facilitated the rapid expansion of the depression. The stoppage of capital exports affected a number of countries, especially Germany, as well as the nations of Central and South America, which, seeing their financing channels interrupted, stopped buying US products (Campa 1990; Bulmer-Thomas 2002; Marichal 2012; Matés-Barco 2017b). The process was completed when the United States reduced its purchases of raw materials from these countries, causing prices to fall dramatically. This paralysis of international trade was compounded by the changes taking place in industry as a result of the second phase of industrialisation: traditional sectors (textiles and coal) gave way to new ones (chemicals and capital goods) (Figure 1.1).

Protectionist measures (tariffs and quantitative restrictions) accelerated the decline in foreign trade. States sought to achieve a larger share of exports, but to import as little as possible, which led to trade paralysis. These "beggar-thy-neighbour" policies – typical of the mercantilism of the 17th century – were once again adopted and caused serious problems for the world economy. Britain and the Commonwealth countries alleviated the harsh grip of the depression by practising the system of "imperial preference".

Another factor that facilitated the dampening of international relations was the collapse of the international monetary system. The abandonment of the gold

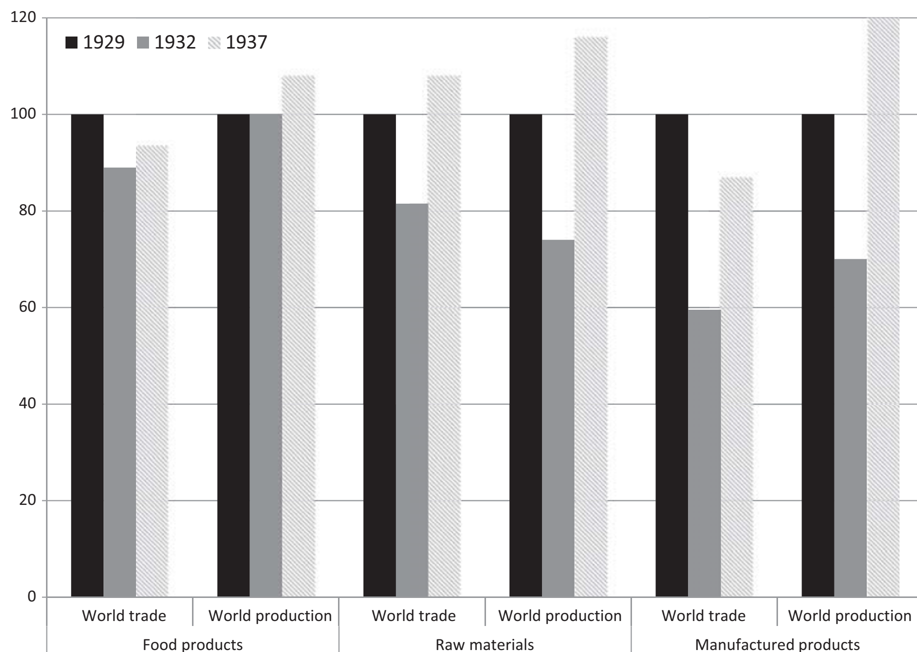

Figure 1.1 Evolution of production and foreign trade (1929–1937) (1929 = 100)

Source: Prepared by author with data from Niveau (1989, 199).

exchange standard affected international means of payment and monetary institutions. The weakness of monetary liquidity made it difficult to finance trade. The crisis in the international monetary system during the First World War caused London to lose its leading role. Between 1918 and 1930, London's struggle with New York for international financial leadership created many problems for economic stability. To a large extent, the failure of the gold exchange standard was a result of this struggle and one of the consequences of the 1929 crisis, but the collapse of the international monetary system became a new cause that aggravated the depression of the following years (Bernanke and James 1991).

The interwar period was a transitional stage between the end of 19th-century capitalism – which some extend to 1914 – and modern capitalism after the Second World War. The demise of old structures and the establishment of new ones took time, which was needed to smooth out the rigidities of market mechanisms. The United States and Britain quickly resorted to devaluation and the search for measures to jump-start their economies. France and Germany, on the other hand, remained on the gold standard and pursued a policy of deflation. In both countries, the consequences were very divergent: while in France the failure of Laval led to the victory of the Popular Front, in Germany social conflicts facilitated Hitler's rise to power (Comín 2002; Wandschneider 2008).

The financial aspects of the crisis reached dramatic proportions and highlighted the need to create international bodies to regulate relations between countries. Conditions for banks began to worsen in the spring of 1931. In Austria, in May of that year, the Creditanstalt, one of the largest mixed banks in the country, went bankrupt. The difficult business environment had forced the bank to acquire 60% of the shares of many Austrian companies, in many cases compelled by the government itself. The bank's non-performing loans amounted to 70% of total losses at the time of the bankruptcy. Moreover, 50% of its shares were in foreign hands and 40% of its business was outside Austria. Faced with abandonment, the government intervened very belatedly: exchange controls were introduced in October 1931 and the state became the bank's preferred shareholder. The inability to stop the collapse of the Viennese bank dragged down the Hungarian and German banks. Between May and June, the Reichsbank lost half of its gold reserves. The United States had to provide aid to Germany by granting a moratorium on the payment of war reparations and debts still outstanding from 1918. Nevertheless, in July 1931 the banking crisis exploded with the collapse of Danatbank, one of Germany's four largest banks. The government closed the banks and the stock exchange for a few days. The aim was to prepare a package of measures to halt the free fall, including raising the interest rate to 10% and injecting liquidity into the mixed banks. Danatbank was merged with Dresdner Bank and its capital, like that of Commerz, was largely taken over by the state. The state's share in Deutsche Bank was one-third. At the end of the 1930s, the banks reverted to private ownership.

The German banking shocks spread to the rest of Europe. The Bank of England, which held modest gold reserves, was beset by demands from other institutions and provoked a government crisis that resulted in the appointment of

new ministers. The new administration ordered spending cuts and tax increases in order to balance the budget. Britain, prompted by various conflicts at the time, was forced to leave the gold standard, with a series of very negative repercussions for those countries that did not leave it, which were the vast majority. The adjustment of monetary policy by the United States led to the almost immediate bankruptcy of more than five thousand banks, 5,096 between 1929 and 1932, and was so far-reaching that it paralysed investment. Between 1929 and 1933, of the 26,000 existing American banks, some 11,000 closed their doors. This led to a strong deflationary process. The fragmented structure of the US banking system was one of the first causes of the chain of bank failures. Most banks were small, operating in very limited areas. The economic conditions of the region where they were located determined the success or failure of their management.

France was the only European country to escape the financial crisis. Its large gold reserves (about 25% of the world's stock) allowed it to withstand the crisis without too much stress. Its main problem was not to lose too much value as it disposed of its sterling reserves, which were heavily devalued. However, economic recovery took many years.

A relative exception to the crisis was the Soviet Union. The triumph of the communist revolution of 1917 had moved its economy away from capitalist liberalism. With an economic structure based on planning and state control, the USSR was largely untouched by the Great Depression of 1929. At the time of the New York stock market crash, the Soviet leadership was focused on five-year plans that initiated a process of rapid industrialisation and collectivisation in agriculture. Stalin's programme focused on encouraging the concentration of agricultural holdings in order to achieve an increase in production, which would lead to industrial expansion and increased taxation. Force and violence, such as purges and mass deportations, were common practice in implementing this policy, and the difficulties of Soviet agriculture in the decades that followed can be explained by the trauma of those years. The Stalinist dictatorship exploited agriculture. The agricultural surplus was supposed to finance industrial development, but the state's appropriation of the harvests, in exchange for very low pay, discouraged initiative and reduced agricultural productivity. Implementation was uneven and incomplete. Some estimates for the first five-year plans (1928–1932 and 1933–1937) indicate that 70% of the objectives were achieved. Despite the mistakes and shortcomings of centralised planning, by the eve of the Second World War, the Soviet Union had become a major economic power (Matés-Barco 2017a).

1.3.4 The impact of the crisis in Spain and Latin America

The economic crisis affected Spain with a certain delay and relative moderation, but with a greater intensity and extent than traditional historiography has maintained (Comín 2011a, 75). The 1930s were characterised by declining production, rising unemployment, and falling prices. Agriculture was affected

not only by falling prices, but essentially by falling exports. There was also a significant contraction in foreign investment and the return of a large number of emigrants. The protectionism prevailing at the time did not insulate the Spanish economy from the negative repercussions of the crisis on an international scale. Spain, even without joining the gold standard, acted in practice as if it belonged to it, as the peseta had adopted the French franc as a reference and appreciated against those currencies that left the gold standard (Comín 2010).

The Spanish crisis at that stage was based on economic backwardness, which was manifested in the primacy of agriculture and the lack of integration of the sectors. The change of regime brought about by the proclamation of the Republic was not the trigger for the problems, but it is true that internal political factors had a "clear relevance and aggravated the economic crisis" (Comín 2011a, 76).

Labour policies resulted in the growth in wages during the socialist republican biennium, but in the following years they remained stable, especially in agriculture. On the other hand, political instability, already detectable since 1928 with the weakening of the Primo de Rivera dictatorship, undermined business expectations and reduced private investment.

In short, it is clear that the Spanish crisis was more superficial and shorter than the international crisis due to the rudimentary nature of the companies, their low level of financing, the predominance of the agricultural sector, and the relative isolation of the Spanish economy (Martín-Aceña 2004, 360–361).

On the other hand, traditional historiography has pointed to 1929 as the turning point in Latin America's economy. That year marked the shift from export-led economic growth to inward-looking development based on import substitution industrialisation. Structuralist economics has viewed this change in a positive light, while more traditional economics has considered it a lost decade. In any case, the transformation is evident. These years saw the emergence of novel economic, social, and political forces that brought about significant changes in the Latin American economy. Although export-led growth became more complicated in these years, the trend towards producing commodities was maintained and foreign trade continued to play a significant role. The total rejection of this export model took place after 1940, although it continued to survive in some small countries.

The onset of the 1929 depression is linked to the crash of the New York Stock Exchange in October of that year, but some signs arrived somewhat earlier in Latin America. One such sign was the rise in prices despite low demand. For example, the price of Argentine wheat peaked in May 1927, Cuban sugar in March 1928, and Brazilian coffee in March 1929. The boom in stock markets led to an excess demand for credit and a rise in global interest rates. This led to a rise in the cost of holding inventories and reduced the demand for primary goods exported from Latin America. In turn, there was a flight of capital seeking higher interest rates outside the region, coinciding with a decline in foreign investors, who also sought more attractive rates of return in New York, London, or Paris.

The collapse of the New York Stock Exchange triggered a chain of disruptions in the main markets supplied by Latin America. First, there was a decline in consumer demand due to the fall in the value of financial assets. The second problem was the credit crunch due to the non-payment of overdue debts and the resulting monetary contraction. Finally, importers were not replenishing stocks of raw materials due to falling demand and the lack of credit.

Prices of export commodities fell by more than 50%. An analogous situation occurred with imports, although the price level did not fall as rapidly. The decline in export volumes and the prices of exported products resulted in a rather dire situation for Latin American economies. However, there were some exceptions, such as Venezuela, which was protected by oil; and Honduras, which held out because of the banana companies that chose this country to establish their low-cost plantations. In other countries, the consequences of the depression were extremely hard because of the effects it had on mining producers in Mexico, food industries in Argentina, and tropical products in the central zone.

External debt – public and private – remained at a nominal interest rate and its repayment created serious problems for many governments. This scenario was compounded by a sharp decline in export revenues, which led to a drastic restriction on imports. Tax revenues from import tariffs fell sharply and generated a measure of collapse. The figures for Brazil are significant, as in 1928 it collected 42.3% of total tax revenue from import duties. Two years later, the same revenue had fallen by a third and tax revenue by a quarter. Chile suffered a similar situation because of its heavy dependence on export taxes.

Debt repayment also affected the balance of payments. Public spending was severely affected, to the extent that Honduran civil servants were paid in postage stamps. Most Latin American republics experienced changes of government during the depression years and, to a large extent, political parties or leaders who had been out of power during the Wall Street crisis were favoured. There were exceptions, however, such as Venezuela, where the autocratic government of Juan Vicente Gómez remained in power until 1935, or Mexico, exhausted by civil war and revolutionary turmoil, which was abandoned to the Nationalist Revolutionary Party. In the absence of credit, governments could not resist and even Argentina, with a degree of solvency on the international markets, was unable to obtain new loans. The impact of the depression, although very uneven, particularly affected Chile and Cuba. In the Chilean republic, between 1929 and 1932, GDP fell by 35.7%, while in Cuba per capita national income fell by a third in the same years.

Some countries withstood the onslaught of the crisis and mitigated its effects. Venezuela benefited from oil production with the lowest unit costs in the Americas. Peru, with exports dominated by foreign companies, managed to slightly mitigate the harsh adjustments. And the Dominican Republic, dependent on sugar exports, took advantage of not having signed the restrictive post-1929 sugar agreements.

1.4 Depression, spread, and solutions

The depression following the crisis of 1929 was very intense; it manifested itself in all its severity until 1932 and its repercussions spanned the entire globe (Accominotti 2011). The decline in economic activity in the United States had very serious repercussions: industrial production halved, and capital goods production fell by 75%. Private investment remained very weak throughout most of the decade and in 1937 was still 30% below its 1929 value (Figure 1.2).

The financial difficulties of farmers, who were unable to repay their loans, together with the fall in agricultural prices, led to the bankruptcy of a significant number of small banks. This negative trend in prices had been going on since 1919, worsened from 1925 onwards, and became critical after 1929, with a fall of 55%. However, the cost of living – which fell by 33% – did not keep pace with prices, so the situation of small farmers became increasingly burdensome. Agricultural production did not decline during the depression, but prices indicate the drop in domestic and foreign demand (Figure 1.3).

Unemployment became one of the clearest manifestations of the crisis. In October 1929, the number of unemployed in the United States was around 5 million and, one year later, it was close to 8 million. By the end of 1932, the figure had reached 12 million, and in 1933 the total was over 13 million. The unemployment rate was 27% of the working population of 48 million. In the autumn of 1932, there were about 6 million unemployed in Germany and in England about 3 million (Figure 1.4).

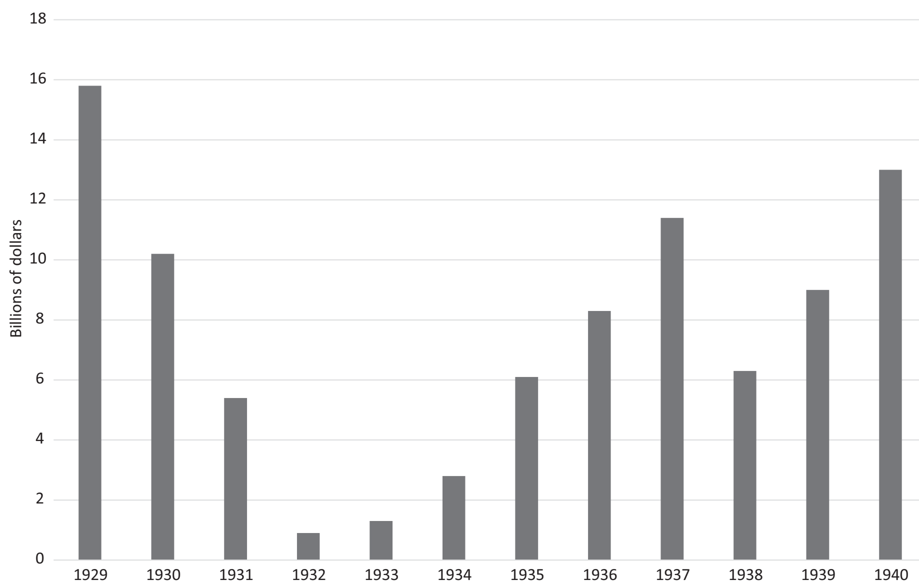

Figure 1.2 Gross private investment in the US (1929–1940) (billions of dollars)

Source: Prepared by author with data from Niveau (1989, 187).

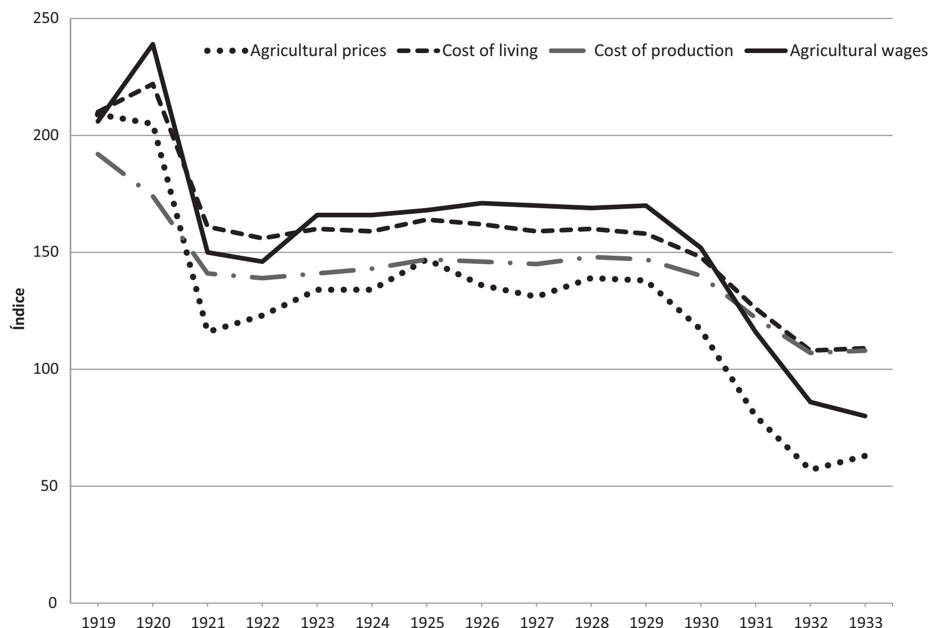

Figure 1.3 Indices of agricultural prices, cost of living, cost of production and agricultural wages in the United States (1919–1933)

Source: Prepared by author with data from Faulkner (1954, 627).

The fragmentation of the banking structure was one of the weaknesses of the US economy. It is interesting to note that it took several months to realise the "seriousness" of the situation. Despite the recovery of 1933 and the following years, it was not until very close to 1940 that the United States achieved full employment and the same volume of production as in 1929. After the good economic performance of 1937, a new crisis phase manifested itself. The depression of the 1930s spread to much of the world because of the size of the US economy and the economic relationships that existed between countries. In 1929, US industrial production accounted for 45% of world industrial output and its imports amounted to 12.5% of the world total (Figure 1.5).

The decline in international trade was somewhat less than that of world industrial production. Between 1929 and 1932, world industrial production fell by 37%, while the volume of world trade fell by 25% in the same years. Along similar lines, falling prices caused the exchange value of goods to fall by 60%. The severity of the crisis in the United States, combined with uncertainty in other parts of the world, led to a massive return of capital. In 1929, foreign investments and imports totalled $7.4 billion. Just three years later, in 1932, this figure fell to 5 billion dollars, a drop of 32%. At the same time, the balance of trade fell dramatically, from 1.44 billion dollars in 1928 to 357 million dollars in 1933. From 1934 onwards, imports outstripped exports, resulting in a deficit of

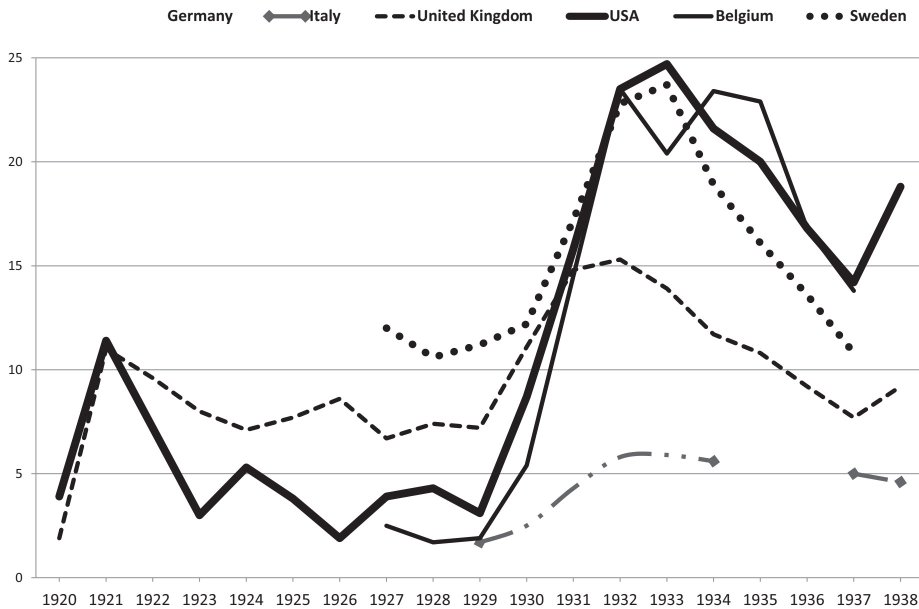

Figure 1.4 Unemployment rate in the United States and in various European countries (1920–1938)

Source: Prepared by author with data from Morilla Critz (1991, 132); Maddison (1991); Zamagni (2001, 162).

$740 million. In the following years, up to the Second World War, it exceeded $1 billion. It is clear that the decline in American global demand was enough to initiate a negative multiplier process in the world economy. For example, the fall in German industrial production from 1928 onwards was due to the outflow of American capital.

International initiatives to alleviate the crisis were few and, to a large extent, misguided. These included the creation of the Bank for International Settlements in Zürich on 20 January 1930. Its main task was to oversee the payment of war reparations. The moratorium imposed by Hoover, president of the United States at the time, and the definitive cessation of payments ordered by Hitler meant that it lost the function for which it had been created. The Swiss bank became a meeting place for central bankers, where international loans could be arranged. It played a key role in the training of economists with international skills, who joined the international organisations set up after 1945. It also excelled as a centre for the production of plans for the reorganisation of the international economic system. Vera Zamagni (2001) considers it to be a precursor in the functions of the European Central Bank and a place of informal coordination of the interventions of the central banks of each country.

Most countries dealt with the crisis by defending the domestic market and restricting imports. It is worth recalling the protectionist measures adopted by

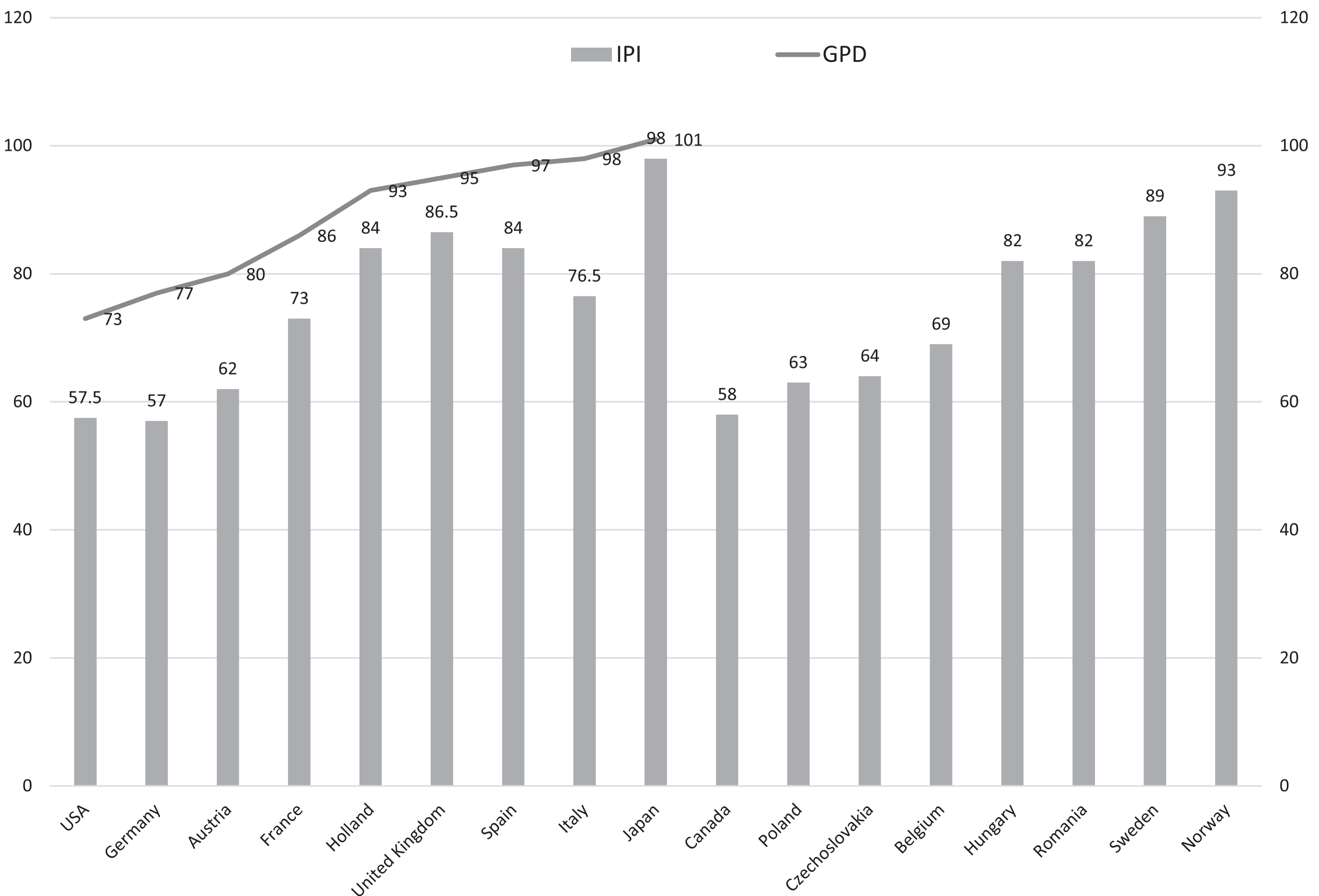

Figure 1.5 Index of industrial production and GDP (1932) (1929 = 100)

Source: Prepared by author with data from Zamagni (2001, 186); Niveau (1989, 187).

the United States in 1930 to curb the depression, especially the increase in tariffs to defend its agriculture. This practice quickly spread to industrial products. The Hawley–Smoot Act, passed by Congress, was a consequence of this economic policy. These measures were imitated by a number of other countries, and, in retaliation, they responded to these decrees by sharply raising tariffs. Although protectionist policies became widespread, there were also attempts to reach international agreements aimed at ending the economic crisis.

The collapse of the international monetary system, together with Britain's abandonment of the gold standard, only exacerbated the situation. The British government adopted tariff increases between late 1931 and early 1932. The chain reaction was not long in coming, and many countries applied quantitative restrictions on imports, a measure that restricted them as much or more than raising tariffs. The multilateral system of trade of the 19th century was disappearing. Faced with collapsing prices and agricultural overproduction, countries defended their agriculture by avoiding buying foodstuffs abroad.

Indebted countries and the least developed economies suffered the consequences of the fall in the prices of raw materials and, above all, in agricultural prices, which accounted for a substantial part of exports. To mitigate this situation, it became common for countries to devalue their respective currencies from 1929 onwards. In the Americas, this was the case in Argentina, Bolivia, Brazil, Venezuela, and Paraguay (Thorp 2002; Matés-Barco 2017b). In Europe, the most striking case was Hungary, but it also occurred in Australia and New Zealand.

To alleviate the effects of these measures, some states reached partial agreements of a regional or preferential nature, but which discriminated against third countries. The Oslo Convention (1930) bound the Scandinavian countries Finland, Belgium, the Netherlands, and Luxembourg. Similarly, in 1932, Great Britain and the Commonwealth countries signed the Ottawa (Canada) agreements, which established "preferential rights" between member countries.

In July 1931, in an attempt to alleviate the effects of the depression, exchange controls were introduced, a protectionist measure intended to stem the flight of capital. Attempts at international cooperation were rather limited, as most countries sought to increase their exports and limit their imports as much as possible. In effect, they had shifted into the practice of 17th-century mercantilism.

In the summer of 1933, the International Monetary Conference – sponsored by the League of Nations – was held and, after several delays, eventually convened in London. The purpose of the event was to take measures to alleviate the serious situation caused by the collapse of the international monetary system in September 1931. The meeting was intended to seek solutions, but it was very complicated because of the different ways in which each country understood its commitment to the gold standard. The United States left in April 1933; France and Italy stayed in despite little internal coherence. Germany was bound to remain by the dictates of the Treaty of Versailles. This disparate situation eliminated any possibility of agreement on a common public spending programme, on stabilising the respective currencies, or on reducing protectionism. The

conference ended with small, irrelevant agreements such as the price of silver or the sale of grain. These were poor results for an event that brought together 64 nations and in which the American lack of solidarity was evident in Roosevelt's words. The American president announced that his government's first measures would be those conducive to national reconstruction and that he could not enter into any international commitments that would interfere with that work. The meeting was a complete failure, demonstrated no willingness to pursue cooperative policies, and was the starting point for countries to devalue their respective currencies, adopt bilateral agreements, and strengthen their protectionist policies. International cooperation had failed, and the world was moving towards different, sometimes antagonistic solutions to overcome the crisis.

In September 1936, a tripartite agreement was reached between the United States, France, and Great Britain, with the aim of safeguarding international equilibrium and defending freedom of exchange. In turn, they were prepared to support each other's currency exchange for 24 hours. In this way, measures taken by a country whose currency was under pressure could take effect without causing any panic. For its part, the United States pledged to provide gold or dollars at agreed exchange rates if necessary. The declaration of intent called for the progressive elimination of measures that hindered trade relations between the countries. In fact, apart from a very slight lowering of tariffs or other similar provisions, this aim was swept aside by the recession of 1938 and by the Second World War. In 1944, at the Bretton Woods Conference, the Allied countries put the sad experiences of the interwar period on the table and tried to lay the new foundations of international trade. Between 1918 and 1939, economic practice had shown that the depression was exacerbated by protectionist and excessively individualistic measures (Feinstein, Temin, and Toniolo 1997).

The repatriation of American capital goes a long way towards explaining the impact of the crisis on Germany. Its policy of systematic deflation, fearing a repeat of the runaway inflation of 1923, intensified the slide towards depression. Germany remained on the gold standard and did not alter its exchange rate. Britain, for example, did the opposite: it devalued the pound in September 1931. Obviously, these issues greatly hampered German exports.

The "costs of poor international cooperation" were very high. On the one hand, the gold standard proved to be an excessively tight fit, making it difficult for a lender to emerge; on the other hand, the economic policies of individual countries, geared towards balanced budgets, only made the situation worse. The economic orthodoxy of the time was inadequate and the old policy mechanisms had become obsolete in a more complex and interrelated world, which required the application of very different parameters from those used at the time of the first industrial revolution. From an international perspective, the economy was in disarray, with a wandering and hesitant direction, which led to the emergence of economic blocs and the outbreak of a global conflict.

In the long term, the crisis brought about important changes for the future of the world economy: on the one hand, the increased role of the state, and on the other, the efforts of the least developed countries to create their own

industry to avoid dependence on the outside world. Nor can we forget the political repercussions, in particular the consolidation and triumph of fascism in several European countries.

1.5 Economic recovery and military rearmament (1930–1939)

The early 1930s saw the only period of economic stagnation in almost a century. International trade was largely paralysed by economic stagnation in many of the most advanced regions. The economic performance of the main European countries was uneven, not only because of the consequences of the 1929 crisis, but also due to the different measures adopted by each of them. The dramatic events from 1939 onwards, full of barbarism and violence, call for an analysis of the events that preceded them to provide a glimpse of the reasons that led Germany to the folly of the Nazi dictatorship. The exploration must extend to France to understand its unpreparedness for war, despite the obvious signs of its imminent outbreak, to Italy to elucidate its imperialist ambitions and its consequent alliance with Hitler, and to Britain, which was the only European nation to experience some measure of economic recovery. The picture for each of these economies was very different, but all needed American help to withstand the onslaught of Hitler's fury.

1.5.1 The United States and the New Deal

As mentioned earlier, attempts were made at international action to put the crisis to rest. However, reality revealed the deep connections between economic and political life, as well as the mistrust existing between some states. As a consequence of both, it proved difficult to find solutions that would please or suit all governments. Reactions to the crisis varied. In the case of the United States, a series of measures known as the "New Deal" were adopted, championed by then President Franklin D. Roosevelt. In order to deal decisively with this accumulation of difficulties, he developed an administration that applied a decidedly interventionist economic policy with the aim of combating the effects of the Great Depression. This programme was deployed between 1933 and 1938 with the aim of stimulating consumption and investment, reforming financial markets, and helping the poorest segments of the population (Romer 1992).

Broadly speaking, the first actions focused on money and credit, followed by the implementation of specialised policies in the agricultural and industrial sectors, with the aim of supporting prices and boosting the purchasing power of the population (demand policies). The first objective was "reflation", to raise prices, restore investor confidence, and give purchasing power to consumers. Two stages can be distinguished, the first in 1933, referred to as "FDR's First 100 Days", with measures designed to bring about a short-term improvement in the economy. The first provision prohibited the hoarding and export of gold (*Emergency Banking Act*). The second – the *Agricultural Adjustment Act*, and no

less important – gave the president extraordinary powers to force the Federal Reserve to extend credit, to devalue the dollar to 50% of its gold value, and to authorise the minting of silver coins in unlimited quantities. With these laws, the president could create as much "inflation" as he saw fit. In October 1933, the dollar was devalued in order to encourage exports and raise domestic prices. The third major measure was the Banking Act, aimed at solving the structural problems of the banking system and protecting depositors by creating a Federal Deposit Insurance Corporation. This law prohibited the granting of credit to finance stock market speculation. The economic results were modest, but the situation improved (Figure 1.6).

In June 1933, one of the most characteristic measures of the intervention programme was implemented: the National Industrial Recovery Act (NIRA), which brought together a series of regulations that were very advanced for the time. Its main objective was to revive the economy by preventing overproduction and developing codes of free competition. In addition to guaranteeing decent living wages, it aimed to ensure that companies made reasonable profits and, above all, that they respected the rules of competition, good business practices, and the elimination of "piracy" or dishonest behaviour. The government sought to raise prices, reduce working hours, and increase wages. The plan authorised the financing of $3.3 billion worth of public works. The great achievement of these years was the Tennessee Valley Hydroelectric Plan, which improved agriculture, industry, and navigation on its rivers. Everything was

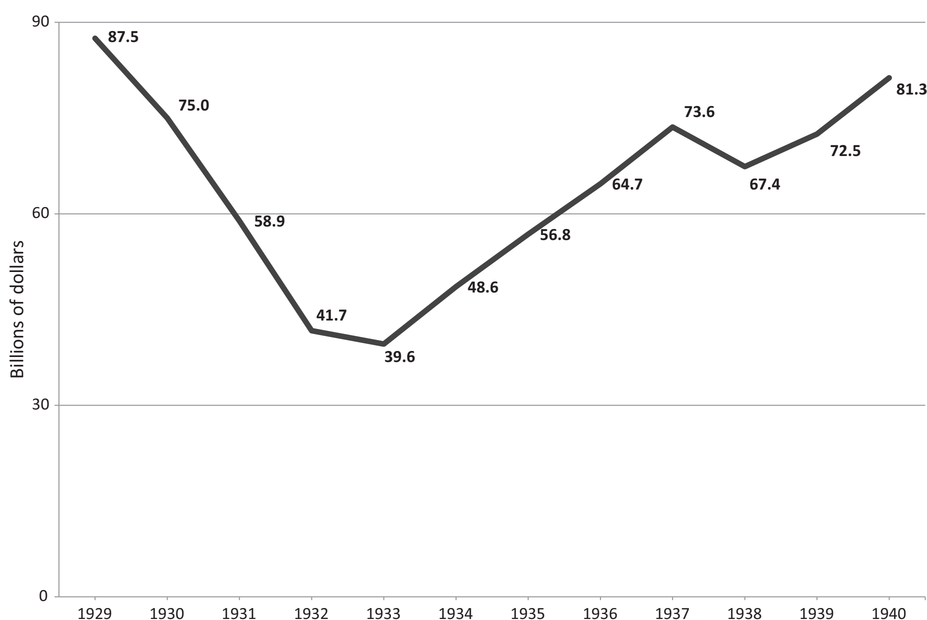

Figure 1.6 US national income (1929–1940)

Source: Prepared by author with data from Niveau (1989, 187).

organised around a public entity – the Tennessee Valley Authority – which built factories and dams, introduced irrigation, repopulated some lands, etc. The great public works programme was not replicated in other parts of the country. Despite its achievements, in May 1935, the Supreme Court declared the NIRA unconstitutional because it blocked antitrust laws that sought to defend competition. In essence, it was a system of private economic planning with government oversight to protect the public interest, guaranteeing the right of workers to organise and bargain collectively. Although it was not his intention, Roosevelt encouraged the formation of monopolies with the New Deal and the concentration of economic power.

To boost job creation, the Federal Emergency Relief Administration was created in 1933, with a budget of 500 million dollars to help the unemployed. Along the same lines, the Public Works Administration was established, which received an appropriation of 3.5 billion dollars to carry out public works and provide loans to state entities for infrastructure improvement and job creation.

Between 1934 and 1936, another important set of economic measures was adopted to modernise the agricultural, banking, and financial structure. The Agricultural Adjustment Act contained a number of monetary provisions and included subsidies for farmers who chose not to plant on part of their land. In 1936, this law was declared unconstitutional. In response, the federal government began paying farmers to grow legumes and grasses on former cropland to regenerate the soil. Between 1932 and 1939, the reduction in the number of farmers reached 7%, and the decrease in the area cultivated with cereals, cotton, and tobacco amounted to 20%. This agricultural policy was quite expensive for state coffers and did not achieve very positive results.

The economic policy represented by the New Deal has been widely criticised. At first glance, what was achieved between 1933 and 1939 was not very significant: unemployment remained high, and investment did not recover to 1928 levels. Private investment was low and public spending was not able to cope with the needs of such a large country (Figure 1.7). The depth of the depression was severe, and a policy based on budget deficits was not sufficient to overcome such a difficult situation. But a closer look shows that the measures taken helped to increase aggregate demand and slow its decline. In the absence of public spending, the depression would have been even more intense.

In the history of capitalist development, the New Deal represents an experience of state intervention, which acted at a very complex juncture and tried to undo outdated structures. Moreover, in the social field, Roosevelt's plan was beneficial because it was very humanitarian. Aid for the unemployed and benefits for the most disadvantaged social groups allowed economic activity to continue, not to mention the attention given to some fundamental areas of the American economy and society: social security, health, housing, natural resources, transport, and communications in general. It is difficult to make an overall assessment of the New Deal, but it is clear that the state had to intervene in the extremely critical situation in which the United States found itself at the beginning of the 1930s. Unemployment did not disappear, and the economy

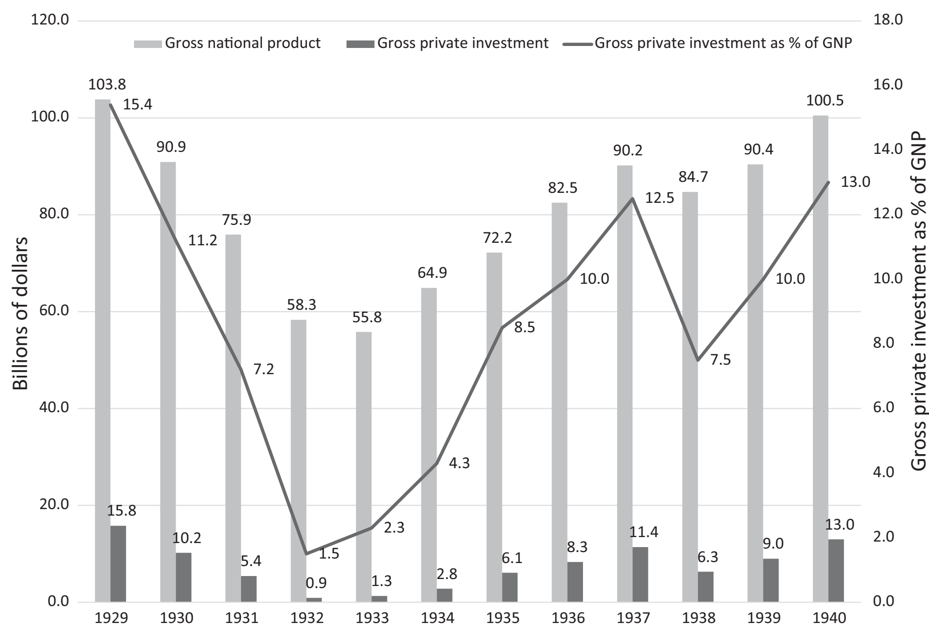

Figure 1.7 Investment in the United States (1929–1940)

Source: Prepared by author with data from Niveau (1989, 187).

was not sufficiently revived, but it did help to alleviate the crisis. Overall, although the legislation and the measures adopted were not entirely successful, they did lead to an improvement in the purchasing power of industrial workers and farmers, as well as to a clear economic recovery.

1.5.2 Britain: the effects of abandoning the gold standard

In Europe, the problems were approached somewhat differently. While the United States had more influence in the rest of the world, Britain was losing ground in international trade. British governments, while adhering to liberal principles, gradually curtailed free trade policies. After abandoning the gold standard in September 1931, Britain looked to protectionist formulas for economic support from the rest of the British Empire. The pound sterling suffered sharp devaluations, against not only the US dollar and the French franc (around 30%), but also other weaker currencies, albeit to a lesser extent. In 1932 and 1933, the average devaluation was between 13% and 9%. Compared to other countries, this devaluation was a major benefit for the British economy, as the stagnation of international trade allowed for some movement in British exports. At the same time, the abandonment of the gold standard made an expansionary monetary policy possible, with low interest rates encouraging

investment. Construction and industrial production experienced remarkable growth, which put Britain in an economically advantageous position.

There are essentially two reasons for the high unemployment figures. Firstly, there were the structural features of the British economy itself, which led to the rationalisation and integration of companies through mergers. For this reason, investment shifted towards new manufacturing and away from traditional British industry, where unemployment was particularly concentrated. The second reason was the lack of a Keynesian fiscal policy, i.e., there was no expansion of public spending until 1938, when Britain began its rearmament policies (Fishback 2010). Alarming signals from Germany put the British economy on alert and war industry production was supported. In any case, the imbalance was evident and could only be countered with help from the United States.

The shift towards protectionism was another important change in the British economy in this decade. The stagnation of international trade in the 1930s led Britain to abandon its leadership as an advocate of free trade, although it maintained preferential treatment for Commonwealth countries, which was ratified in the Ottawa Treaty. This allowed Britain's foreign trade to be oriented towards the colonies, to the extent that they accounted for 50% of its exports and 40% of its total imports. This level of exchange was based on the enormous privileges granted to the colonies and was the beginning of the future process of decolonisation. The share of exports in national production fell from 33% in 1907 to 27% in 1924 and only 15% in 1938. In the same year, exports to Europe were around 30%, a percentage that fell to 20% after 1945. This decline was largely due to the severe impact of decolonisation on the British economy and the lack of interest in the process of European integration. The British government issued regulations – the Special Areas (Development and Improvement) Act (1934) – to help the mining regions of South Wales, Durham, and southern Scotland. The textile industry in the Lancashire district and the shipbuilding industry suffered a similar situation. Unemployment in these areas ranged from 30% to 60%. Migration to London, the southeast of England, or the former colonies was common in these years. At the same time, economic aid was granted to companies setting up in these areas and interest rates were kept low to facilitate investment.

1.5.3 France: crisis and defeat

France sustained its economy at acceptable levels in the years following the crisis, and its most acute manifestations came late. The consequences were not particularly severe, but they lasted longer and did not bottom out until 1936. When international war broke out three years later, in 1939, the French economy was even more shaky. Its low unemployment rate, large gold reserves, and economic dynamism in the 1920s enabled it to withstand the first onslaughts of the recession. A series of governments adopted a range of mostly ineffectual measures, and, as in other European countries, the economic turmoil sparked social protests.

After the devaluation of the pound sterling, France's income from tourism and exports fell sharply. Until 1936, the devaluation of the franc was avoided, and a restrictive monetary policy continued, which led to progressive deflation and a reduction in prices and wages. Although later than in other countries, the crisis also eventually reached France. Rising unemployment, falling prices, declining wages, and shrinking corporate profits were widespread. Several credit companies went into crisis: Banque Nationale du Crédit, Banque d'Alsace-Lorraine and Crédit Foncier du Brésil. Bankruptcies multiplied and savers lost their deposits. Scandals hit the headlines and exposed the deceitful collusion between politicians and big bankers. Increasing risks of devaluation led to the outflow of large amounts of capital and gold. The chaotic situation led to the rise to power of a left-wing government – supported by socialists and communists – headed by Léon Blum. The triumph in 1936 of the Popular Front, under the leadership of Blum, a veteran socialist, marked a shift in French economic policy, which was inspired by Roosevelt's American experience. The change was based in particular on the theory that explained the crisis in terms of public underconsumption and envisaged recovery through increased purchasing power. However, the objectives achieved by the Popular Front were of the same tenor as its predecessors.

The first measures of the new government were aimed at raising wages and reducing working hours. These wholly inadequate measures led to the export of capital and forced the inevitable devaluation of the French currency. The situation remained unfavourable because of the absence of investment and the inability to inject measures to boost recovery. In June 1937, Léon Blum asked parliament for exceptional powers, which were denied. Political paralysis continued for a few more months with short-lived governments, until April 1938. The Blum experience was notable for having practically eliminated unemployment, although it did not increase the level of production to any great extent. In 1937, at close to full employment, national output was 82% of what it had been in 1929. There were several reasons for this situation: the 40-hour working week, the return of industrial workers to the countryside, and demographic stagnation. In May 1938, Édouard Daladier came to power and put Paul Reynaud in charge of the economy. The change in economic policy was evident in the repeal of the measures taken by previous governments. To this end, investment incentives were approved, a vigorous military rearmament programme began, and industrial production returned to growth. However, the German attack in May 1940 could not be met with sufficient strength, and France found itself devastated and subdued in a brief military campaign lasting only 40 days.

1.5.4 Germany: Hitler and rearmament policy

Germany, in order to pull itself out of the economic crisis of 1929, pursued extremely deflationary policies: taxes were raised considerably, and interest rates reached very high levels. Germany's precarious economic situation collapsed, and the public turned its back on the Weimar Republic. There were several

reasons for this breakdown that explain the difficult situation in which Germany found itself. The first is that the collapse of the German economy inevitably led to the cancellation or suspension of war reparations, with all that this entailed for Germany itself and for creditor countries. A second aspect, no less important, is that the Treaty of Versailles imposed conditions that prevented the devaluation of its currency (the mark). However, in July 1931, exchange controls were introduced that insulated the mark from the effects of its appreciation against other devaluing currencies. The third issue was that, since 1928, there had been no foreign capital inflows into Germany, which meant that war reparations had to be paid out of the balance of payments surplus. To achieve this goal, a very restrictive economic policy had to be pursued. Other, no less relevant issues show how a revaluation would have increased the real weight of the debt; or the role played by wages, which were inflexible downwards due to the power of the trade unions and would have made fiscal policies largely ineffective. Ultimately, what is important is to highlight how complex it was for alternative policies to emerge that would improve Germany's problematic situation (Schnabel 2004).

Several measures shaped German economic policy throughout 1931. First, domestic prices were lowered, wages were cut (by up to 15%), and exchange controls were introduced in order to stem the exodus of capital. Nevertheless, the German economy was still floundering, and in 1934 it remained at a lower level than in 1929. To curb the external imbalance, the government introduced import licences, tighter controls on capital outflows, and bilateral agreements with other countries.

Prime Minister Brüning and then Von Papen, who succeeded him in 1932, attempted to revitalise the German economy, but the failure of the extremely restrictive policies brought the Weimar Republic into disrepute. At the end of 1932, the Nazi party achieved great electoral success, which was the preamble to Adolf Hitler's seizure of power in January 1933. Studies on the subject have clearly pointed out the malevolent connection between one action and another, as well as their knock-on effects. On the one hand, there was the disastrous policy of war reparations with hyperinflation and the destabilisation of the German economy; on the other, the ensuing economic crisis, the rejection of restrictive policies, and the search for dictatorial solutions based on revenge and violence.

Germany was the first industrialised nation to achieve a full recovery, largely through the implementation of a systematically managed economy after Hitler came to power. One of the main goals of Nazi economic policy was to make the German economy self-sufficient in the event of war. Thus, they directed their research investments towards the development of goods that could be manufactured with the raw materials available in Germany. Trade agreements with countries in eastern Europe and the Balkans were strengthened, which encouraged the exchange of German manufactured goods for raw materials, thereby averting the outflow of foreign currency. Investment in sectors such as transport and construction was also bolstered. During these years, for example, the Volkswagen company emerged as the flagship of the German industrialisation

process. In this line, there was a notable increase in public spending: in 1928 it accounted for 15% of national income, in 1934 it was at 23%, and by 1938 it had reached 33%. Between January 1933 and December 1934, the number of unemployed fell from 6 million to 2.6 million. State aid to enterprises in the form of subsidies was very high. These facts reinforced the popularity of the regime, which directed all productive effort towards a war economy.

Rearmament began in 1936 and was intensified from 1938 onwards. The government directly controlled part of the resources through the "priority markets" and left the other part to the market. Hitler's aim was to build up a stockpile of armaments by promoting the war industry, which would allow a blitzkrieg, as he did not consider it appropriate to take resources away from the private economy and civilian industry. However, the forecasts were not realised because of Göring's ineffective leadership and Hitler's decision to attack Poland ahead of schedule. Nevertheless, the Allied powers and the world were impressed by Germany's massive war effort.

The autarkic economic policy was another of the practices that prompted rearmament. It had a certain importance in the chemical industry to produce substitute materials, although dependence on other countries was very great in oil, iron, and metals needed for the aircraft industry. Hitler also promoted the economic exploitation of some central European countries, especially with the annexation of Austria (1938) and Czechoslovakia (1939). The creation of a "living space" through hegemony in other countries was of no particular significance, although trade in these areas improved somewhat. Imports from countries such as Spain, Italy, Yugoslavia, Bulgaria, Romania, Greece, and Turkey rose from 9.8% in 1929 to 18.7% in 1938, and exports from 11.2% to 20.8% in the same years. Although the increase is substantial, it was not sufficient to cover the colossal raw material needs of the German economy.

In short, Nazism used the economy for its war aims, although it did not achieve the levels of efficiency it sought, nor did it manage to synchronise the rhythms of production with military operations. It is true that it set in motion a powerful, technologically advanced war machine that had the whole of Europe on the ropes; but its "energy Achilles' heel", the resistance of Stalin's USSR, and the entry of the United States into the conflict thwarted its chances of victory.

1.5.5 Stabilisation policies to curb the crisis in Latin America

Latin American governments had to take measures to stabilise the economic situation and cope with the impact of the depression. First, they had to withstand the decline in capital inflows and the fall in export earnings; and second, they had to cope with the contraction in tax revenues, which resulted in a large budget deficit that could not be financed from foreign sources.

It was thought that the adoption of the gold standard would automatically adjust the external imbalance. However, exports fell so sharply that after 1929 it was not possible to restore that balance. Gold and foreign exchange reserves fell particularly in those countries that tried to keep to the gold standard. In

Colombia they dropped by as much as 65%, and in other countries it was decided to abandon it – as was the case in Argentina in 1929 – or to limit the outflow by means of banking restrictions. Most countries created a system of import quotas. Currency devaluation was rarely practised, as few governments appreciated the severity and duration of the crisis. In 1931, the British suspension of the gold standard and the depreciation of the pound sterling meant that the currencies of some Latin American countries suffered a tremendous collapse against the US dollar. However, in 1933, after the suspension of the gold standard in the United States, the opposite effect occurred with a sharp appreciation of Latin American currencies. In any case, it forced the respective governments to seek solutions for the monetary system and exchange rates. In general, almost all of them tried to peg their currencies to the pound sterling or the US dollar.

Monetary policy during the depression was quite loose in many Latin American countries. Efforts to raise taxes, including tariffs, proved insufficient. Policies to reduce the budget deficit – due to the troubled social situation – leaned mostly towards debt servicing and ignored wage cuts, especially in the public sector.

Public investment was boosted by road construction programmes in almost all countries. The growth of the road network was very significant and contributed indirectly to the expansion of agriculture and the development of manufacturing. Private investment also saw a slight rise. Growth in private consumption fuelled industrial progress in the 1930s. The recovery in domestic demand was driven by the implementation of flexible monetary and fiscal policies, as well as by the recovery of the export sector.

The main change in the world trading system was the rise of protectionism. World trade had been growing steadily since 1932. For two years, the most industrialised countries reached a high level of imports. This trend allowed the exports of Latin American countries to remain at very stable levels. The big beneficiaries – Colombia, Nicaragua, Mexico, Bolivia, Chile, and the Dominican Republic – were the exporters of gold and silver due to the price increases in the 1930s. There were also some exceptions such as Honduras, Cuba, and Argentina.

The recovery of the export sector, in both volume and monetary value, contributed to the growth of Latin American economies in the 1930s. This revival led to an expansion of domestic demand that enabled the non-export sector to increase its presence in the respective countries. Agriculture and manufacturing were the main beneficiaries of this orientation, but sectors such as construction and transport also benefited. Argentina saw a significant recovery in GDP, despite the lack of export growth. This was largely because it had a larger industrial structure than the other countries and manufacturing was a major contributor to its economy.

The industrialisation of these years brought about a significant change in the composition of industrial production in the different countries. Processed food and textiles were the most important branches of manufacturing, but several new sectors came to the fore. Among the latter were consumer durables, chemicals and pharmaceuticals, metals, and paper. The market for industrial products

diversified and domestic consumption expanded into basic supplies for other industries. Nevertheless, by 1939, industry's share of GDP remained modest.

On the other hand, the protectionism that preserved the domestic market did not make it easy to overcome the many inefficiencies in industry so that it could compete abroad. At the dawn of the Second World War, it was still small in scale, with a limited number of workers per establishment. Labour productivity was also quite low, well below that of the United States, and most of it was employed in food and textile production. This low output was due to a shortage of electricity, a lack of skilled labour, restricted access to credit, and the use of antiquated machinery.

The financial system in Latin America did not undergo substantial alterations, but did see the creation of new central banks, the expansion of insurance companies, and the growth of secondary banking. Its stability is striking, which was due to the close relationship between banks and the export sector.

Latin America's recovery in the 1930s was relatively rapid. By 1932, Colombia had recovered its GDP level to that of 1928. Brazil achieved the same in 1933, Mexico in 1934, and Argentina, El Salvador, and Guatemala in 1935. Cuba and Chile did not reach 1928 levels until 1937 because of the severity of the crisis they suffered. Honduras, due to the successive banana export crises, did not recover its economy until 1945.

The economic policies developed in those years by the respective governments had a certain degree of success. The incompetence of many of the leaders was compensated for in a few ways. First, there was the emergence of a remarkable group of well-trained civil servants and economists who were in charge of fiscal and monetary policy and were able to make decisions in a relatively apolitical context. Second, the relative incidence of inflation was not a serious problem during those years.

1.6 By way of conclusion: a final assessment

Between 1929 and 1939, the European economy was very uneven and varied from country to country. Until the rearmament at the end of the decade, the policies adopted by governments were driven by domestic mechanisms and did not take into account a global perspective. The United States sought a solution to its problems through the New Deal, which led to a renewal of American policy and institutions, although it did not have a decisive impact on economic recovery.

The countries that made the greatest economic progress in this decade were Germany and Japan. The former because its productive recovery was based on high public spending, for example on motorway construction, and the latter because the crisis was very contained and the subsequent upturn very solid. Great Britain was at an intermediate level, with a rapid recovery, although without reaching the level of Japan and Germany. France and the United States were the worst performers, the US because it suffered a very severe crisis and France because it developed ineffective recovery policies. The economies that coped best with the crisis pursued expansionary monetary policies, and Germany

pursued an economic policy that was beneficial from all points of view. However, the United States adopted very negative and inadequate measures and did not develop its full productive capacity until it became involved in the war.

In addition, the study of the Great Depression of 1929 provides an insight into the economic developments since 2008. Both the US housing crisis – which turned into a global recession – and the European financial crisis of a few years later show parallels with the interwar period. There are commonalities in both crises: the role of financial fragility, the propagation of the crisis through fixed exchange rates, and the intellectual weakness of political leaders to foresee in advance the dark clouds that were looming on the economic horizon. To some extent, the lessons of the recovery from the Great Depression have been reflected in the measures adopted by various countries in the 2008 crisis, especially in expansionary policies, in both the monetary and fiscal spheres.

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