ECONOMIC AND BUSINESS HISTORY 24/25

LECTURE 11 – FROM DEGLOBALIZATION TO DEPRESSION

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PLAN

1. Winner's Curse
2. Crash
3. Great Depression

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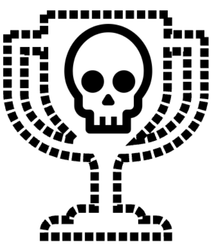
1. Winner's Curse



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WHO WON WWI?

Shares of the World Industrial Output (1913 and 1926-9)

	USA	Germ.	GB	France	Russia/ URSS	Sweden	Japan	India	Rest of the W
1913	35,8	14,3	14,1	7,0	4,4	1,0	1,2	1,1	21,1
1926-9	42,2	11,6	9,4	6,6	4,3	1,0	2,5	1,2	21,2

Kenwood e Lougheed 1999: 173.

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The Spoils of Victory

- Germany sold capital goods (locomotives, trains, ships) and stocks (incl. German-financed US railway companies) to the US to obtain dollars to pay for the 1919 war reparations.
- In 1917, the confiscation and compulsory licensing of 5,000 German patents (e.g., Aspirine) transferred the technological leadership in chemistry and steel sectors to the US
- Financial and physical capital abundant in the US
- Foreign markets lost by Euro Big3 went to the US

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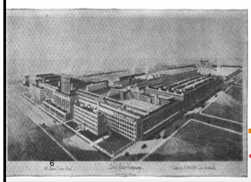
Large Firms

- Capital stocks and the conquest of markets lost by the Europeans contribute further to increase the size of the firms
- The US vast internal market, as well as a large amount of wealthy consumers meant that size was an advantage for businesses
- Assembly lines and other efficiency-enhancing technologies (pre- and post-1918) contribute to the rise of the large firms, like Ford and GM (See Text 6)



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Largest industrial firms, 1917 and 1930 (by Stock value in current USD)

	USA		GERMANY		UNITED KINGDOM	
	1917	1930	1919	1930	1913	1929
1st	2.449,5	2.394,5	278,2	641,4	142,6	510,9
2nd	574,1	1.770,9	199,4	634,1	110,2	497,7
3rd	381,5	1.315,8	128,9	508,3	77,0	138,0
4th	314,1	820,6	107,7	375,6	66,2	112,5
5th	306,3	801,1	101,0	290,6	53,3	100,2
25th	143,3	308,5	28,8	58,8	18,6	25,7
50th	90,3	174,7	17,7	33,5	9,8	15,6
100th	43,6	80,1	9,3	16,5	5,6	8,9
200th	24,4	36,1	4,4	6,3	3,0	3,8

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Domestic Economy: firms and the markets

- Despite the emergence of large firms, US market remained competitive
- US gov regulation (anti-trust) prevented "coordination strategies" by the firms:
  - CARTEL – price setting agreements, by competitors
  - TRUST – union of competing businesses and creation of a mother company, onwed in shares by the older owner (Trustees)
  - Nevertheless, the prevalence of large firms with good access to the capital markets leads to the spread of :
    - HOLDINGS – firm created to control other businesses/businesses groups

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Domestic Economy: families

- With WWI, USA received more physical and financial capital and its vast increases in productivity allowed vast market segment to emulate the high class of the *Belle Époque*
  - High-tech durables, like cars and domestic appliances (iron, radio, toaster, fridge...) became mass-consumption items

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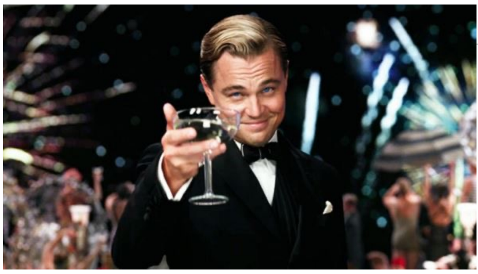
The *Roaring Twenties*



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Euro: The Spoils of Defeat

- The great sacrifices demanded from the working class and from women during WWI led to **universal** (all men and women, regardless of status) **voting**
- This meant a change from capital-friendly to labour-friendly institutions: especially, concerns with unemployment led countries to become protectionist
- Also, state budgets became larger and more redistributive (pensions, war debts, state-owned firms)

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2. Crash

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The Roaring 1920s were great for the US, right?

Yes, but there were 'hidden' vulnerabilities

- With WWI-induced protecionism, the US was 'leading alone'
  - The world retaliated on US 'unfair' competition (USA continued to be strongly protectionist, even after 1918, when it had clear comparative advantages in many fields) and worker-influenced European govs wanted to protect firms and workers
  - Non-US firms adapted to domestic, not foreign, demand and hence not as innovative as before
- Also, Fast growth ► high savings ► low return rates!!!
- In the 1st Globalization, this sequence led to the outflow of capitals to capital-poor countries, benefitting GB, Fr and Ger holders of financial and physical capital

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Deglobalization in the World Capital Markets

With WWI, USA became a creditor nation and its capital market became the most important in the world

- European stock and fixed capital -> productivity growth -> high growth rates
- Abundant (but country-tied) capital -> low return rates from investment

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Deglobalization and the 1929 Crash

- There was a brief period of re-globalization from 1925 to 1928 (with American investment in S America and Central Europe)
- However, giving in to pressures from the American banks, in 1928 the American **FED** suddently **RAISED** its discount rate and **LIMITED** outward capital flows
- US capital-owners stopped exporting their capital and, instead, brough it back from European and S American countries
- This led to a **BUBBLE** in the US capital market, invaded by a glut of returning capital (not to mention industrial crises in Europe, notably Germany…)

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Post-1929 Financial Collapse

This bubble popped in October 1929 (Black Thursday 24; Black Tuesday 29)

- *Crash* led to the public suspicion regarding banks
- Direct consequence?
  - Distrust of the banks and the financial system (not necessarily, the GD)
  - Frequent "Bank Runs" followed, with c. 6000 broken banks 1929-22 (c. 25% of existing)

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3. Great Depression

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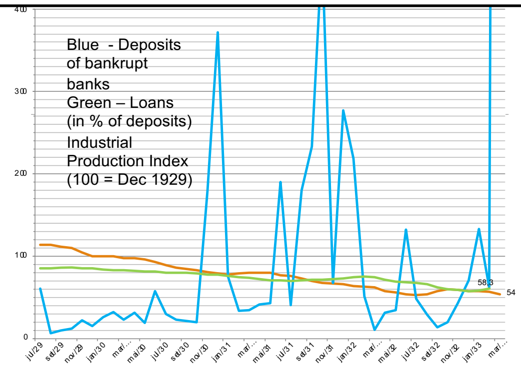

Fonte: Bernanke, 1983.

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From Bank Runs to the GD

- Bank Runs severed the link between savings and investment
- As banks try to keep liquidity, they limit loans, starving companies of capital
- As investment faltered, jobs were destroyed and did not hire

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GD in the US

Abrupt, deep and long recession in 1930-33

High unemployment

Even the recovery of the GDP (complete by 1936) did not eliminate unemployment

Low expectations:
- Consumers
- investors

Ano	FED Discount Rates	GDP growth	Unemployment rate
1928	4,2	1,1	4,4
1929	4,8	6,1	3,2
1930	3,9	-8,9	8,7
1931	2,9	-7,7	15,9
1932	3,5	-1,3	23,6
1933	3,8	-2,1	24,9
1934	2,1	7,7	21,7
1935	2,0	7,6	20,1
1936	2,0	14,2	16,9
1937	1,8	4,3	14,3
1938	1,5	-4,0	19,0
1939	1,5	8,0	17,2
1940	1,5	7,7	14,6
1941	1,5	18,2	9,9

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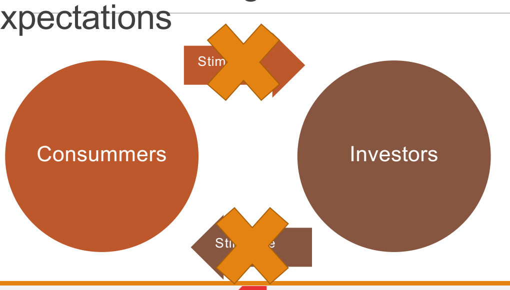
Unemployment and high interest rates increase negative expectations



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Initial US response: More Proteccionism!

US Congress tried to protect American agriculture with higher tariffs (*Smoot-Hawley* 1930 tariff that was being discussed in … September 1929)

US government approved fresh limits for capital outflows and further restrictions on immigration

The main negative effect of proteccionism was the foreign impact

- Other countries retaliated and increased their tairffs and approved more restrictions on American products (thus hurting American exports, firms and workers even more)

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World Spread of the GD (trade)

As the US adopted a protectionist policy to protect domestic employment, countries retaliated

- Wave of tariff increases (aggravating WWI-era changes)

The result is further Deglobalization and less exploitation of comparative advantages

Political and Social concerns, rather than economic efficiency

Table 2. – International Tariff Levels

Country	Average Ad Valorem Equivalent Tariffs 1920–1929	1930–1940
United States		
Total imports	13.0	16.6
Dutiable imports	35.1	44.5
Other countries		
Trade–Weighted Average	9.9	19.9
Canada	13.4	15.2
France	7.1	21.0
Germany	7.2	26.1
Italy	4.5	16.8
United Kingdom	9.8	23.2

Kenwood e Lougheed 1999

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World Spread of the GD (finance)

As the US controlled its capital outflows, countries had little to benefit from keeping the gold standard

All countries abandoned gold in 1933

Devaluations everywhere, increasing exchange rate risk and protectionism

The result was further Deglobalization; non-capitalist economies seemed to be immune to this:

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Distribution of the World Industrial Output in 1913 and 1926-9 (%)

	1913	1926-9	1936-8
USA	35,8	42,2	32,3
Germany	14,3	11,6	10,7
GB	14,1	9,4	9,2
France	7,0	6,6	4,5
URSS	4,4*	4,3	18,5
Sweden	1,0	1,0	1,3
Japan	1,2	2,5	3,5
India	1,1	1,2	1,4
Rest	21,1	21,2	18,7

Kenwood e Lougheed 1999: 173.

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