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**THE DEPRESSION AND THE FAILURE OF IMPERSONAL TRUST:
What Have We Really Learned from the Great Depression?**

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The Depression and the Failure of Impersonal Trust: What Have We Really Learned
from the Great Depression?

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The great crash of October 1929 did not spell the long-heralded end of capitalism. Nor, for that matter, did the yawning, decade-long Great Depression end it, any more than the War to End All Wars (a.k.a. WWI) end European Civilization, so called. Endism can be a bad habit if taken too seriously, which is to say when not used as a device to call attention to events worthy of it.

The Great Depression was one such capital event. If nothing exactly ended, plenty changed. But what? And with what, if any relevance for our own present circumstances?

Revisiting the Great Depression in search of lessons for the current crisis has become increasingly popular as of late, as a rash of books, essays, conferences and the like attest. A good deal of this searching has confined itself to technical analyses of monetary and fiscal policies. Some of it is avowedly partisan, if not more broadly ideological, in purpose; some of it even sounds like the speaking ghosts of reincarnated Republicans from Vermont and New Hampshire circa 1934, people who hated Franklin Roosevelt more than they claimed even to hate the devil himself. And a very good deal of it—practically all of it—misses the point. How we view that period had as much to do

with how leaders chose to portray their actions and how we reacted to those portrayals as much as to the specifics of the actions themselves.

What really changed then, and what may also be changing now, is the way the world's elite thought of themselves and their institutions. Above all, what happened in the early 1930s was a loss of trust in authority, specifically a loss of faith that the institutions that ordered society could be counted on to provide stability and enable prosperity for those willing to work for it. The great western idea that suffered the greatest damage was the extent to which anonymous exchange with millions of strangers could be trusted to provide good outcomes without supervision or filtering.

This idea—essentially the idea of impersonal social trust—was the most dramatic accomplishment of industrial civilization's rise from the eighteenth to the early twentieth century. Perhaps the really big accomplishment of early modern economic growth was not (or not just) the Industrial Revolution, but the way in which the system of commerce in the leading western economies began to move away from highly parochial, narrow networks of personal exchange and came to rest on increasingly complex national and international commercial networks of impersonal exchange mediated by competition and a very Adam Smithian understanding that individual self-seeking gain between strangers could lead to enormous universal benefits. Of course, none of this existed in a pure form anywhere in the world. Everywhere, power and political rent-seeking, or nationalism or ethnic or religious factionalism, or sheer envy and spite interfered with and distorted the workings of this commerce. And human civilization from long before the Romans or the Chinese had worked to develop complex abstract forms to deal with ever more elaborate forms of trade and commerce. Nonetheless, western society had seen an

advance of the liberal idea that impersonal exchange, oftentimes exchange between legal fictions like the corporation making use of ever more abstract legal contracts and resting on a foundation of highly abstract finance, could supplant for the better the more limited kinds of cultivation and production for individual consumption, with limited trade inside a village or town that humans have been most comfortable with for most of human history. If the idea of money itself seems unnatural, where an item not necessarily desirable in and of itself serves as a stand in for the complex wants and valuations of untold individuals, how much more difficult to grasp was an international finance founded upon ever more complex forms of financial exchange used in turn to motivate and support ever larger and more complex organizations locked into complicated contracts that not only brought items from around the globe to the homes of middle-class European families, but so multiplied the possibilities of production that new inventions could be integrated into reliable mechanisms for delivering more food and clothing to people from all walks of life. People, it must be remembered, who were increasingly divorced (especially in the largest cities) from the farms that grew their food, the factories that made their goods, and especially from the financiers who negotiated the deals that made this web of trade possible.

The rise in western prosperity and the promise of global participation in this new and abundant world seemed for some proof that petty politics, and especially its ugly handmaiden, war, were throwbacks to a less enlightened, pre-liberal era that would recede into the background as economic progress continued.

In crude political form, this was encapsulated in the view retailed by Norman Angell that countries that traded with each other were too intertwined to go to war. But

at a more general level, it was part of the general faith that trade, market competition, and the gold standard had produced a system of impersonal exchange that made large-scale, uncoordinated cooperation possible, productive, and reliable. The common man did not worry about such high and mighty notions, but to the extent that he moved from trusting the corner grocer to relying on national suppliers or from worrying about the trustworthiness of individual bankers to trusting a currency or banking system backed by a larger, more diffuse international system held together by gold and the faith that governments and bankers managed that relationship properly, he served as a brick in the edifice of modern political economy.

I don't mean political economy in the traditional sense of the science of politics and economics but in the sense of an intertwined economic system mediated by political agencies and sustained by beliefs about how states should interact with private individuals. If the world was (materially at least), almost unambiguously better at the beginning of the twentieth century than it had been a hundred years earlier, this led to expectations about how progress should continue that were unwarranted, producing severe reactions due to failed hopes.

If markets had come to play a more prominent part in the industrial West, it was not because markets had just been invented. It was because social and political systems had evolved in which powerful elites were willing to tolerate institutions that diffused economic power and weakened the state at the expense of private enterprise. If they had done so grudgingly (because of the pressures of a more powerful citizenry) or willingly (out of a sense of the rightness of freer trade) was less important than the simple fact that it is easier to support a system when you are doing well and can see your self as doing

better in the future. And despite the many imperfections and even injustices of the western capitalist system, greater numbers of people in all walks of life were markedly better off than at any time in human history. But that simple progressive narrative seemed to come to a halt in the twentieth century.

The years from 1914 to 1929 would already have been accounted among the most turbulent in western history had there been no Great Depression. The War to End All Wars had devastated Europe and left the major powers much poorer and much weaker than before. The triumphs of the previous century and the era of the long peace of the Pax Britannica had come to an end. The U.S. was politically a beneficiary of this transformation, moving from a net debtor to a net creditor. Moreover, having played a major role in deciding the war, without having suffered directly from it, the U.S. emerged as the leading economic and political power of the twentieth century. Even then, America was not without its challenges. A severe depression in 1920 saw industrial production fall by about 25 percent and the Bureau of Labor's wholesale price index fell by about 46 percent from 1920–21. Unemployment rose from about 560,000 in 1918 to 5,000,000 in 1921. Nonetheless, this severe contraction was short-lived and recovery was swift beginning in 1922. The Federal Reserve is credited with fueling the recovery with easy credit and the purchase of government securities. In addition, proposals by President Harding to substantially roll back taxes on the wealthy which had been initially raised to fund the war were eventually enacted during the Coolidge administration.

The boom that followed from 1923–1929 was one of the most sustained and impressive in U.S. history. This was truly a golden age, with rising GDP, vastly increased investment, stable commodity prices, rising real wages, modest unemployment,

a booming stock market, and important technological advances in many areas. Ownership of new products like cars, trucks, radio and other household appliances spread throughout the general population. Credit innovations—most especially the spread of payment on the installment plan—contributed to expanding household consumption. The ability to borrow and increase consumption in an orderly and even banal fashion seemed to belie standard intuitions about avoiding debt or constraining one's purchases to the level of current income. Buying capital goods with money one did not yet have quickly went from evidence of imprudence to something well within the range of good bourgeois behavior.

Federal, state, and local governments used growing incomes to fund public infrastructure in the 1920s that saw expansion in electrification, highway construction, and in telephone lines. The stock market, following a slump in 1921 saw a remarkable run up in the decade with the Standard and Poor's Index nearly quintupling from its 1921 low to a high in September, 1929. This too was jointly bolstered by the optimism surrounding overall economic prospects as well as new opportunities for buying stocks on margin. Nonetheless, dramatically raising margin requirements in 1929 did not seem to have dampened the observed demand for stocks substantially.

The crash of 1929 and the subsequent economic slump and prolonged depression therefore took most contemporaries as a complete surprise. Indeed, the uniquely severe catastrophe of the 1930s is so unusual that modern analysts should perhaps be more cautious than usual when drawing lessons from this period in the present day. The stock market peaked in September, 1929 with the Dow Jones average falling within a month by 17 percent. An initial recovery is misleading and is followed by a crash in October.

Subsequently, the Dow will show steady declines until the market has lost some 89 percent of its value by the time it hits bottom in 1932. Within the first year industrial output falls 12 percent from its 1929 peak, falls another 21 percent in 1930 and in total would fall by almost half from 1929 to 1932. GNP will eventually fall by a third in three years and unemployment would hit a high of some 25 percent. Though the timing abroad is slightly different, much of Western Europe is also hard hit and throughout the early 1930s, most of the western world suffers through the worst global economic downturn in the modern industrial era.

Much has been written about the transformations that occurred during that period and their impact on the modern world. But what is most striking is the contrast between what we may refer to as the “popular view” of Depression-era political economy and the consensus view of the economics profession and of specialists in economic history. There is a wide gap between the reality of the economic policies pursued by the American presidents and the way those policies were promoted to the public.

Conventional wisdom tends to treat President Hoover as a clueless advocate of laissez-faire who refused to take action to stimulate the economy in the middle of the dramatic downturn. In contrast, Franklin Roosevelt was the heroic leader who transformed the American economy through his promotion of the New Deal and expansive government programs that provided the necessary stimulus that pulled the U.S. out of the slump.

Yet this simplistic story finds little corroboration in the historical record. In point of fact, most of what both presidents did in the areas of fiscal policy did little to cure or prolong the Depression. Hoover was hardly advocating “do-nothing” policies. Indeed,

many of his interventions worsened the economy for precisely the reasons that orthodox theory would have predicted (such as his attempts to balance the budget by raising taxes in 1932 or strengthening support for the gold standard). On the other hand, he started the Reconstruction Finance Corporation to extend public credit to support failed banks, to fund public works, subsidize state relief, and otherwise engage in policy that might be seen to presage the more widely praised interventions of the Roosevelt era. Conversely, Roosevelt's interventions were neither as thorough nor as systematically revolutionary as they have often been portrayed, while economic historians have stressed that it was in the realm of monetary and not fiscal policy that FDR had the most success.

Though there is still a lively debate about the "true" cause of the Great Depression, there is now a strong consensus that a series of mistakes by the Federal Reserve (both of commission and omission) were responsible for turning what was a bad downturn into an unprecedented catastrophe. The Federal Reserve's focus on curbing speculation in the stock market by restricting lending and its unwillingness to extend liquidity and expand the money supply in the face of a collapsing economy and a wave of bank panics in the early 1930s is seen by almost all specialists as the major culprit for aggravating the severity and extent of the downturn. Monetarists such as Friedman or Schwartz note that the Fed did not ease monetary policy as expected and indeed never engaged in sufficiently expansive policy throughout the critical crisis period of 1929–33. Allan Meltzer has argued that this stemmed from a failure to distinguish between real and nominal interest rates because in a period of rapidly increasing deflation, even "low" nominal interest rates might be equivalent to extremely high real rates of interest. Worse is that the Fed even raised interest rates in 1931.

Experts disagree about the benefits of Roosevelt's various fiscal measures, with some scholars even arguing that many policies worsened unemployment and slowed recovery. But both supporters and critics of the New Deal actually seem agreed that the net effects of the various fiscal interventions was extremely modest at best. Keynesians view Roosevelt's interventions as perhaps helpful but spending was so small relative to the problem that any effects on the economy were bound to be modest. Current chair of the Council of Economic Advisors Christina Romer wrote in her widely cited article on "What Ended the Great Depression?" (1992) that "unusual fiscal policy contributed almost nothing to the recovery from the Great Depression." She further added that this was "fundamentally due to the fact that the deviations of fiscal policy from normal were not large during the 1930s." Other critics have focused on the ways in which the regulatory interventions such as the NIRA (National Industrial Recovery Act) codes' attempts to regulate labor so as to increase wages and set minimum prices could only hamper any recovery, by encouraging inefficiency, cartelization, discouraging investment, and working against the price flexibility needed for a more rapid rebound.¹ Where supporters and critics are in agreement is that the single most important policy move on the president's part was Roosevelt's decision to pull the U.S. off the gold standard. By abandoning the gold standard and allowing the dollar to be devalued, Roosevelt effectively provided the monetary stimulus that the Fed seemed unwilling to supply and may be said to have been working against for much of the early 30s.

¹ See for example the discussion in Harold L. Cole and Lee E. Ohanian (2004) "New Deal Policies and the Persistence of the Great Depression: A General Equilibrium Analysis," in the *Journal of Political Economy*. For a somewhat mixed picture, see Fishback, Horrace, and Kantor (2005) "Did New Deal Grant Programs Stimulate Local Economies? A Study of Federal Grants and Retail Sales During the Great Depression" in the *Journal of Economic History*.

Until World War II, nothing that the Roosevelt administration did was to have as much of a benefit to the economy as the decoupling of the dollar from gold had in 1933. Indeed, so powerful was the rebound after abandonment of gold that many scholars who are not as convinced of the standard monetarist case against the Federal Reserve think that it is the gold standard itself that was to blame. The evidence we have is that the earlier a nation abandoned gold, the quicker was its recovery. For these scholars, it was adherence to gold that tied the hands of the Federal Reserve and forced the policy decisions that in hindsight we see as foolish and counterproductive.

Whichever version of events one prefers it is clear that the abandonment of gold coming in the first few months of Roosevelt's inauguration in 1933, industrial production spiked upwards, the stock market began a slow recovery, and GDP began to move upwards from its decade lows.

Indeed, modern day adherents of the view that the gold standard itself, and not insufficiently vigorous monetary action on the part of the Federal Reserve, was the true "cause" of the Great Depression tell a story that highlights the inadequacy of the gold standard system to deal with the many structural, often anti-market changes that occurred after the First World War.

The gold standard itself was originally a mechanism for smoothing financial exchange by limiting the state's power to inflate the currency arbitrarily. To the extent that this was also coupled to commitments to prudent budget policies, open markets, and forthright participation in the world capital markets, the nineteenth century financial system contributed mightily to that era's globalization. But as many economic historians have noted (e.g. Bordo and Rockoff, or Flandreau), it may not have been the gold

standard per se that was as important as the extent to which the adoption of the standard was part and parcel of a whole package of market-friendly, trust-enhancing, economic policies without which the standard itself would have been insufficient to promote trade and investment.

Economic historians who put special emphasis on the dysfunctional nature of the gold standard in the 1920s² stress the incompatibility between the rigidities of the financial constraints of the gold standard with the increasing lack of wage and price flexibility after the First World War. In this view, the full range of nineteenth century globalization, complete with market competition, open trade, and sound finance was lost in the 1920s. In contrast, the gold standard merely hampered adjustments at a time when the spread of unionism and more corporatist big business as well as more constricted world trade undermined flexible market prices. By adhering to the gold standard, countries that had already abandoned much of the nineteenth century market system clung to a formal symbol of that era in the hopes that it would buy stability and prosperity. Instead, by forcing governments to focus on the exchange rate and not on employment or output, nations under the gold standard were driven to deflate. Consequently the U.S. Fed raised interest rates in 1931 not because their views of monetary policy advocated higher interest rates in times of depression but because higher rates were deemed necessary to maintain U.S. commitments to gold.

For most observers, the difference between the gold standard view and more conventional monetarism will seem like the finer points of an arcane theological

² See Barry Eichengreen and Peter Temin, "The Gold Standard and the Great Depression" NBER Working Paper 6060, 1997.

discussion. What is relevant is that going off the gold standard was the one thing that experts agree made the most difference to promoting recovery.

Given the importance of financial and monetary policy in causing and aggravating the Great Depression, it is therefore striking how much attention was paid to the regulatory and fiscal dimensions of economic policy. Indeed, since Keynes' book on the General Theory did not appear until 1936, one might say that Keynes succeeded because he came up with a theory that justified the interventions that leading government figures had been independently moving towards.

Even then, one is struck by the prevalence of other policies in the 1930s that seemed to aggravate the problems of the Depression without in any way fitting neatly into the Keynesian or stimulus views of recession fighting. After all, what is one to make of the widespread popularity of protectionism and high tariffs throughout the Western World? Indeed, nationalist policies of every stripe, whether in the form of cartelization of industry in the U.S. or of more widespread regulation and control in Europe, especially in Germany, would not seem to be natural accompaniments of a neutral, technocratic view of recovery. And why would a policy oriented to stimulus and expansion see rising tax rates throughout the western world, with the U.S. in particular reversing the trends of the 1920s and raising top rates from a low of 24 percent in 1929 to a top rate of 79 percent in the late 1930s and then an even higher rate of 94 percent during the war?

Above all, what is interesting is how much of FDR's worst policies represent a repression of business, a distrust of competition, and in general, a disdain for the market that seems unprecedented, unhelpful, and in the end more universally popular than would seem warranted given their checkered histories of mixed success.

In some ways, this was not so much a break from normalcy as a return to the natural way of doing this. Large-scale systems based on anonymous exchange are a recent phenomenon. The system of orderly, global trade developed in the nineteenth century under the financial and political leadership of the United Kingdom and was backed by the gold standard produced growth and prosperity, but never inspired the kind of devotion that nationality and communal ideology more easily induce. Politically, the world had had only limited experience with democracy and market capitalism. The more common system—recently dubbed by Nobel laureate economist Douglass North and his colleagues John Wallis and Barry Weingast as the “natural state”—consisted of political systems with limited access to property rights and universal trade, reserved for elites who treated control of the political economy of the kingdom or nation as their reward for preserving the peace and limiting the outbreak of violence. This order—under which the entire world lived for most of human history and which today still represents the default for most nations has the advantage of both stability and compatibility with people’s intuitions. The West has so taken for granted the triumph of the liberal nation state that it is necessary to remind us of how fragile its origins were and how little loyalty a system grounded in decentralized trade commands.

The evidence we have is that people do not put their “faith” in large-scale systems of commerce. It is much easier to focus on political economy as a system of extended loyalties in which successes or failures can be “blamed” on individuals or groups which we either oppose or feel loyalty towards. Despite the prevalence of market behavior throughout history—in the sense that people will always truck and barter and competition always emerges in one form or the other.

In good times, economic systems are supported by inertia and a utilitarian compromise that appeals to the broad center. But challenge that success and one observes how shallowly that conviction is held. The American preference for the free market is neither as common nor as American as its advocates would have you believe. There may be a visceral support for individualism and self-reliance that shades over into a superficial affirmation of markets at times, but that can work against it at others. Moreover, there are always strong minorities in favor of a more communal, even socialistic approach to the economy especially among the elites, which serves as a complement to the populist pressures in segments of the public at large. Whatever the case may be, it is safe to say that there is much less of an attachment to some disembodied “market” than conventional wisdom suggests.

In contrast, it is very easy to find those who saw markets and the process of commercial integration that we now refer to as globalization as fundamentally wrong. This view was appropriately summarized by Karl Polanyi in *The Great Transformation*, where he noted that the “market economy if left to evolve according to its own laws would create great and permanent evils.” Writing in 1944, Polanyi was keen to attack the rise of the modern market economy and to welcome interventions that crippled it. Although modern economic history does not place much stock in his claims that till just a few centuries ago, markets and market forces played little role in most economies, he was correct in observing that everywhere states had tried to control markets and that the nineteenth century therefore represented a startling shift in the extent to which formal institutions were permitted to abet and encourage market competition.

Polanyi claimed that markets were unnatural to the way human beings tend to operate at the individual level when in fact, exchange and competition were pervasive throughout history. What was unusual were reasonable unfettered markets because unfettered markets were inimical to elites everywhere. The very unpredictability, openness, and yes, often instability of large-scale market systems meant that the ruling classes tried to constrain commerce and markets to ensure order and their social success. Indeed, one of the virtues of slow economic growth is its very predictability and stability albeit at a cost of widespread poverty and stagnation. If the nineteenth century showed that markets brought prosperity and an end to older political systems, the early twentieth seemed to demonstrate that the newer system did not guarantee stability, perhaps especially when governments thought they were most in control. Of course, the failure to regulate the market properly, or even to adhere to the regulations in place, brought still more calls for regulation and control, often in ways quite tangential to the specific problems of macroeconomic stability and financial safety and sometimes directly interfering the risk-taking essential to innovation and growth.

Seen as a reversion to older habits, the odd mix of regulation, make work, intervention, protectionism, nationalism, even (as in Germany) anti-Semitism, that were part of the western policy response to the 1929 stock market crash and the subsequent worldwide depression seem less like incoherent flaying in all directions and rather more like an international retrenchment in social relations as many spurned the system of abstract, anonymous, and international exchange that had been built up for more parochial, inward looking responses, sometimes to the point of destructiveness.

In the period just before WWI, merchandise trade—which is what people usually mean by international trade—was roughly an eighth of gross output. It took six more decades for such a high level of commerce to be attained again. Certainly there was no law which dictated that free trade, industrialization, the spread of markets, cosmopolitanism, and peaceful cooperation necessarily went hand in hand, but they certainly reinforced one another. Perhaps the mistake was in assuming that trade ensured peace or that growing markets guaranteed orderly progress and not just increased prosperity. Or it may well be, that the willingness to accept an international system reliant upon anonymous exchange, not centrally planned, and not beholden to any one national leader—no matter how much that system may have been influenced or distorted by no small amount of meddling, both good and bad—was not easily accepted by the bulk of mankind. Indeed, the severity with which people rose to tear up or overturn that conventional system, despite the unprecedented prosperity it had wrought seems a testimony to how paper thin support for liberal trading regimes has always been.

It seems odd that humans in their day-to-day interactions, think of buying or selling as the most natural of activities and when unprompted will recreate markets in the most dismal of circumstances. But something about the ideology of a market system, or perhaps even more vaguely, a generally decentralized order seems unthinkable, or perhaps literally inconceivable for most. Their support for the existing order seems predicated on only the best or most favorable of circumstances, which even under good times puts market under stress for the disorder and creative destruction that are unleashed as a necessary input towards wider progress. Let that progress falter or fail, and support for the system is quickly replaced by a need to assign blame and to personalize or

politicize the failure. In that sense, western markets are like western medicine, acceptable though unintuitive for most, but difficult to stomach unfettered when times are rough. Just as an outbreak of incurable plague would both lead to a renewed search for sound cures and an atavistic appeal to folk remedies and randomly seized superstitions, so did the Depression stimulate both new and productive thinking about the sources of business instability as well as harmful or destructive appeals to extreme nationalism, protectionism, and militaristic aggression in much of the western world.

Economists have a hard time dealing with the problem of nationalism. The essence of the Smithian insight, elaborated at depth in almost all of modern economics is that voluntary trade is mutually beneficially and hence specialization is the necessary road to riches. Indeed a corollary is that trade between people or nations with different preferences and capacities is especially beneficial. In difference is wealth. But this very difference runs up against the problem of Smith's historical predecessor and intellectual counterpoint—Thomas Hobbes. For Hobbes, the problem of political economy is the maintenance of public order. And that order has to run uphill against human beings tendency to engage in war and conflict. Hence, to the extent that people prefer those who are most like them, usually meaning those of similar ethnicity, religion, culture, or nationality, then difference can undermine order as easily as it promotes prosperity.

In short, people want action. Moreover, a severe crisis that affects all economic performance, no matter how narrow the source of the problem, leads to a reconsideration of, and often a loss of faith by the public of the entire political economic system itself. Since there is no clear idea of what constitutes the totality of this system, nor what its boundaries are, a crisis allows for a redefinition that permits targeting the blame in ways

that nurture long simmering fears and resentments. Furthermore, those with a vested interest in particular changes, whether narrowly venal or more broadly ideological, act in a way that does as little as possible to avoid profiting from crisis.

It is important to note that the managerial intervention of the Roosevelt era and the more dramatic centralization of the economy in Germany and other parts of Europe were different in degree but not necessarily in kind from earlier interventions in the late nineteenth century. Already there had been attempts to reimpose protectionism and reassert national control in Europe or to extend regulatory powers of the State in the U.S. Most of the leading anti-liberal movements—whether pushed by Populists or Progressives in the U.S. or the various forms of socialism in Europe took for granted that politics was needed to impose order and bring social harmony to an unfettered market economy. But the types of remedies that were tried and the zeal with which reformers sought to repudiate the past suggest that changes in the management of political economy were less of a technocratic revolution than a global transformation that was facilitated by the immediate necessity of responding to a crisis.

Indeed, although there is much that unites the fumbling mix of interventionist and managerial solutions tried by both Hoover and Roosevelt, it is interesting that Roosevelt's fumbles were greeted both during and after the Depression with greater forbearance to a large extent because he seemed to have a coherent vision that rejected the notion that all was well and that a change was needed.

Roosevelt was careful not to suggest that he was overturning the entire American economic system, nor did he nor his advisors feel that they were promoting anything as radical as socialism or fascism. But it is significant that he chose members of his famed

Brain Trust who were associated with a rejection of market competition and went out of their way to signal that the interventions were part of a new paradigm. Most prominent of these “critics” (whose ideas have done much to shape subsequent views of the economics of the Depression and on through the postwar period) was Professor Rexford Tugwell of Columbia, in many ways the point man for the Roosevelt Brain Trust. Tugwell’s writings stressed the failure of laissez faire and of market competition which he saw as outmoded. Tugwell strongly argued for increased concentration and regulation of business with especial encouragement to be given to expanded business size. In this, Tugwell not only gave his blessing to the recent industrial trends leading towards larger scale but backed the Rooseveltian desire to exploit public regulation and control both as a check on monopoly but also as a superior alternative to private enterprise. Thus, planning was to be a new mantra and, however different the National Industrial Recovery Act (NIRA) or the Agricultural Adjustment Act (AAA) were from the more radical state expansions in various parts of Europe, the new thinkers all shared the view that planning was good, inevitable, and modern.

Nonetheless, Roosevelt also deserves much credit for dealing in a pragmatic and forthright fashion with the crisis he faced. There was a very poor understanding of what was happening in the world by commoner and expert alike, the data often did not exist to properly understand what was happening, or in many cases the measures were relatively new to the economic profession and to the government. Systematic measures of gross national product and aggregate unemployment indices were for the most part innovations of the early twentieth century. But this pragmatism was tied to a spin that made the Rooseveltian interventions hated by some and widely lauded by others.

The Depression accelerated the worldwide trend to deprecate liberal democracy and market capitalism and to anticipate its imminent demise that had begun around the time of the Great War. Mussolini and the fascists had already been popular with many leading intellectuals before the rise of Hitler. To the extent that the elites were initially seduced by him, it was just as often because of, rather than in spite of his preference for planning and state control of industry and his apparent success in “organizing” Italian industry. The decisive fashion with which the Nazis seemed to deal with the German economy’s problems further contributed to the belief that a strong hand and direct government intervention in the economy were a necessary part of modern life. Indeed, it has long been conventional wisdom that the Nazis ran a more pervasively “Keynesian” policy of fiscal stimulus than did Roosevelt, if only inadvertently. Of course the fact that economic specialists today take a rather jaundiced view of earlier claims that the Nazis had engaged in effective economic fiscal expansion rather than papered over the cracks through regulation, militarization of the economy, and price controls does not change the way that those policies were viewed at a time and for a full generation after (see in particular the work of Albrecht Ritschl, who has written the most comprehensive takedown of the view that the Nazis were successful Keynesians). Thus, compared to the legacy of the nineteenth century, Roosevelt’s various attempts at fiscal expansion and regulatory control seem radical and groundbreaking. However, they seemed tame and even moderate relative to the most radical desires of either those favoring socialism and planning or relative to the more extreme hopes of Progressives. Indeed, even the orthodox socialists in Germany (the SPD) were discredited during the Depression because they had been arguing for something akin to *laissez-faire*. In their view of

orthodox Marxism, the turmoils of the interwar period were seen as part of the natural demise of capitalism, and intervention would only hinder the natural transition to a more just social order. In contrast, the Nazis' more forthright interventions and the wonders that Hitler seemed to bring to the economy provided him with support and respect both at home and abroad.

It is ironic that Britain's actions—where the state was far more conventional in macroeconomic policy than the U.S. have elicited so little commentary. Britain's recovery began earlier than in the U.S. for the simple reason that Britain abandoned the gold standard in 1931, some two years before Roosevelt. In addition, the government adopted a cheap money policy that is seen in hindsight to be the sort of policy that the Fed should have promoted with even more vigor. Unfortunately, the British, like virtually everyone else in the West, but unlike the Britain of the late nineteenth century, repudiated their views of free trade and turned to high tariffs and protection of home industry thus contributing to the worldwide decline in trade and global integration that not only depressed worldwide growth but contributed to the mood of autarky that was part of the rush to conflict and then war.

One important counterfactual to ponder: If FDR had only engaged in the most important financial policies that helped us out of the Depression, with fewer makework programs and less of an overarching rhetoric of a New Deal, while promoting faster recovery, would he be as celebrated today as he is? I think a prudent observer would have to say that the opposite is just as likely. An FDR who used no transformative rhetoric but who successfully managed a halting recovery using the language of Hoover would more likely have been less well-remembered. Very possibly he would have been

assailed for failed opportunity, and there would have been a greater eagerness to show where his policies had misfired.

If it was World War II that truly restored the U.S. economy, why do we not look to Truman as our savior? After all, at a time when many economists foresaw a deep recession after the war, Truman oversaw a period of rapid recovery that was much broader and more impressive than anything under Roosevelt. He did this while shrinking the government and dismantling regulations at a rate that Reagan could only have dreamed of. Most especially, he smoothly pulled us back from wage and price controls that could have easily been allowed to linger and by so doing moved us back in the direction of a competitive, open-access economy. Had there been a lingering recession and a continuation of older, harmful regulations, Truman would have taken the blame but not the failed policies of the earlier administration.

The critical problem for us is to ask, what is it that restores impersonal trust? Is it mere confidence? How much of it has to do with substantive rules and regulations? How much of it is tied to the rhetoric used by our leaders? The heterodox economist Hyman Minsky long argued that financial systems were prone to booms and busts and that regulation is needed to tame these excesses and to rein in the casino-like tendencies of the market. But to what extent can we have confidence that regulators will not only know what the right regulations should be but enforce them properly? The Federal Reserve of 1929, given its constraints of abiding by the gold standard may well have been limited in how they could respond to the crisis. Roosevelt's decision to abandon the gold standard would almost seem to have been an arbitrary judgment in hindsight. And one might argue that the strong role assigned to the postwar Federal Reserve to maintain the dual

task of stabilizing the price level and keeping watch on output and employment might well have contributed to the new crises we are faced with. Perhaps our best option is to bear in mind that we should always be guided by the understanding of how important yet unnatural the modern system of impersonal finance and trade really is and that we need to preserve that system as a basis for our prosperity. This will almost surely entail new risks, and many of the regulatory solutions that will be tried for our current crisis will themselves induce responses to circumvent or go beyond those constraints which will in turn generate new crises. But given the widespread fear and political pressures to pull back from the market that will wax or wane as crises deepen or fade, we may be able to do little more than remind ourselves that patience and prudence are as always, good watchwords for government, amidst the many trials and errors we will surely endure.