CHAPTER 10

Why Do We Call It The **"Great"** Depression?

The Federal Reserve Bank of St. Louis

Migrant family looking for work in the pea fields of California.
PHOTOGRAPH BY DOROTHEA LANGE, 1935. FROM FDR PRESIDENTIAL LIBRARY.

WHY DO WE CALL IT THE "GREAT" DEPRESSION?		
Federal Reserve Bank of St. Louis, Research Division—Economic Education		
C3 Disciplinary Focus Economics	**C3 Inquiry Focus** Using disciplinary concepts to evaluate evidence and construct explanations	**Content Topic** The Great Depression
C3 Focus Indicators **D1:** Explain points of agreement and disagreement experts have about interpretations and applications of disciplinary concepts and ideas associated with a supporting question. (D1.3.9-12) **D2:** Use benefits and costs to evaluate the effectiveness of government policies to improve market outcomes. (D2.Eco.7.9-12) **D3:** Gather relevant information from multiple sources representing a wide range of views while using the origin, authority, structure, context, and corroborative value of the sources to guide the selection. (D3.1.9-12) **D4:** Construct explanations using sound reasoning, correct sequence (linear or non-linear), examples, and details with significant and pertinent information and data, while acknowledging the strengths and weaknesses of the explanation given its purpose (e.g., cause and effect, chronological, procedural, technical). (D4.2.9-12)		
Grade Level 9–12	**Resources** Resources cited in this chapter and the Federal Reserve Bank of St. Louis' Great Depression website	**Time Required** 2–3 days

Introduction and Connections to the C3 Framework

Ask your students what they know about the Great Depression, and they will likely respond that it was caused by the Stock Market Crash of 1929, and that it ended as a result of an alphabet soup of New Deal programs. The content in their history textbooks likely reflects this level of misinformation. When introduced to the study of the Great Depression students are likely to ask: why should we study or care about the Great Depression—an event that affected our great-grandparents? Shouldn't we focus on more recent events?

How can you help your students understand why they should study this watershed event? How can your students move beyond the simplistic and inaccurate assessment of its causes and solutions to gain a deeper understanding of the factors that caused the Great Depression and its impact on the American people and on the U.S. economy? How can you help them learn to use economic tools to analyze the impact of other events and policies on the U.S. economy, including the most recent economic crisis, the Great Recession?

This chapter suggests ideas for guiding students through an inquiry that allows them to think economically and apply concepts from economics, civics, and history to analyze the Great Depression while using the educational resources of the Federal Reserve Bank of St. Louis, which are available on its Great Depression website, to support their understanding. (The overview on pages 104-105 of this chapter is one of many such resources.) This lesson focuses on the compelling question: Why Do We Call It the "Great" Depression? The lesson calls on students to develop supporting questions, investigate those questions using carefully selected sources, and compose explanations in response to the supporting questions.

Eleanor Roosevelt talking with a project superintendent in Des Moines, Iowa. June 8, 1936. This project, sponsored by the Works Progress Administration, planned to convert a city dump into a water front park.

The combination of content resources developed by the Federal Reserve Bank of St. Louis and the C3 Framework provide an opportunity for students to go in search of new knowledge to help them understand and explain the causes of the Great Depression and its impact on the American people. These lessons employ the four dimensions of the C3 inquiry arc over 2-3 class periods with an emphasis on Dimension 2—Connections to Disciplinary Tools and Concepts. The goal of these lessons is to engage students in critical historical thought while utilizing key economic content, data, and primary source material.

Inquiry Arc

Dimension 1: Developing Questions and Planning Inquiries

This lesson begins by posing for students the compelling question: *Why Do We Call It the "Great" Depression?* Although students should have regular opportunities to construct their own compelling question, this question represents a common curriculum topic and is sufficiently complex to necessitate a wide range of interesting supporting questions. The lesson develops as students construct supporting questions as they "explain points of agreement and disagreement experts have about interpretations and applications of disciplinary concepts and ideas associated with a supporting question." (D1.3.9-12)

An approach to developing supporting questions for inquiry is first to show your students photographs from the Great Depression found at http://www.stlouisfed.org/great-depression/gallery.html. Ask the students what these photos communicate about this time in our history and what the students already know about the Great Depression. In response to the question about the photos, students might say that people looked poor, tired, desperate, and hungry, and that many were out of work. These initial ideas are a starting place for students to explore some of the more complex concepts and ideas related to the Great Depression. For example, have students compose questions based on the five Ws (who, what, when, where, why):

- Who was affected?
- What caused this hardship?
- Where did this happen?
- Why were there so many people out of work?
- Why wasn't there enough food?
- When did this occur?

From these questions, students might then be asked to consider what they already know about the Great Depression. These ideas might include:

- It was caused by the stock market crash.
- It happened a long time ago and lasted for a long time.
- The New Deal ended the Great Depression.
- World War II ended the Great Depression.
- Farmers destroyed crops, milk, and other products.
- Banks were closed.

The compelling question that is our focus, "Why Do We Call It the 'Great' Depression?" can lead to supporting questions, such as:

- What is a depression?
- How did we know this was a depression?
- How did it compare to previous depressions?

From these questions, students can move into data related to measuring the economy—such as real GDP, unemployment, and inflation. They can use these data to compare the period of the Great Depression with other crises and with more normal periods since 1929. Once students have their supporting questions, they can examine points of agreement and disagreement that experts have concerning the related ideas and concepts. In terms of what caused the depression, students may continue by looking at factors that economic historians have investigated as causes for the Great Depression, such as changes in specific industries (agriculture, automobile, housing, banking and finance).

Use the initial questions and the students' knowledge of the Great Depression to guide them to develop other supporting questions.

- How did the Great Depression affect people?
- How did people deal with the Great Depression?
- How is a depression different from a recession?
- What are the indicators used to determine a depression?
- How did the Great Depression end?

Answering these questions will support research by the students investigating a number of compelling questions relating to the Great Depression in addition to the compelling question that is the focus of this chapter. They include:

- What caused the Great Depression?
- What events or policies ended the Great Depression?
- What government or Federal Reserve policies were effective/ineffective?
- How did the Great Depression change the U.S.?

Dimension 2: Connections to Disciplinary Tools and Concepts

With compelling and supporting questions in place, students could begin to examine points of agreement and disagreement among experts about the Great Depression and the reasons why it had such damaging effects for such a long time. They might consider the impact that policies designed during the Great Depression had on the size of the government and its role in the economy. This should involve evaluating "the selection of monetary and fiscal policies in a variety of economic conditions." (D2.Econ.12.9-12) They could consider incentives established by these policies, including changes related to the banking industry, such as the implementation of the Federal Deposit Insurance Corporation (FDIC); agricultural support policies; and Social Security.

Economists measure the economy by analyzing economic indicators. Ask students if they know what unemployment, inflation, and real gross domestic product are. Point out that understanding what these indicators are and how they are measured provide the basis for understanding the health of the economy now and during the Great Depression. Students can examine "help-wanted" advertising in newspapers in the United States before, during and after the Great Depression. (These and the other indicators mentioned in this paragraph are accessible on the website of the Federal Reserve Bank of St. Louis at http://research.stlouisfed.org/dashboard/440.) Ask what they might conclude regarding help-wanted ads during times of recession (many fewer help-wanted ads). Have students look at graphs of the unemployment rate and ask how the help-wanted ads graph correlates with the unemployment rate graph (lower number of help-wanted ads, higher rates of unemployment). Explain that during recessions, businesses hire fewer workers—and even let workers go. The demand for workers decreases. Show students other graphs, such as the rate of change in real gross domestic product (real GDP) growth, and the percent change in

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The Great Depression: An Overview

by David C. Wheelock

One reason to study the Great Depression is that it was by far the worst economic catastrophe of the 20th century and, perhaps, the worst in our nation's history. Between 1929 and 1933, the quantity of goods and services produced in the United States fell by one-third, the unemployment rate soared to 25 percent of the labor force, the stock market lost 80 percent of its value and some 7,000 banks failed.

At the store, the price of chicken fell from 38 cents a pound to 12 cents, the price of eggs dropped from 50 cents a dozen to just over 13 cents, and the price of gasoline fell from 10 cents a gallon to less than a nickel. Still, many families went hungry, and few could afford to own a car.

Another reason to study the Great Depression is that the sheer magnitude of the economic collapse— and the fact that it involved every aspect of our economy and every region of our country—makes this event a great vehicle for teaching important economic concepts. You can learn about inflation and deflation, Gross Domestic Product (GDP), and unemployment by comparing the Depression with more recent experiences, including the financial crisis and Great Recession of 2007-09. Further, the Great Depression shows the important roles that money, banks and the stock market play in our economy.

A third reason to study the Great Depression is that it dramatically changed the role of government, especially the federal government, in our nation's economy. Before the Great Depression, federal government spending accounted for 3 percent of GDP. By 1939, federal outlays reached 10 percent of GDP.[1] (At present, federal spending accounts for about 20 percent of GDP.) The Great Depression also brought us the Federal Deposit Insurance Corp. (FDIC), regulation of securities markets, the birth of the Social Security System and the first national minimum wage.

WHAT CAUSED THE GREAT DEPRESSION?

Economists continue to study the Great Depression because they still disagree on what caused it. Many theories have been advanced over the years, and there remains no single, universally agreed-upon explanation as to why the Depression happened or why the economy eventually recovered.

The 1929 stock market crash often comes to mind first when people think about the Great Depression.

The crash destroyed considerable wealth. Perhaps even more important, the crash sparked doubts about the health of the economy, which led consumers and firms to pull back on their spending, especially on big-ticket items like cars and appliances. However, as big as it was, the stock market crash alone did not cause the Great Depression.

Some economists point a finger at protectionist trade policies and the collapse of international trade.

The Smoot-Hawley tariff of 1930 dramatically increased the cost of imported goods and led to retaliatory actions by the United States' major trading partners. The Great Depression was a worldwide phenomenon, and the collapse of international trade was even greater than the collapse of world output of goods and services. Still, like the stock market crash, protectionist trade policies alone did not cause the Great Depression.

Other experts offer different explanations for the Great Depression. Some historians have called the Depression an inevitable failure of capitalism. Others blame the Depression on the "excesses" of the 1920s: excessive production of commodities, excessive building, excessive financial speculation or an excessively skewed distribution of income and wealth. None of these explanations has held up very well over time. One explanation that has stood the test of time focuses on the collapse of the U.S. banking system and resulting contraction of the nation's money stock. Economists Milton Friedman and Anna Schwartz make a strong case that a falling money stock caused the sharp decline in output and prices in the economy.[2]

As the money stock fell, spending on goods and services declined, which in turn caused firms to cut prices and output and to lay off workers. The resulting decline in incomes made it harder for borrowers to repay loans. Defaults and bankruptcies soared, creating a vicious spiral in which more banks failed, the money stock contracted further, and output, prices and employment continued to decline.[3]

MONEY, BANKING AND DEFLATION

Money makes the economy function. Money evolved thousands of years ago because barter—the direct trading of goods or services for other goods or services— simply didn't work. A modern economy could not function without money, and economies tend to break down when the quantity or value of money changes suddenly or dramatically. Print too much money, and its value declines—that is, prices rise (inflation). Shrink the money stock, on the other hand, and the value of money rises— that is, prices fall (deflation).

In modern economies, bank deposits—not coins or currency—comprise the lion's share of the money stock. Bank deposits are created when banks make loans, and deposits contract when customers repay loans. The amount of loans that banks can make, and hence the quantity of deposits that are created, is determined partly by regulations on the amount of reserves that banks must hold against their deposits and partly by the business judgment of bankers.

In the United States, bank reserves consist of the cash that banks hold in their vaults and the deposits they keep at Federal Reserve banks. Reserves earn little or no interest, so banks don't like to hold too much of them.
On the other hand, if banks hold too few reserves, they risk getting caught short in the event of unexpected deposit withdrawals.

In the 1930s, the United States was on the gold standard, meaning that the U.S. government would exchange dollars for gold at a fixed price. Commercial banks, as well as Federal Reserve banks, held a portion of their reserves in the form of gold coin and bullion, as required by law.

An increase in gold reserves, which might come from domestic mining or inflows of gold from abroad, would enable banks to increase their lending and, as a result, would tend to inflate the money stock. A decrease in reserves, on the other hand, would tend to contract the money stock. For example, large withdrawals of cash or gold from banks could reduce bank reserves to the point that banks would have to contract their outstanding loans, which would further reduce deposits and shrink the money stock.

The money stock fell during the Great Depression primarily because of banking panics. Banking systems rely on the confidence of depositors that they will be able to access their funds in banks whenever they need them. If that confidence is shaken—perhaps by the failure of an important bank or large commercial firm—people will rush to withdraw their deposits to avoid losing their funds if their own bank fails.

Because banks hold only a fraction of the value of their customers' deposits in the form of reserves, a sudden, unexpected attempt to convert deposits into cash can leave banks short of reserves. Ordinarily, banks can borrow extra reserves from other banks or from the Federal Reserve. However, borrowing from other banks becomes extremely expensive or even impossible when depositors make demands on all banks. During the Great Depression, many banks could not or would not borrow from the Federal Reserve because they either lacked acceptable collateral or did not belong to the Federal Reserve System.[4]

Starting in 1930, a series of banking panics rocked the U.S. financial system. As depositors pulled funds out of banks, banks lost reserves and had to contract their loans and deposits, which reduced the nation's money stock. The monetary contraction, as well as the financial chaos associated with the failure of large numbers of banks, caused the economy to collapse.

Less money and increased borrowing costs reduced spending on goods and services, which caused firms to cut back on production, cut prices and lay off workers. Falling prices and incomes, in turn, led to even more economic distress. Deflation increased the real burden of debt and left many firms and households with too little income to repay their loans. Bankruptcies and defaults increased, which caused thousands of banks to fail. In each year from 1930 to 1933, more than 1,000 U.S. banks closed.

Banking panics are pretty much a thing of the past, thanks to federal deposit insurance. Widespread failures of banks and savings institutions during the 1980s did not cause depositors to panic, which limited withdrawals from the banking system and prevented serious reverberations throughout the economy. Similarly, banks did not face large-scale deposit withdrawals during the financial crisis of 2007-09. However, investors lost confidence in money market mutual funds, prompting a temporary federal guarantee of those funds to slow withdrawals. Also, many banks and other financial firms were unable to roll over their short-term debt in wholesale funding markets, forcing a few of them out of business.

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1. In 1929, federal net outlays totaled \$3.1 billion and GDP totaled \$104.6 billion. In 1939, federal net outlays totaled \$9.1 billion and GDP totaled \$93.5 billion. Data are from Federal Reserve Economic Data (FRED®), Federal Reserve Bank of St. Louis.
   http://research.stlouisfed.org/fred2/series/FYONET
   http://research.stlouisfed.org/fred2/series/GDPA

2. Milton Friedman and Anna J. Schwartz. *A Monetary History of the United States, 1867-1960.* Princeton: Princeton University Press, 1963.

3. Former Federal Reserve Chairman Ben Bernanke wrote an important article showing that banking panics contributed to the nation's economic collapse not only by reducing the money stock, but also by increasing the costs of borrowing and lending. Ben S. Bernanke. "Nonmonetary Effects of the Financial Crisis in Propagation of the Great Depression," *American Economic Review*, June 1983, v. 73, issue 3, pp. 257-76.

4. Before 1980, only banks that were members of the Federal Reserve System could borrow directly from Federal Reserve banks.

inflation year over year. Ask them what they notice about real GDP growth during recessions (as indicated by a shaded area on the graph) and what they notice about percent change in inflation during recessions. Ask students what the graphs show for the period between 1929 and 1939—deflation (or negative inflation), unemployment as high as 25%, and declining real GDP. Ask students to explain what these data communicate about the time period.

Dimension 3: Evaluating Sources and Using Evidence

Successful inquiry requires that students "Gather relevant information from multiple sources representing a wide range of views while using the origin, authority, structure, context, and corroborative value of the sources to guide the selection." (D3.1.9-12) To accomplish this goal, have students explore additional source material regarding the Great Depression found in Federal Reserve Archival System for Economic Research (FRASER), http://fraser.stlouisfed.org. These sources may require scaffolds for students to make meaningful use of them. Consider using historical source scaffolds such as APARTS or SCIM-C. These scaffolds are designed to support students as they conduct document analysis. You may also need to excerpt material from these sources, depending on the time available.

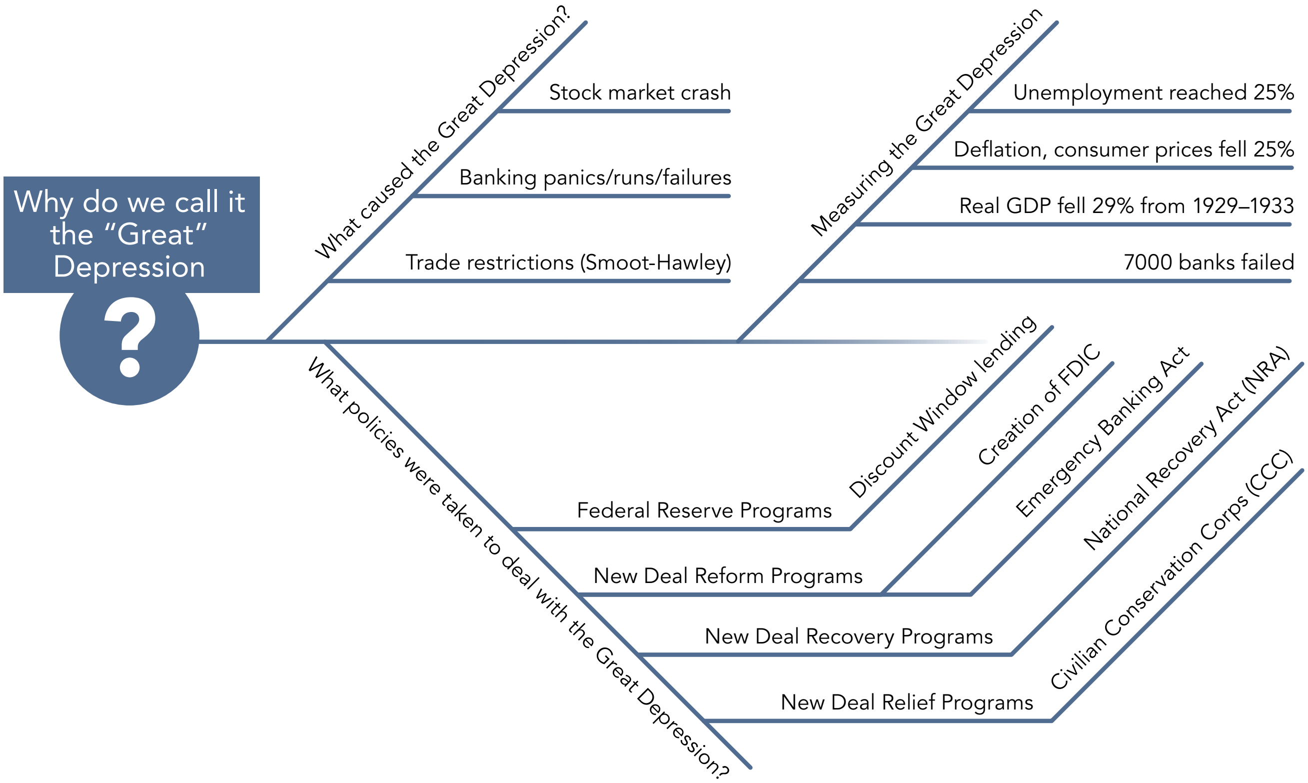
Have students evaluate information from the various sources with regard to the value of that information in responding to the compelling question framing the inquiry. Based on the content learned from various sources students should take a position on an issue arising from the compelling question, "Why Do We Call It The 'Great' Depression?" For example, a position might be that another recession of the magnitude of the Great Depression can be avoided. Or, students might provide an explanation for why the Great Depression lasted so long, and so on.

Have students create a fishbone diagram illustrating the causes and effects of the Great Depression. To create the Fishbone (or Ishikawa) diagram, students should decide on one major effect that relates to the compelling question, Why Do We Call It The "Great" Depression? For example, they might select "Great Depression" as the effect. This effect should be placed in the head of the diagram. Then, students should then start thinking about causes. They should list causes on the bones of the fish and try to arrange these causes in categories so that patterns can be determined.

Have students annotate the diagram indicating sources that support their claims. Point out that students should use data to explain why this was a "Great Depression," describing the magnitude of change and the duration of change.

Students can also review the measures that were taken (and not taken) to deal with the Great Depression. New Deal programs were carried out in two stages—from 1933-1934, and from 1935-1941. They focused on three areas:

1. Relief programs that would help immediately (for example the Works Progress Administration, the Federal Emergency Relief Administration, and the Federal Theatre Project);



Fishbone diagram illustrating the causes and effects of the Great Depression.

2. Recovery programs that would help rebuild the economy (such as the Farm Security Administration and the Agricultural Adjustment Administration); and
3. Reform programs to prevent the disaster from recurring (such as the establishment of the Federal Deposit Insurance Corporation, known as the FDIC, which guaranteed bank deposits).

Students could consider both the extent and limitations of these initiatives. One group of students could examine relief programs and evaluate their impact. A second group could study recovery programs and appraise their effectiveness. A third group could focus on reform programs by identifying the objectives of the programs and weighing the evidence on whether or not these objectives were accomplished. Roosevelt's programs certainly restored confidence in the financial system and in the U.S. economy. However, the Great Depression went on for a very long time despite the New Deal measures, and students should also consider the possible limitations of some of the measures. For example, did the Revenue Act (Wealth Tax Act) of 1935 have a negative effect on GDP by reducing investment and incentives to produce? Did the National Recovery Act (NRA) encourage the formation of industrial cartels, limit competition, and discourage employment? Did the New Deal agricultural programs slow the economic recovery by discouraging production and employment?

Students could also examine the role of the Federal Reserve in allowing the money stock to collapse. Runs on the banks led to bank failures because banks had converted many of the deposits of customers into loans and did not have reserves to meet the demands of so many customers to withdraw their money. The Fed could have helped to solve the problem of the lack of the necessary reserves by lowering the discount interest rate, opening discount window access to more banks, and making more open market purchases of securities. The Fed learned from its mistakes and reacted very differently to the Great Recession arising from the financial crisis of 2007-2009. Students could study the options available to the Federal Reserve at different times in the Great Depression, and consider policies that might have been more effective than those actually followed in restoring confidence in the financial system and reviving the economy.

Dimension 4: Communicating Conclusions and Taking Informed Action

In communicating their arguments regarding this Great Depression inquiry, regardless of the method of communication, students should acknowledge various views by presenting an opposing point of view and then forwarding an argument that supports their view and explains the error in the opposition's view—citing sources as evidence to do so. Students might choose to develop an argument regarding what ended the Great Depression. In doing so, they must recognize the argument held by many that Roosevelt's New Deal programs ended the Depression. Then citing sources, they might develop support for an argument that the primary role of the New Deal programs was a change in consumer confidence and that other economic factors actually brought the Great Depression to an end.

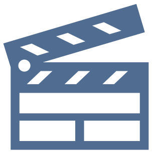
Students should use the annotated fishbone diagram they created, data, and information from the sources they have identified to communicate their findings about the Great Depression. Provide the following suggestions for communicating results. All examples should include use of data and information from sources. All data and sources should be properly cited. The C3 Framework suggests that students should "construct explanations using sound reasoning, correct sequence (linear or non-linear), examples, and details with significant and pertinent information and data, while acknowledging the strengths and weaknesses of the explanation given its purpose (e.g., cause and effect, chronological, procedural, technical)." (D4.2.9-12) Following are examples of how students might accomplish this communication task.

WRITE A REPORT TO A CONGRESSIONAL COMMITTEE REGARDING THE CAUSES OF AND PROPOSALS FOR ENDING THE GREAT DEPRESSION

Such a report should indicate an understanding of the various factors that contributed to the Great Depression including decreasing money stock, bank failures, the stock market crash, deflation, and the Smoot-Hawley Tariff. Proposals for ending the Great Depression should include policies that could be undertaken by the Federal Reserve and/or the government for expanding the money stock, regenerating consumer confidence in the banking system, and promoting employment. Students should identify the impact of these potential policies on unemployment, government spending, real GDP, and consumer confidence. The report should draw on real GDP, inflation, and unemployment data for the time period. The report should include an analysis of the data based on an understanding of the factors that contributed to the Great Depression.

USE VIDEO, OR PERHAPS AUDIO EQUIPMENT, TO RECORD A NEWS STORY PLACED DURING THE GREAT DEPRESSION (E.G. AN OLD TIME NEWS REEL OR RADIO PROGRAM). THE VIDEO OR RADIO PROGRAM SHOULD INCLUDE INTERVIEWS WITH FICTIONAL PEOPLE (POLICY MAKERS AND CITIZENS) WHO LIVED DURING THE PERIOD.

Videos or audio recordings should include information from citizens who were affected by the stock market crash, unemployment, deflation, and bank failures, sharing their stories. Policy makers should suggest policies that could be undertaken by the Federal Reserve and/or the federal government and explain how these policies would affect unemployment, government spending, real GDP and consumer confidence to alleviate citizens' distress. Either the interviewer or the policy maker should draw on relevant data.



PRODUCE A DOCUMENTARY THAT EXPLORES ONE OR MORE OF THE QUESTIONS DEVELOPED DURING THE INQUIRY STAGE OF THE LESSON.

The documentary should employ graphs and charts that indicate an understanding of economic indicators—real GDP, unemployment, and inflation. In addition, depending on the question, the documentary should address the factors that together created the worst economic collapse in U.S. history, and address the impact of New Deal policies, the failure of the Federal Reserve to act appropriately, and so on.

COMPARE A RECENT RECESSION TO THE GREAT DEPRESSION. WHAT SIMILARITIES AND DIFFERENCES ARE EVIDENT? WRITE AN ESSAY EXPLAINING THE ANALYSIS.

The essay should compare the primary economic indicators related to recessions between the two events—real GDP growth, unemployment rates, and the duration of the two events. In addition, the essay should compare factors that led to/created the problem as well as a comparison of the Fed's monetary policy actions and the federal government's fiscal policy actions relative to the two events.

About the Federal Reserve Bank of St. Louis

The Federal Reserve Bank of St. Louis is one of 12 Federal Reserve Banks in the Federal Reserve System. The Federal Reserve Bank of St. Louis is the 8th District of the Federal Reserve System serving parts of Missouri, Illinois, Indiana, Kentucky, Tennessee and all of Arkansas. As part of its outreach efforts, the Federal Reserve Bank of St. Louis provides online resources—courses, videos, podcasts, lesson plans, and whiteboard activities to K-12 educators throughout the country, free of charge.

The authors of this chapter are Mary Suiter, assistant vice president and economic education officer at the Federal Reserve Bank of St. Louis; Barbara Flowers, economic education coordinator at the Federal Reserve Bank of St. Louis; and Scott Wolla, senior economic education specialist at the Federal Reserve Bank of St. Louis. The opinions expressed in this chapter are those of the authors and not those of the Federal Reserve Bank of St. Louis or the Federal Reserve System.