THE GREAT DEPRESSION & THE NEW DEAL
A Very Short Introduction

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In the spring of 1931 Senator Robert Wagner (D-NY) claimed that President Herbert Hoover had, in the face of crisis, “but clung to the time-worn Republican policy: to do nothing and when the pressure becomes irresistible to do as little as possible.”\(^1\) Hoover did not “do nothing,” but he did not do enough either. Instead he followed a general policy for crisis management he had already clearly established.

Indeed, when Hoover ran for president in 1928, Americans associated him with competence in a crisis. Some Republican leaders showed skepticism; Calvin Coolidge, whom Hoover served as secretary of commerce, complained, “That man has offered me unsolicited advice for six years, all of it bad.”\(^2\) But a new emergency had reminded Americans of Hoover’s virtues.

Rains swelled the Mississippi River early in 1927, and in the middle of April the levees near Cairo, Illinois, collapsed. Hundreds of thousands of acres disappeared beneath the water, and more levees burst. Coolidge, who had to this point preferred hopeful inaction, now appointed Hoover to head an emergency committee. A successful mining engineer, Hoover had gone into public service after making his fortune. During World War I, Woodrow Wilson made Hoover head of the effort to provide food and other relief to the war’s dispossessed, and Hoover earned a reputation as a
logistical genius. “He is certainly a wonder and I wish we could make him President of the United States,” Assistant Secretary of the Navy Franklin Roosevelt wrote in 1920.³ Hoover owed his reputation partly to his talent of organizing and using bureaucracy, and partly to his talent at organizing and using the press. “[T]he world lives by phrases,” he once said.⁴

As head of the 1927 flood-relief effort, Hoover showed both the extent and limits of these talents. He organized and managed evacuations, saving lives; he oversaw the establishment of camps to house refugees; he backed federal control of river management to forestall future disasters. Hoover also turned a blind eye as southern whites prevented black evacuees from leaving guarded camps lest the South lose its labor supply. And he used whites’ fear to his advantage, threatening local businessmen by saying, “I’ll send your niggers north starting tonight,” if they did not contribute money to a reconstruction fund.⁵

Like the engineer he was, Hoover could build a machine to solve a problem, but he expected someone else to operate it. He accumulated $13 million in funds for reconstruction loans and made sure everyone knew it, but he did not ensure that the money would get lent to the stricken area, and the vast majority of it was not. Further, although he favored massive federal spending on engineering improvements in river management, he opposed increasing the government’s humanitarian role, declaring, “No relief to flood sufferers by Congress is desirable.”⁶

As a prospective presidential nominee, Hoover knew he had to promise loyalty and attention to the habitually Republican black voters, without alienating potential white voters. He let African American leaders know he favored a reconstruction plan to subdivide the large farms in the flooded region into small plots for black farmers. But he thereafter declined to support the plan—or the black evacuees—in any substantial way.⁷ The flood gave Hoover the ability to claim that he could show grace
under pressure. Doubters were few, though sometimes acute: the Baltimore journalist H. L. Mencken wrote that Hoover’s “achievements all diminish rather than increase on analysis.”

For the 1928 election Hoover’s record turned out not to matter much. Hoover won not because of what he had done but because of what his opponent, Al Smith, was: a Catholic. Smith was many other things—most notably, governor of New York, in whose assembly he had also served. New Yorkers knew him as a progressive who had helped reform the state constitution and investigate the infamous Triangle factory fire. Smith had backed bills for workplace health and safety and against child labor. But his accomplishments and Hoover’s alike vanished amid a war of symbols waged with Hoover’s preferred weapons: phrases. While Hoover kept his distance from the worst slurs, his allies attacked Smith for representing the “sneering, ridiculing…foreign-populated city of New York,” for opening the way to “card playing, cocktail drinking, poodle dogs, divorces, novels, stuffy rooms, dancing, evolution, Clarence Darrow, overeating, nude art, prize fighting, actors, greyhound racing, and modernism.”

What in hindsight looks like a critical election—the choice of a leader for a period of profound crisis—turned on these insubstantial issues of cultural conflict. The election mattered for two major reasons: it left the Republicans in control of government on the eve of the Depression, and it put Hoover, who opposed public relief even in crisis and who believed in the power of phrases to shape the world, in charge of the federal response to economic calamity.

On October 25, 1929, the day after Black Thursday, Hoover told reporters, “The fundamental business of the country, that is the production and distribution of commodities, is on a sound and prosperous basis.” Hoover’s message was, in the *Wall Street Journal*’s words, “in harmony” with the leading bankers and
leading industrialists, who emphasized that “the break . . . was a technical one within the market and not based on fundamentals.” Hoover repeated his belief in the soundness of American enterprise, saying, “Any lack of confidence in the economic future or the basic strength of business in the United States is foolish. Our national capacity for hard work and intelligent cooperation is ample guaranty of the future.”

Hoover relied heavily on the idea of “intelligent cooperation.” He saw himself as cheerleader to American enterprise, not as a referee, coach, or player in the economy: he would call for teamwork and hope to see it produced. He invited important figures in American industry to meet, asking them to reason together, planning how to keep the crash from turning into a depression. He urged employers not to cut wage rates, and they agreed to cooperate.

Hoover went further still in his requests, asking state and local politicians to hasten and augment their spending on roads and other public works, believing that in various government treasuries there lay “a substantial reserve for prompt expanded action.”

None of these strategies required much action from anyone in the federal government, beyond uttering the occasional encouraging phrase. None provided any immediate relief to Americans. None cost the federal government money. All depended on people outside Washington, DC, to stop the disaster. None worked. The businessmen’s pledge to uphold wage rates said nothing about whether they would reduce hours or lay workers off, and they did both. As early as January 1930, Business Week reported that “Some automotive companies . . . discharged employees with what seemed precipitous haste.” Smaller employers, too numerous and minor to get an invitation to Washington, did not feel bound by the wage pledge. Accordingly, unemployment rose and overall wages dropped, even in cases where the nominal rate of pay stayed the same.

Nor were local and state governments able to respond effectively to Hoover’s plea. They spent some money on construction projects,
but as the crisis continued they had less to spend. Tax revenue fell and the bill for local poor relief rose. These two draining effects on local budgets forced local governments, by the hundreds, to delay, if not repudiate, their debt payments. These government defaults put pressure on another weak pillar in the Hoover plan: his dependence on what he called, in November of 1929, “[t]he magnificent working of the Federal Reserve system and the inherently sound condition of the banks.” This assessment proved faulty.

Since beginning operations in 1914, the Federal Reserve System had functioned like a central bank for the United States, regulating the supply of credit in response to economic production. Central banks were supposed also, as the British journalist Walter Bagehot wrote in 1873, to “lend freely” in times of economic crisis, forestalling panic.

But the officers of the Federal Reserve System had not established their own clear set of rules for intervening in crises. Some believed the system must act swiftly to forestall disaster; others thought that the system should keep its credit in reserve unless the need grew truly dire. The balance of opinion within the Federal Reserve rested with the anti-interventionists, as did the balance of opinion within the economic profession during the 1920s. Mostly, economists thought that an economy in crisis should be left alone and that weaker banks and firms should go under. They thought that during a boom period, some businessmen made poor calculations under the influence of excess optimism: they borrowed too much, produced, and stocked too much in anticipation of demand that would never materialize. Economists thought that these poor calculations helped bring on a crisis in the first place, and that the proper role of a downturn was to correct these errors of judgment. As the most popular basic economics textbook of the era said, “The period of depression, then, is one in which . . . production is kept at a low level until surplus stocks are disposed of, and new commitments are not made until there is
a reasonable assurance of profits. In other words, the period of depression, gloomy and unpleasing as it is, serves as a breathing spell for business[.]”19

Moreover, even had economists generally agreed on the need for intervention in time of crisis, the Federal Reserve’s officers would have had difficulty knowing just when that crisis had deepened to a point requiring their action. The U.S. government kept no regular statistics on unemployment or on total economic output, nor did it have a system of accounting for national income.20 Debate among Federal Reserve bankers often rested on anecdotal evidence or assumptions about what was happening in the economy.

In consequence, while in the immediate wake of the Crash the Federal Reserve System took some steps to make it easier for banks to lend and borrow money, after a few months it did little. Some of its members fretted over the relative inaction, noting that the depression seemed to be spreading around the world, particularly afflicting America’s debtors. In the spring of 1930, George L. Harrison, governor of the Federal Reserve Bank of New York, visited Europe and observed “a shortage of working capital, and thus a restriction of purchasing power, in a number of countries . . . affected by the stringent credit conditions prevailing last year.”21 Harrison believed the Federal Reserve would need to lessen restraints on credit, but a majority of the System’s governors disagreed.

The Federal Reserve’s caution worked together with the Congress and the president to bring the international economy to a near halt. On June 17, 1930, Hoover signed the Smoot-Hawley Tariff into law, raising taxes on imports to America. The idea for a new tariff bill had arisen in 1928 as a method of protecting American farmers, who were suffering a long bad patch, from foreign competition. By the time it passed, many farmers opposed its provisions, as did newspaper editors, some manufacturing executives, and a number of foreign governments that believed it
would cut the American market off from the rest of the world, with dire consequences. Members of the automobile industry, which accounted for 10 percent of American exports, were especially alarmed.22 A GM executive warned that “a creditor nation . . . must, if it hopes to preserve its prosperity . . . buy foreign goods of every possible description.”23 Thomas Lamont, a partner in the J. P. Morgan and Company investment bank, claimed he “almost went down on my knees to beg Herbert Hoover to veto the asinine Hawley-Smoot tariff.”24

But a higher tariff looked to other constituencies like a good idea. Republicans favored tariffs in response to economic complaint. They had used one in the postwar depression of 1921, and it seemed to work then. So they did it again, by partisan majorities—more than 90 percent of House Republicans voted for the bill, more than 90 percent of House Democrats voted against; in the Senate, 78 percent of Republicans were for, and 86 percent of Democrats were against.25

The aftermath seemed to prove the critics correct. In the years that followed, other countries retaliated by erecting their own tariff barriers, and world trade fell by one quarter of its volume. Blocking other countries from their American markets made it harder for foreign powers to repay their debts outstanding from World War I. As one writer explained in the New York Times, “there is not enough gold in the world to pay America; therefore America must be paid by loans from America and by goods sold in America.”26 With the restriction of credit in 1928, loans from America had begun to fall off, and with the restriction of trade in 1930, goods sold in America began to fall off. Payments to America would have also to fall off, as countries sought to protect their own citizens. Cutting down trade meant cutting down the international flow of borrowed money.

At the end of 1930, the difficulty of borrowing money finally took its toll. In the last two months of the year, bank failures imperiled
enormous sums on deposit, more money than suspensions had put at risk in the preceding year. Nor did the panicking end even then; the spasmodic collapse of the American banking system continued. During Hoover’s presidency, more than 20 percent of American banks went under.

The American banking system had, contrary to Hoover’s assurances, some inherent weaknesses. The laws of many states prevented banks from establishing branch offices. Banks with many interconnected branches, lending money in different places and to different kinds of borrowers, depended less on the fortunes of any single locality and could weather a crisis more easily, while unbranched American banks, or unit banks, failed relatively easily. States that allowed branch banking had stronger, more competitive banks that drove out or absorbed weaker banks. These states entered the Depression with a stronger, more stable financial system. Likewise, the Canadian banking system, with extensive branch banking, survived the Depression largely intact.

The Crash hit American banks hard. Some had made loans to fund speculation; others held foreign assets that went bust, as American loans overseas halted and other countries could no longer meet their obligations. But most important, banks suffered because their clients suffered and could no longer pay off loans or make new deposits in their savings accounts. Payment on loans and new deposits provided banks with their major source of income. As banks’ income dried up, they could not pay their own creditors. Increasingly they had to close their doors.

The Federal Reserve System, in keeping with the opinion of a majority of its members that the dying banks were a natural, if painful, part of the circle of life in modern business, did not prevent these failures or forestall further ones. Their inaction accorded with the prevailing orthodoxy of their day. But the prevailing orthodoxy of the 1920s defied the older, and tested, belief set forth by Bagehot in 1873 as well as the evidence before
them. Banks continued to fail, in great sickening waves of calamity, each closure sending new ripples of fear far and wide. Americans began to mistrust their banks altogether, which in turn made it still more difficult for banks to get credit.

Much the same could be said of Hoover: while he hewed to the respectable opinion of his day, he defied both the evidence of his senses and a longer-established tradition that cried out for action. And in consequence he too found it harder and harder to get credit as he might have in normal times. Early in October of 1930, Hoover emphasized the psychological causes of Americans’ troubles: “The income of a large part of our people is not reduced by the depression . . . but is affected by unnecessary fears and pessimism.” As to whether the government should take any action, he allowed it might cut the tax on capital gains, which would permit investors to keep more of their profits from trading. A few weeks later, on the anniversary of Black Thursday, Hoover quashed rumors that he would call Congress into special session to take action against unemployment. “No special session is necessary to deal with employment,” he declared. “The sense of voluntary organization and community spirit in the American people have not vanished.” Hoover’s belief in the power of encouraging phrases abided: Americans needed to believe, he thought, in the adequacy of voluntary, civic, nongovernmental action.

A few weeks later, an elite class of Americans lost their jobs all at once: congressional Republicans. In the House of Representatives, the Republicans lost fifty-two seats and yielded control to the Democrats. In the Senate, the Republicans lost eight seats, leaving neither party with a clear majority.

On February 3, 1931, Hoover reiterated his opposition to federal unemployment relief, explaining that he would favor it only “if the time should ever come that the voluntary agencies of the country, together with the local and State Governments, are unable to find resources with which to prevent hunger and suffering.” Like the
Federal Reserve, which kept its gold in vaults while banks failed, Hoover would not open the federal treasury for relief until after private and local public institutions collapsed. He opposed federal relief on principle, believing that Americans risked being “plunged into socialism and collectivism” if the federal government provided aid directly to its citizens.35

He did not keep faith with cooperative and local efforts entirely in vain. Some businesses tried hard to keep employment stable. General Electric cut back on the number of styles in which it produced lightbulbs, and also committed to fifty weeks of work in 1931 for employees who had been with the firm for two years or more. Some unions worked with their industries to establish unemployment insurance funds. Some companies retrained their workers, in order to ease their movement within the firm. Still others established loans for the unemployed.36 States did what they could. Governor Franklin D. Roosevelt of New York requested an emergency relief program of the state assembly in the summer of 1931, and Albany responded by devoting $20 million, which went to the relief of more than 300,000 families. Other states followed suit, spending tens of millions of dollars to aid their citizens.37

Yet these efforts did not suffice. Consumers spent cautiously when they had no confidence, and hardly at all when they had no jobs. Businesses that depended on consumers’ continued confident borrowing suffered. As James Farrell, the president of United States Steel Company, told a congressional hearing late in 1931, “it is difficult to create business beyond the demands of buyers.”38 And as businesses laid off their workers, fewer and fewer consumers had money to spend.

Hoover did not refrain entirely from federal action. In February 1931, he signed legislation creating a Federal Employment Stabilization Board, tasked with timing and scaling federal spending on construction to respond to unemployment.39 But he
supported such laws reluctantly, telling an ally that he preferred “to cut expenses and to give to the country and the world an exhibit of a balanced budget,” and he opposed other legislation to expand federal public works. Hoover also ordered stricter enforcement of anti-immigration legislation, and in March of 1931, the New York Times reported the White House’s claim that “President Hoover, in his efforts to relieve the unemployment situation . . . has kept out of the country nearly 100,000 aliens who would have been admissible under normal business conditions.”

In June 1931, Hoover moved to halt the international propagation of credit collapses, declaring a one-year moratorium on intergovernmental debts. He had his eye particularly on Germany, whose fiscal affairs were sinking ominously. “It is not,” the Times declared, “that war is threatened there,” but rather that “[i]t is today as if there were but a single nervous system for the entire civilized world,” and an injury to one extremity affected the whole body.

The moratorium might have delayed a further international financial collapse, but it could provide no immediate relief for Americans. The unemployment rate continued to soar. Retrospective estimates suggest it rose from about 9 percent in 1930 to about 16 percent in 1931 and then to an appalling 23 percent in 1932. During the Depression, government statisticians sensitive to the deepening crisis and wishing to measure its proportions developed the concepts and methods of measuring and defining unemployment that underlie these modern calculations. But their early work produced gloomy numbers, contrary to what the Hoover administration wished to hear and say. The president subjected the chief of the Bureau of Labor Statistics to forcible retirement, as the New York Times reported: “‘Retired!’ he shouted. ‘Please don’t put it that way. It is not a proper word.’”

In desperation, and in the beginning of his campaign for reelection, Hoover approved a last set of policies for lifting the
Depression. Alarmed by the impending collapse of the California-based Bank of America, Hoover called for emergency legislation to relieve the nation’s banks. In January of 1932, he signed into law the Reconstruction Finance Corporation (RFC), capitalized at $500 million and permitted to issue notes of up to $1.5 billion so it could lend money, principally to financial institutions, and thus act (as the Federal Reserve was not) as an energetic lender of last resort and rescue the nation’s credit-providing institutions. RFC operated on the theory that if it could ease pressure on banks, eventually they would confer a similar comfort on their borrowers. Within two weeks of its creation, it was making a hundred loans a day.

Hoover also signed a bill allocating $125 million to the Federal Land Bank system, a network of banks established in 1916 to provide farm mortgages. The extra money would prop up the banks in the face of defaulting borrowers and savers who demanded their deposits. Likewise, in the summer of 1932, Hoover signed into law a system of Home Loan Banks to shore up banks that had lent money for homeowners’ mortgages. He signed a further bill easing the restrictions on banks within the Federal Reserve System and allowing the Federal Reserve Board greater latitude in manipulating interest rates.

All these measures probably helped loosen restrictions on credit and got bankers and businessmen to lend and borrow more freely again, which might eventually have led to the substantial reemployment of the American people. But they did nothing immediate for non-banker Americans. Hoover’s supporters unintentionally damned their own efforts, explaining correctly that they did nothing directly for ordinary citizens. As Secretary of the Treasury Ogden Mills explained, the president’s policies “set free the recuperative and constructive forces within business itself…so that the nation’s business might have an opportunity to do for itself what the Government cannot hope to do for it.”
Hoover stood by the principles of relief he had established in 1927—encouraging phrases, widely publicized, and aid to lenders, but no direct assistance to American workers. He disavowed any direct connection to citizens, explaining that he thought the presidency conferred “a power for leadership bringing coordination of the forces of business and cultural life.”

He left himself entirely open to criticism from Governor Roosevelt, who declared in April of 1932 that “The present administration . . . has either forgotten or it does not want to remember the infantry of our economic army. These unhappy times call for . . . plans . . . that build from the bottom up and not from the top down, that put their faith once more in the forgotten man at the bottom of the pyramid.”

Roosevelt’s speech brought disapproval even from members of his own party, for stirring up the masses against the rich. But by summer he would be the Democratic nominee for president, and in November he would put Herbert Hoover out of work, winning the presidency by a landslide, on the hope that he, as Hoover on principle would not, might bring relief to ordinary Americans.

Notes

4. Barry, Rising Tide, 266.
5. Ibid., 368.
6. Ibid., 401.
7. Ibid., 384–93.
10. Ibid., 314, 316.
20. Ibid., 116.
21. Ibid., 151.
37. Ibid., 169–70.
38. Ibid., 139.
45. Ibid., 42.
47. Ibid., 197.
48. Ibid., 200.