

Randall E. Parker, *The Economics of the Great Depression: A Twenty-First Century Look Back at the Economics of the Interwar Era*

(Edward Elgar 2007)

G. R. Hawke¹

In his foreword to this volume Ben Bernanke comments: 'History is a highbrow form of gossip. The stories of individuals swept up in — and occasionally influencing — the tide of world events are intrinsically fascinating, in no small part because they so often display the eternal verities of the human condition.' (Randall 2007: vii).² There was a good deal of gossip in Randall Parker's earlier book, *Reflections on the Great Depression*³ — in which senior economists reflected on their experiences as young economists during the Great Depression — but there were also interesting reflections. Friedman's declared admiration for Keynes — 'a great human being and a great economist' — and his dating of his own departure from Keynesianism to post-1936 debates about the role of governments rather than to economic analysis ensured that *Reflections* escaped common myths. Even more notable was Samuelson's observation: 'I think of the Great Depression as a concatenation of a multiplicity of factors. This is a lousy theory. But it is more important to describe the facts correctly than to have a simple elegant theory which misses the facts. (Randall 2002: 32)

The Economics of the Great Depression repeats the format of interviews used in *Reflections* but the subjects are younger economists who have contributed significantly to recent analysis of the Great Depression. The interview format works well, although there can be few topics for which it is appropriate, and even here historical understanding is variable. Parker's standard interview format included the observation that in 1981 the study of the Great Depression seemed dead, using Brunner (1981) as his foil. This, however, tells us more about Parker's intellectual autobiography than it does about the literature of the Great Depression. Recent advances have built on previous ones, and there was no lull in the 1970s and 1980s. Indeed, Parker's books show a continual advance, built on the striking innovations of Friedman & Schwartz in the 1960s, the contribution

¹ Victoria University of Wellington.

² Perhaps there is more force in T.S. Ashton's observation that humans are fascinated by growth, whether of a flower, a child, an economy, or knowledge.

³ Randall E. Parker *Reflections on the Great Depression* (Edward Elgar, 2002)

of Temin (1976) in the 1970s, and beginning in the 1980s the revival of Gold Standard considerations by Eichengreen (1992).

A major puzzle about the Great Depression is what initiated it — even remembering Samuelson's acceptance of multiple causation and preferring it to the seductive appeal of searches for a simple explanation. James Hamilton asks: '... why did stock prices go down? Was it a rational anticipation of something about to happen? If so what and how were people recognizing it?' (Randall 2007: 69) Despite the appeal of arguments like that of Temin for changed consumption plans, perhaps engendered by uncertainty about the durability of the boom of the 1920s based on motor vehicles, suburbanization and the impact of electric consumer durables, the best answer remains 'consumption fell much more strongly than usual for the start of a recession ... [T]here were these many different factors that mattered' (Romer in Randall 2007: 26).

There is more agreement that the monetary policy decisions of the Federal Reserve turned a cyclical downturn into the Great Depression; but not a complete consensus. While some would still argue that monetary contraction initiated depression as well as intensifying a downturn so as to create the Great Depression, there are Real Business Cycle advocates who argue that the Great Depression can be explained as a productivity shock. Parker includes Lee Obhanian among his interviewees, and cautions about initial unjustified dismissal of earlier contributions, but the dominant view is that 'the real business cycle models that have been written about the Great Depression with which I am familiar are not serious models of the Great Depression ... they're not taken seriously, except by macroeconomists who don't know any better' (Calomiris in Randall 2007: 221). It is hard to argue with that.

Recent scholarship is even firmer in establishing the significance of the international dimension. Or perhaps it would be better to say that it rediscovered what had been known, but was forgotten. Eichengreen, who has done more than anybody else to formulate current understanding, generously acknowledges Kindleberger (1973) and pre-war writers. But then the point was commonplace in the 1930s as in Keynes's observation in 1930–31: 'The maintenance of the gold standard keeps a country's investment policy and its current rates of interest somewhat rigidly linked to those prevailing in the other gold standard countries, since any considerable departure from the policies pursued elsewhere will lead to a loss of gold.'⁴ It is a commentary on the insularity of much US academic work that this had to be rediscovered. It is even more remarkable when one considers the amount of work in other countries, in Europe, Asia and Latin America as well Australia and New Zealand, on the relative contributions to the

⁴ Collected Works, 21, p. 286 cited in Donald J. Markwell "Keynes and Australia" Reserve Bank of Australia Research Discussion Paper 2000-4, p. 17.

experience of the 1930s of external causes and pre-existing domestic circumstances.

Still, it is good to see it recovered, and pithily summed up by Robert Lucas: 'We had our spending collapse because the money supply contracted. And I suppose they [Canadians] got theirs because Americans stopped buying Canadian goods' (Lucas in Randall 2007: 96).⁵

The impact of the Gold Standard in the US was through conventional thinking, and this is one of the areas where recent analysis has had most impact. Federal Reserve members did consider alternative policy actions, although not in any serious way a departure from the Gold Standard. Essentially they were imprisoned in established ways of thinking: 'They were real bills doctrine people. Prices were not rising. Prices were actually falling very little, but falling. But they were real bills people and the Federal Reserve Act is written on the basis of the real bills doctrine. So inflation to them meant they were monetizing non-productive credit' (Meltzer in Randall 2007: 226). Or:

The story was they followed something called the Riefler-Burgess doctrine which said that you look at two things. You look at member bank borrowing in New York and whether it's greater than 500 million dollars and you look at the level of nominal short-term interest rates. If member bank borrowing was below 500 million dollars, the way the Fed interpreted things in the 1920s and 1930s was that it was a state of monetary ease. They believed that member banks only came to the window when they really needed to. They didn't go there to make profits. The Fed looked at member bank borrowing in 1930 and 1931 and they said, 'Gee, nobody's coming to the window. I guess things are good.' I mean really, that's the key point. (Bordo in Randall 2007: 201)

Contemporary economic scholarship has added a good deal. While many have been puzzled about why people were concerned about inflation in the 1930s and have found an answer in changed ideas and terminology, we have learned only recently (from Japanese experience as much as abstract thought) that the zero bound on nominal interest can be significant. The US recovery is now traced substantially to declines in real interest rates: 'But, expansionary monetary policy can cause expectations of inflation. And the evidence we have suggests that this happened. As a result, real interest rates fell dramatically after 1933' (Romer in Randall 2007: 134). We have also learned to look at local circumstances, not least for institutional features which frustrated real interest rate declines (see Hawke 1973), but also for how the US banking structure had a significant effect in the US: '[T]he shocks often had different magnitudes in particular regions, at particular times, and that the complexity of the Great Depression

⁵ Lucas explicitly rejects an unspecified productivity shock as an alternative.

partly resulted from out unit banking system, which connected the fates of banks in particular regions to the borrowers in their particular location' (Calomiris in Randall 2007: 213). We have also learned not to ignore the debt deflation process, as emphasised by Ben Bernanke.

Understanding of the Great Depression has progressed continually since the 1930s. Economic historians will be especially interested in the reflection:

I think it is a new generation realizing that the Great Depression was fundamentally important. I wonder, as we're sitting here pondering this, what role the new economic history played. ... The revolution in economic history that started in the late 1960s. What had been questions we answered just with words, we started to actually get some old data and evaluate empirically and analytically. I think some of what we saw in the early 1980s is taking that philosophy and looking back at the macro economy, not just as slavery or some of the issues that have been so hot in the new economic history. (Romer in Randall 2007: 136)

Christina Romer recognised that new macroeconomic tools have also played a key role, but perhaps the most important lesson of all is the indispensability of approaching contemporary problems with the best available knowledge, not the lessons of previous generations.

References

- Brunner, K. (ed.) 1981, *The Great Depression Revisited*, Boston: Martinus Nijhoff.
- Eichengreen, B. 1992, *Golden Fetters: The Gold Standard and the Great Depression, 1919–1939*, New York: OUP.
- Hawke, G. R. 1973, 'The Government and the Depression of the 1930s in New Zealand: An Essay towards a Revision', *Aust. Econ. Hist. Rev.* XIII (March): 72–95.
- Kindleberger, C. P. 1973, *The World in Depression, 1929–1939* (Berkeley: University of California, 1986; originally London: Allen Lane, 1973)
- Temin, P. 1976, *Did Monetary Forces Cause the Great Depression?*, New York: Norton.