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Editorial note: In this piece, Professor Horwitz comments on Professor Eggertsson. We hereby invite Professor Eggertsson to reply to Professor Horwitz, and would welcome such reply for publication in the next or any future issue of the journal.

Great Apprehensions, Prolonged Depression: Gauti Eggertsson on the 1930s

Steven Horwitz[1]

ABSTRACT

> *[U.S. Treasury Secretary Henry Morgenthau, Jr.]*: No, gentlemen, we have tried spending money. We are spending more than we have ever spent before and it does not work. And I have just one interest, and if I am wrong, as far as I am concerned, somebody else can have my job. I want to see this country prosperous. I want to see people get a job. I want to see people get enough to eat. We have never made good on our promises…
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> But why not let's come to grips? And as I say, all I am interested in is to really see this country prosperous and this form of Government continue, because after eight years if we can't make a success somebody

1. Charles A. Dana Professor of Economics, Department of Economics, St. Lawrence University, Canton, NY 13617.
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> else is going to claim the right to make it and he's got the right to make the trial. I say after eight years of this Administration we have just as much unemployment as when we started.
> *Mr. Doughton*: And an enormous debt to boot!
> *HMJr.*: And an enormous debt to boot! We are just sitting here and fiddling and I am just wearing myself out and getting sick. Because why? I can't see any daylight. I want it for my people, for my children, and your children. I want to see some daylight and I don't see it…
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> —Transcript of private meeting at the Treasury Department, May 9, 1939, F.D. Roosevelt Presidential Library[2]

Gauti Eggertsson's article "Great Expectations and the End of the Great Depression" in the September 2008 issue of the *American Economic Review* offers an interpretation of the transition from the Hoover to the Roosevelt Administration that will provide ammunition for defenders of the New Deal and others who generally see activist government as the appropriate policy response to major economic declines. Eggertsson argues that the period 1933 to 1937 represented an end of the Great Depression, and that such recovery was driven by a regime change between the Hoover and Roosevelt administrations. The Hoover administration was defined by adherence to three "policy dogmas" that Roosevelt decisively rejected. Roosevelt took actions to make his commitment to rejecting those dogmas credible, and such moves shifted expectations in ways that led to recovery.

The "policy dogmas" in question are ones normally associated with significant limits on government intervention, while their rejection gave Roosevelt much more latitude to expand government activism. Eggertsson contends that the Hoover Administration was defined by its adherence to three "almost universally accepted policy dogmas of the time: (a) the gold standard, (b) the principle of the balanced budget, (c) the commitment to small government" (Eggertsson 2008, 1477). He portrays the Roosevelt Administration, by contrast, as not only rejecting these "dogmas" (and apparently having no "dogmas" of their own), but also as intending[3] to signal a regime change that would change the public's expectations about not just the future magnitudes of important macroeconomic aggregates, but also shift their expectations about the policy-making process itself. Those expectational shifts were, he argues, key to recovering from the Great Depression.

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2. This transcript is also cited in Folsom (2008, 2).
3. Eggertsson implies that the Administration intentionally managed public expectations, for example when he writes: "The key to the recovery was the successful management of expectations about *future policy*" (1476).

He provides a dynamic stochastic general equilibrium model that attempts to show how, if the supposed Hoover regime had continued, so would the slide: “In the absence of the regime change, however, the economy would have continued its free fall in 1933, and output would have been 30 percent lower in 1937 than in 1933…” (Eggertsson, 1506).

The model’s relevance and value stands or falls with the soundness of its representation or explanation of the most important factors in the actual history. I argue that Eggertsson’s research fails on several counts:

1. It is wrong to view the Great Depression as over by 1937. Just as recovery from an illness is a return to one’s normal state of health, economic recovery is a return to economic normalcy. Eggertsson’s recovery is illusory. Even the Roosevelt Administration recognized that there was little in the way of meaningful recovery as late as 1939 as the opening quote from Henry Morgenthau indicates. Also, it is inappropriate to separate the period 1933-1937 from the years that followed.

2. Eggertsson is accurate in his depiction of Hoover as committed to the policy of maintaining the public’s right to convert 20 dollars into an ounce of gold. But that view did not preclude the result that Eggertsson thinks needed to be obtained, namely significant monetary expansion. Moreover, if the traditional terms were too constraining, redefining the gold content of a dollar while maintaining normal convertability was another “gold standard” option. It should be noted that Eggertsson, by treating the monetary regime during Hoover as simply “the gold standard,” follows the fashionable “gold standard” monolithism; he fails to recognize that a more classical kind of gold standard had already been abandoned.

3. As for the two other alleged “policy dogmas,” namely, balanced budgets and small government, they not only were not “almost universally accepted” but they greatly misrepresent what Hoover believed and what his administration did. Hoover’s own track-record and the policies he adopted after the stock market crash belie Eggertsson’s characterization of dogmatic attachment to balanced budgets and small government. Eggertsson’s depiction of the “Hoover” regime contradicts the historical record.

4. By using the phrase “policy dogmas” to describe Hoover’s views while giving Roosevelt’s no specific label, Eggertsson implies that no dogmas guided Roosevelt’s policies. Here too, the historical evidence suggests otherwise. Roosevelt too had his policy dogmas, and they often exacerbated problems, delayed recovery, and weakened the long-run dynamism of the U.S. economy.

5. Yes, the Roosevelt Administration rejected the three positions attributed to Hoover (though in 1932 Roosevelt did promise to balance the budget), and, yes, its bents were decidedly more statist. But it is misleading to view its policies as

anything close to a consistent strategy for recovery. At least in the first term, the Roosevelt administration was much more about long-run reform than about a coherent set of recovery policies, and there is no reason to believe that Roosevelt or his administration had a concerted plan about which specific policies to undertake to achieve long-run reform. Eggertsson (1476) suggests that the regime change was intentionally designed to shift expectations. But much of what Roosevelt did he made up as he went along. The particular policies adopted or proposed by Roosevelt often changed from year to year, season to season, and even month to month.

6. Eggertsson gives no discussion of Robert Higgs' (2006a) work on the debilitating effects of uncertainty regarding rules, which Higgs dubs *regime uncertainty*. Eggertsson flagrantly overlooks the ways in which Roosevelt's policies generated great uncertainty and great apprehension. The broad ideological dogmas of the Roosevelt Administration stepped up the assault on profits, property, and liberty, and involved virulently anti-business propaganda. As Higgs argues, the combination left private investors fearing for their property and the value of their long-term investments. By heightening apprehensiveness, Roosevelt's bold experimentation snuffed out private investment in long-term projects. An electronic search determines that "private investment" never appears in Eggertsson's article.

Will the Real Herbert Hoover Please Stand Up?

If Eggertsson's paper were merely an exercise in modeling, asking what might happen if "an" economy transitioned from accepting to rejecting the three policy dogmas in the midst of a severe recession, that would be one thing. But Eggertsson is declaring an explanation of the Great Depression. He has a duty to portray accurately the policy positions of both Hoover and Roosevelt (as well as the evolving condition of the economy). In the case of Hoover, at least two of Eggertsson's three policy dogmas are severe distortions of Hoover's beliefs and practice.

Eggertsson's portrayal of Hoover as dogmatically committed to a balanced budget and small government is utterly at odds with Hoover's personal history and stated beliefs, as well as the actual policies he put into place while president. Hoover's first major role in government was as head of the Food Administration upon the US entry into World War I in 1917. He leapt into that job with great energy, having long believed that government can and should play a large role in the economy. In 1912, he had supported Teddy Roosevelt and the Progressives for the presidency, and was touted by many, including Franklin Roosevelt, as a potential Democratic presidential candidate in the 1920s. He was a registered

Republican, however, and in 1921 accepted a position as Secretary of Commerce under President Harding, a job that he retained through most of the 1920s.

Hoover vowed to turn what was one of the lowest-profile departments of the federal government into a more visible one, specifically by increased interaction with businesses and involvement in economic policy. Donald Stabile (1986) has characterized his views as a desire to "transform the structure of the US economy from one of laissez-faire to one of voluntary cooperation" (819). In her book *Herbert Hoover: Forgotten Progressive,* Joan Hoff Wilson (1975, 68) summarizes Hoover's economic views this way:

> Where the classical economists like Adam Smith had argued for uncontrolled competition between independent economic units guided only by the invisible hand of supply and demand, he talked about voluntary national economic planning arising from cooperation between business interests and the government… Instead of negative government action in times of depression, he advocated the expansion of public works, avoidance of wage cuts, increased rather than decreased production—measures that would expand rather than contract purchasing power.

When paired with his long-standing antipathy to free trade (65-66), this was hardly the program of a "limited government" or "laissez-faire" dogmatist. Other ideas he championed around this time included "increased inheritance taxes, public dams, and, significantly, government regulation of the stock market" (Rothbard 2008 [1963], 188).

As early as the 1920-21 recession, Hoover was becoming famous for convening conferences with business leaders as a way to use the power of government to generate what he saw as desirable "cooperation" as opposed to individualistic competition. In contrast to Harding's much more genuine commitment to laissez-faire during that recession, Hoover quickly got busy organizing conferences and relief efforts and exhorting businessmen and the public to bring that spirit of "mobilization" and "spontaneous cooperation" experienced during the war to peacetime economic reconstruction. At one conference on unemployment in September of 1921, Harding opened with remarks committing him to keeping the federal government out of such issues, and yet Hoover followed by expounding the need to "do something." The conference leaders, with Hoover's approval, coalesced around a call for more "government planning to combat depressions and to bolster the idea of public works as a depression remedy" (Rothbard 2008 [1963], 192). Historian David Kennedy (1999, 48) describes Hoover's activism this way: "No previous administration had moved so purposefully and so creatively in the face of an economic downturn. Hoover had definitively made the point that government should not stand by idly when confronted with economic difficulty" (see also Vedder and Gallaway 1993, 67-68).

In the 1920s, Hoover used his position as Secretary of Commerce to call for a number of government interventions into the recession, all of which were rejected by Harding and the rest of his Administration. As Commerce Secretary, Hoover also stepped into a number of labor relations issues, trying here also to use the power of government to resolve various disputes. Thus, the ideal of small government was neither "Hoover's" nor "almost universally accepted." Powerful government actors along with many leaders of private industry boosted for American forays in fascism, which was often openly admired.

Eggertsson is largely correct about Hoover's commitment to the gold standard. In numerous speeches at the time, Hoover asserted the importance of gold to a stable monetary system and healthy economy, even after 1929 as the depression began to unfold. The presupposition in Eggertsson's take is that "eliminating the gold standard" (1504) was necessary for reflationary monetary policy. But, as Friedman and Schwartz (2008 [1963], 174-86) first pointed out and Bordo, Choudhri, and Schwartz (2002) have confirmed, the stock of "free gold" (i.e., that portion of the Fed's gold holdings not needed for meeting its minimum reserve requirements or collateral against its various liabilities) during the early 1930s was more than sufficient to support the expansion of the money supply necessary to offset the fall in the velocity of money that was driving down total expenditures and severely exacerbating the problem of bank failures. Moreover, Timberlake (2005, 217) points out that the levels of gold reserves aside, the Fed Board had it within its power to simply "suspend gold reserve requirements entirely" if it had the will to do so. Faulting Hoover for his commitment to "the gold standard" overlooks the ways in which the desired remedy was in the hands of the Federal Reserve at the time without the need to abandon gold convertibility at 20 to 1, much less convertibility entirely. Richard Timberlake (2005) and Lawrence H. White (2008) argue that the more important "policy dogma" blocking reflationary monetary policy was not convertibility to gold nor the traditional rate of conversion, but the Fed's commitment to a version[4] of the Real Bills Doctrine that unfortunately kept the Fed focused on credit conditions to the exclusion of money-supply conditions. Eggertsson's diagnosis of monetary problems as caused by Hoover's commitment to gold never mentions the ruling monetary doctrine at the Fed nor the ample stock of gold. It presupposes that

4. For a defense of the Real-Bills Doctrine in the context of the Great Depression and otherwise, see Hortlund (2006).

sizeable expansion was incompatible with a gold standard of any sort—a presupposition that is probably false.

Hoover's lack of commitment to "small government" and "balanced budget" dogmas would be on display when faced with the 1929 crash. His first moves consisted mostly of calling more conferences of industrial leaders in Washington, the major outcome of which was a pledge by them not to lower wages in the face of the recession so as to maintain "purchasing power." Hoover also enlisted the Federal Farm Board, which was created under his watch in June of 1929, to enhance its role as a cartelizer of American agriculture (Kennedy 1999, 43-44; see also Rothbard 2008 [1963], 228 and Smiley 2002, 13). The Federal Farm Board lent hundreds of millions of tax dollars to farmers and established the Farmers' National Grain Corporation, which bought up wheat at the artificially high price created by the FFB. Kennedy (1999, 44) quotes Hoover as saying of the FFB that they had a "responsibility, authority and resources such as have never been conferred by our government in assistance to any industry." Similar cartel devices were created in livestock and other agricultural products.

By 1930, Hoover was pushing for the maintenance of wage rates even more firmly, and fighting for and signing the Smoot-Hawley Tariff. Viewing Hoover as dogmatically committed to small government will have to contend with his willingness to extend the power of government to regulate the prices and importation and exportation of a huge number of goods under Smoot-Hawley. If his commitment to small government was genuine, it is hard to imagine him fighting for that tariff, even as over 1000 economists objected (see *EJW* Editors 2007). Almost all historians of the Great Depression agree that the tariff was one reason that what was a nasty recession became a more severe depression, yet Eggertsson never acknowledges this example of Hoover's extension of government's power.

Federal government expenditures rose from $4.2 billion in 1930 to $5.5 billion in 1931, a one-year increase of 31 percent. The deficit for 1931 was $2.2 billion, by far the largest peacetime deficit ever (Rothbard 2008 [1963], 263-264). In February of 1931, Hoover signed the Wagner Employment Stabilization Act, which increased expenditures for public works. Despite falling prices, Hoover continued to urge industrialists to maintain wages, a cause helped notably by the Davis-Bacon Act, which limited hours and promised "prevailing wages" in government construction projects. Hoover also tried to help keep wages up by urging Congress to dramatically restrict immigration, further evidence of his readiness to expand the powers of government. By the end of 1931, Hoover was moving to expand public works and government relief expenditures as well as threatening and/or engaging in intervention in the financial and housing markets.

Contrary to the impression that Eggertsson creates, Hoover was throughout this period rather unconcerned with the federal government's budget deficit. In fact, Eggertsson (2008, 1487) offers only two very thin pieces of evidence for Hoover's supposed dogmatic adherence to balanced budgets. The first is a quote from a December 1930 statement (which he misdates as July):

> For the Government to finance by bond issues deprives industry and agriculture of just that much capital for its own use and for employment. Prosperity cannot be restored by raids on the public Treasury.

The context of that statement was Hoover complaining about bills being introduced that would have greatly increased government expenditures "beyond the sums which I have recommended for the present and next fiscal year by a total of nearly $4,500 million." Furthermore, Hoover claims:

> The gross sums which I have recommended to carry on the essential functions of the Government include the extreme sums which can be applied by the Federal Government in actual emergency employment or relief, and are the maximum which can be financed without increase in taxes.

So Hoover's complaint here is about expenditures *beyond* what he had already proposed for 1931, which eventually amounted to a 31 percent increase over those of 1930. In fact, Hoover explicitly rejected dogmatic commitment to a balanced budget in May of 1931. Kennedy (1999, 79) reports on Secretary of State Henry Stimson's diary note that Hoover argued "strenuously against the budget balancers in his own cabinet. 'The President likened it to war times…He said in war times no one dreamed of balancing the budget. Fortunately we can borrow.'" This calls into question Eggertsson's (1482) claim that Hoover's deficit "was not a deliberate policy," which he contrasts with Roosevelt's deliberate deficits. It also suggests the regime change that is central to Eggertsson's argument is mostly illusory.

There are similar problems with the second piece of textual evidence he presents for Hoover's commitment to a balanced budget, which comes from a speech from September of 1931. It is important to remember that this speech was given toward the end of a year in which Hoover was *already* running a $2.2b deficit, the largest peacetime deficit in US history up to that point. Eggertsson (1487, his ellipses) quotes Hoover as follows:

> Every additional expenditure placed up on our government in this emergency magnifies itself all out of proportion into intolerable pressures, whether it is by taxation or by loans. Either loans or taxes […] will increase unemployment. […] We can carry our present expenditures without jeopardy to national stability. We can carry no more without grave risks.

Examination of the speech raises further concerns about Eggertsson's scholarship. Eggertsson omits the opening clause of the sentence, immediately preceding the quoted material. Hoover (1931) said "Whatever the deficit may be and in whatever manner it may ultimately be met, every additional expenditure…" Thus, not only does Eggertsson misquote the speech by writing "Every" with a capital E, he has deliberately omitted Hoover's immediately proximate approval of an historically large budget deficit. Furthermore, earlier in the speech, Hoover (1930, my emphasis) refers to the "high and *necessary* extra burden of public works in aid to the unemployed, of aids to agriculture, and …increased benefits and services to veterans" as elements of expenditure already being undertaken. The larger context of that speech is Hoover, again, saying that a deficit in and of itself is not necessarily a big problem, but that at that point he had gone as far as he was willing to go. Note too that this speech calls into question his supposed commitment to small government, given the number of programs he lists as part of the "high and necessary extra burden of public works."

The final nail in the coffin of Eggertsson's attempt to contrast so starkly the Hoover and Roosevelt Administration's policy regimes is the set of proposals Hoover offered in 1932, the year before the transition. Kennedy (1999, 83) refers to this set of programs as "Hoover's second program" and also notes that it "lay the groundwork for a broader restructuring of government's role in many other sectors of American life, a restructuring known as the New Deal." (See also Rothbard (2008 [1963], ch. 11, who terms this "The Hoover New Deal".) Hoover's policies consisted of several major new government programs and their associated expenditures, including a "Reconstruction Finance Corporation," making more banks eligible for discounting at the Fed, various programs to help mortgage holders, larger federal public works, more immigration restrictions, and loans to the states. Many of these measures anticipated precisely those that Roosevelt would put into place in the early days of his New Deal. Given all of this activity, describing the break between Hoover and Roosevelt as a "regime change" that rejected the dogma of small government is severely inaccurate. Eggertsson is right, however, that 1932, at least, saw Hoover raising the budget deficit as a bigger concern, leading to him pairing those expenditures with the Revenue Act of 1932, which raised taxes dramatically for many citizens. The higher tax rates yielded lower tax revenues, with the result being a somewhat smaller but still historically large deficit of $1.4b at the federal level. So despite his professed concern about the deficit, Hoover's actual policies did little to cause it to disappear—just as Roosevelt's campaign talk of 1932 did little to reduce deficits thereafter.

Hoover's own recapitulation of what his administration had done in response to the depression speaks for itself. In his August 1932 acceptance of the Republican presidential nomination, Hoover (1932) said:

> We might have done nothing. That would have been utter ruin. Instead we met the situation with proposals to private business and to Congress of the most gigantic program of economic defense and counterattack ever evolved in the history of the Republic. We put that program in action… These programs, unparalleled in the history of depressions of any country and in any time, to care for distress, to provide employment, to aid agriculture, to maintain the financial stability of the country, to safeguard the savings of the people, to protect their homes, are not in the past tense—they are in action…No government in Washington has hitherto considered that it held so broad a responsibility for leadership in such time.

With just months to go in his term, Hoover clearly saw the work he had done over the prior three years as being anything but adherence to Eggertsson's "almost universally accepted policy dogmas." True to form, Hoover had approached the onset of the Great Depression with an aggressive expansion of government, including record budget deficits and an enormous increase in tariffs and income taxes, as well as an attempt to strong-arm businesses into not cutting wages in the face of a severe deflation, itself the result of mismanaged government intervention in the monetary system. The Roosevelt Administration was hardly a "regime change," as Kennedy (1999, 118) observes: "If Roosevelt had a plan in early 1933 to effect economic recovery, it was difficult to distinguish from many of the measures that Hoover, even if sometimes grudgingly, had already adopted." Eggertsson's portrayal of the Hoover presidency makes reckless mischief with the historical facts.

The Ideology of the New Deal

Eggertsson is more accurate in characterizing the Roosevelt Administration, but there too we find serious problems. First, Roosevelt is said to have rejected the "policy dogmas" of Hoover and, by implication, had no policy dogmas of his own. Second, he strongly implies that Roosevelt's policies were part of a deliberate strategy to turn around expectations and thereby generate recovery. He is wrong on both counts.

We may distinguish levels of policycraft. Higher up are guiding beliefs or ideological views held by policymakers, and, lower down are the particular policies adopted as means toward the broader goals, values, or visions. Thus, when Eggertsson refers to the supposed "policy dogmas" of Hoover, he is talking of guiding beliefs. If one is committed to "smaller government," there are a number of ways to advance that goal. If one is ideologically committed to a balanced budget, one could pursue a variety of combinations of taxation, expenditure, and segniorage. Eggertsson seems to suggest that Roosevelt had few "dogmas" of the first sort, rather just a generic pragmatic benevolence, but a package of specific policies to advance the generic goal of well-being. The reality was pretty much just the opposite: Roosevelt *did* have a guiding set of ideological beliefs and goals (dogmas, if you wish) but he was constantly improvising as to what sorts of concrete policies would best enable him to advance them.

The Roosevelt Administration had strong ideological commitments that guided its decision making. Central to Roosevelt's rise to power and to the shape of his presidency was the group of intellectuals known as the "Brain Trust." In early 1932 as he was putting together his campaign, Roosevelt decided to put less emphasis on the traditional advisory group of politicians and businessmen and instead looked for the best minds in the universities as a source of ideas. His various friends and political advisors put him in touch with a group of intellectuals that included Raymond Moley, Adolf Berle, Samuel Rosenman, Hugh Johnson and Rex Tugwell. This group of progressives had a long-standing relationship with one another, much of it centered around magazines such as *The Nation* and *The New Republic*. They reflected the collectivist values and statist ideas of the Progressive Era, notably that sufficiently wise and good-hearted people with the relevant data could use the power of government, especially economic planning, to improve on free-market coordination. Major Brain Trust figure Rex Tugwell, along with other intellectuals of the same kind of statist mindset, went to the Soviet Union in 1927 to explore alternatives to US-style capitalism (Shlaes 2007, ch. 2). Though not full-bore collectivists in the Soviet tradition, they all believed that scientific management could do the free market one better.

Among the dogmas Roosevelt's advisors clung to was the belief that the depression was caused by underconsumption. The variants were many, but the general argument was that wealth in the 1920s had flowed to the rich and not the poor, leaving the latter without the means to consume all of the production that had characterized the era. This supposed mismatch between consumption and production was the result of a lack of coordination, and was inevitable under free enterprise. Other versions of the theory argued that overly intense competition was part of the problem as it encouraged the expansion of production and the lowering of prices that cut into corporate profits. Also, members of the brain trust, and Roosevelt himself, strongly believed that greed, particularly by those who became wealthy in the stock market and other forms of speculation, was a root cause of the depression, a belief that lead to a consistent pattern of scapegoating of wealthy and prominent businessmen. Such jealousy and hostility towards independent and possibly dissident islands of wealth and cultural power is typical of the mentality of progressivism, fascism, and socialism. Finally, it was a further article of faith among Roosevelt and many of his advisors that, with the closing of the western frontier, the possibilities for growth were limited, especially for the poorest, with the ethical implication that those who had made their fortunes would be made to "share" them with the rest of society. Many of these beliefs were reflected in portions of Roosevelt's speech in July of 1932 accepting the Democrats' nomination for the presidency (Folsom 2008, 37). In a speech two months later in San Francisco, Roosevelt reiterated many of these themes, adding that his administration would have to face "establishing markets for surplus production; of meeting the problem of underconsumption; distributing the wealth and products more equitably and adapting the economic organization to the service of the people" (Roosevelt quote at Folsom 2008, 41). The Roosevelt team was hardly dogma-free when it came to both diagnosing the Great Depression and planning rehabilitation.

Yet the diagnosis of Roosevelt's brain trust was not that the US economy had caught a transient malady that emergency responses could cure. Rather they saw the Great Depression as the manifestation of chronic problems in the US economy and capitalism more generally. Shlaes (2007, ch. 9) argues that they also saw the election of Roosevelt as the opportunity to put into place a variety of structural and institutional reforms that would address those chronic problems. Instead of a set of policies focused on how to *recover* from the particular episode of the Great Depression, Roosevelt's advisors were creating a set of *reforms* that would transform the very structure of the US economy for the long haul. In his autobiography treating his involvement in the New Deal, Ray Moley (1966, 292) wrote that during the NRA's creation, "The concept of recovery as distinguished from reform was forgotten." Putting aside the question of whether their diagnosis and prescriptions were accurate, there can be little doubt that they were driven by a set of ideas about the causes of the Great Depression and the structural cures required.

This matters for Eggertsson's argument because numerous observers of the New Deal have argued that it was much more about reform than recovery.[5] Viewing Roosevelt's assumption of power as a shift in tactics in the management of expectations is problematic because many of the actors in question did not see what they were doing as about short-run counter-cyclical policy (recovery) but as about long-run structural reform. Those reform proposals were guided by a set of deep-seated beliefs on the part of Roosevelt's advisors, not a "dogma-free" attempt to remedy the present economic crisis.

Roosevelt the Experimenter

Within the broad set of structural changes thought desirable by the advisors, there was ample room for differences in policy specifics. Even with the broad contours of the problems and the solutions identified, how the administration chose to go about enacting policy could vary. Roosevelt himself referred to his preference for "bold, persistent experimentation" during the early days of his campaign in 1932 (Roosevelt 1932). His willingness to try things, see if they worked, and change courses if they failed certainly is to be preferred to stubbornly sticking to policies that continue to fail.[6] That experimentation poses two problems for Eggertsson's argument, however. First, it suggests that there was not the sort of coherent, organized regime that he suggests in the article. Second, Eggertsson ignores the degree to which that experimentation itself prolonged the depression and made it more severe than it would have been under a less experimentalist regime.

Examples of Roosevelt's ad hoc approach to policy are not hard to find. During the famed first 100 days, Roosevelt talked up almost every possible policy option as part of the reform agenda he wished to pursue. The list of programs is itself impressive in its sheer scope, which reflected an acceleration along the statist path trod by Hoover. The range of programs was full of contradictions, from slaughtering millions of baby pigs and tearing up acres of cotton under one program while other programs were trying to feed and clothe the impoverished, to the ways in which different programs affected prices and international trade. As Shlaes (2007, 149) argues, the key for Roosevelt was that "Americans must know

5. This point is a running theme in Shlaes (2007) and Best (1991). Kennedy (1999) titles an entire chapter "A Season for Reform," and Smiley (2002, 97) writes: "There is little evidence that recovery was first on the agenda of any of these competing groups [of FDR advisors]; rather, all intended first to reform industry in one way or another, in order to move to the 'correct' path of recovery."
6. The "experimental" nature of the Roosevelt presidency is supported by Moley (1966, 224): "We were wide open to the influx of ideas—new ones and old. Anything seemed acceptable that appealed to our common sense and was worthy of a trial."

Washington was doing something. If there were contradictions between experiments and within them, well, that did not matter."

Eggertsson focuses on Roosevelt's decision to abandon "the gold standard," so as to push up prices. This decision is part of the set of policies that Eggertsson suggests was a coordinated "regime change" on the part of Roosevelt and his advisors. But Roosevelt's approach to the monetary regime was hardly systematic. Shlaes (2007, 147-148) describes how the administration was setting the price of gold in 1933:

> Over the course of the autumn, at the breakfast meetings, Roosevelt and his new advisers experimented alone. One day he would move the price up several cents; another, a few more.
>
> One morning, FDR told his group he was thinking of raising the gold price by twenty-one cents. Why that figure? his entourage asked. "It's a lucky number," Roosevelt said, "because it's three times seven." As [Treasury Secretary] Morgenthau later wrote, "If anybody knew how we really set the gold price through a combination of lucky numbers, etc., I think they would be frightened."

Shlaes (2007, 160ff) also describes the way Roosevelt handled the delegation sent to an international monetary conference in June of 1933. He sent a number of different representatives, but could not decide on what outcome he wished them to reach in their negotiations. He sent contradictory telegrams to different members of the delegation, including directing them not to accept an agreement with France and the UK that they had earlier negotiated. After having promised them he wanted the gold standard maintained, Roosevelt switched views yet again, leaving his delegation in the lurch. One member asked Raymond Moley to ask Roosevelt "not to change his policies again, because his sudden turns had been exceedingly embarrassing" (as quoted in Shlaes 2007, 163). Meanwhile, from early June to mid-July, the stock market was on a 10 percent slide. August found Roosevelt issuing a variety of executive orders with respect to gold, with new ones coming days after previous ones, often directly contradicting them. These are hardly the actions of president using a consistent set of policies to engineer the public's expectations—except in the sense that they would be made to expect a government full of caprice and presumption.[7]

One of the reasons for Roosevelt's ongoing experimentation was that he was constantly listening to different voices among his advisors. Roosevelt was

7. Again, see Moley (1966, 229): "But if the country could have known how unclear we were [about economics], the tide of confidence [from the banking system rescue] would have frozen in its course."

notoriously fickle about who he listened to and trusted, and when experiments variously failed, he was highly likely to decide next that a different member of the brain trust had the right ideas. As a new voice captured his attention, new policy experiments came forth. Although the message coming from all of those advisors was broadly consistent in the penchant for greater statism, the particular policies enacted in his first term changed with the vicissitudes in Roosevelt's hunches and could hardly be treated as a systematic shift in regimes in the way that Eggertsson suggests.

The ad hoc nature of Roosevelt's economic policy became even clearer during his run for re-election in 1936. It was fairly clear by this point that the variety of policy experiments he had tried in the three previous years had failed to make more than a dent in the depression, as unemployment remained near 20 percent and key macroeconomic variables were nowhere near their pre-depression levels. Out of policy options rooted in any real framework that would address the problems, Roosevelt instead turned to coalition building and using new programs neither for *recovery* nor *reform*, but for the third "r": re-election. As the public continued to demand more from the federal government, Roosevelt shrewdly began to craft policies that benefitted a bloc of voters and interest groups that would define the Democratic coalition for decades to come. He ratcheted up his attacks on the "economic royalists," on whom he blamed the depression and the lack of recovery. The combination of the rhetoric of class warfare and policies (e.g. Social Security) that attracted large blocs of voters was sufficient to win him a landslide re-election. The policies in question, however, had little to nothing to do with recovery from the depression. What was once experimentation and structural reform had now morphed into a cruder political calculus. Roosevelt's bold, persistent experimentation is not just a refutation of describing his policies as a coherent recovery strategy, it also raises the question of whether that very experimentation was a cause of the remarkable prolongation of depression.

Regime Change or Regime Uncertainty?

Eggertsson's paper, like many studies of the New Deal, takes a peculiar view on what constitutes recovery. There is admittedly a great deal of debate over these issues, but it is not unreasonable to argue that the two most important indicators of the economy's macroeconomic health, real GNP per capita and the unemployment rate, did not return to their 1929 levels until at least 1939 in the case of GNP and at least 1941 in the case of unemployment. The GNP date reflects "back to 1929" levels and not "back to where trend would have been in 1939." Back to trend would have taken several years more, depending on the data one uses. Unemployment as conventionally measured remained above 14 percent through 1939. Even if one excludes those in government make-work programs from the unemployment rate, it remains above its 1929 figure until the early 1940s (Hughes and Cain 2007, 481).

Even thinking generously, recovery from the Great Depression did not occur until at least six years after Roosevelt assumed power, and perhaps as many as 15 years. It is true that annual real GNP figures bottomed out in 1932 and 33, with the subsequent years showing improvement. Unemployment was worst in those years as well, but saw little sustained progress back to normalcy in the mid and late 1930s. So the question is why one should even view the Roosevelt years as an example of a successful recovery process, given that it took anywhere from 6 to 15 years to get the economy back to pre-depression levels of the major macroeconomic indicators.

In the 1936 election, things were still bad enough that Roosevelt had ratcheted up his anti-business rhetoric, blaming the private sector for the ongoing depression. The economy indeed had put the worst in the past by the time the first full year of Roosevelt's first term was complete and the relative growth that characterized the next few years was significant, but in the larger context of the depression, it was not nearly enough to lead to meaningful recovery, especially with respect to unemployment. The Administration itself was aware of how little they had really accomplished on the latter issue. Like a mountain that rises from the floor of a deep ocean, even the growth that Eggertsson points to was still not enough to bring the economy back above the surface from which it had descended. The change from Hoover to Roosevelt hardly results in any sort of transition to economic normalcy.

It is true that by some measures the US economy had improved over the first several years of the Roosevelt Administration. Three points are worth making. First, it is always hard to disentangle how much of the improvement was due to any regime change under Roosevelt and how much was due to underlying market forces toward adjustment and correction.

Second, the Fed's monetary loosening and the recovery of the banking system were also sources of recovery, independent of the New Deal programs per se. Eggertsson rightly identifies importance of the monetary expansion that came under Roosevelt, but wrongly characterizes this as somehow an exclusive view of that administration. There was healthy debate among economists of the 1930s over monetary policy, with the reflationary position being very much in the mix.

Finally, measured aggregates do not well distinguish between productive and unproductive expenditures. The New Deal could have indeed paid people to dig holes in the ground and fill them up as a way of increasing GNP, but that would hardly have made the population better off. Employment aggregates can even be quite misleading about employment. By measuring "hours worked" rather than "unemployment," Higgs (2009) shows, we get a more accurate picture of the state of 1930s labor markets. He demonstrates that labor hours stayed flat from 1932 to 1934, then rose until 1937, dipping in 1938, before rising again. Despite that increase, he concludes that "even as late as 1940, total hours remained below the 1929 level by 6 percent, and only in 1941, with the population vigorously engaged in mobilization for war, did total hours exceed the 1929 value, by 3 percent" (Higgs 2009, 4). Looking at labor hours confirms the observation by Morgenthau in the opening quote: six or seven years of New Deal programs had not caused employment to recover to pre-Depression levels. Whatever the aggregates say, this was not much recovery at all.

One of the questions that any discussion of the effectiveness of the New Deal must confront is why the return to health was so drawn out. If New Deal policies are being claimed to serve as a model for recovery (rather than reform), it is reasonable to ask why we should adopt an approach that took anywhere from 6 to 15 years to get the private sector back to pre-depression levels, much less trend. Serious engagement with this question is absent from Eggertsson's account.

He makes no effort to grapple with two other relevant arguments of Robert Higgs.[8] First, Higgs (2006a) has argued that it was the policies of the New Deal itself that prolonged recovery by creating what he has termed "regime uncertainty," which refers to the way in which a barrage of innovation in policy, especially innovations inimical to freedom, create uncertainty about the rules of the game, uncertainty that in turn retards private investment, particularly in long-term assets, and hence retards economic growth. Second, Higgs (2006b) argues that true recovery did not take place until after World War II. He says that highly non-standard conditions during the war distorted the meaning of standard macroeconomic data in ways that made the economy look to naïve eyes more healthy than it was.

The regime-uncertainty argument takes its start from the aforementioned legal and cultural assaults on private enterprise and individual liberty. Higgs points out that one of the worst performing variables of the depression years was private investment. Gross private investment virtually disappeared from 1929 to 1933, and then began a very slow recovery that by 1941 was still not quite where it was in real terms in 1929. It is not until the conclusion of World War II that private investment exceeds pre-depression levels. Further, as Higgs (2006a, 7) explains:

8. Although the Higgs papers were published in one volume in 2006, the core arguments of the individual papers cited were published in 1992 and 1997, making them very much available to someone writing in the last few years.

> One appreciates even better the deficiency of investment in the 1930s by considering net, rather than gross, investment… In 1929, when [gross private investment] was $16.2 billion, net investment was $8.3 billion. Net investment fell precipitously to $2.3 billion in 1930 and then became negative during each of the following five years. In the period 1931-35, net investment totaled *minus* $18.3 billion… For the eleven years from 1930 to 1940, net private investment totaled *minus* $3.1 billion. Only in 1941 did net private investment ($9.7 billion) exceed the 1929 amount.

Conventional macroeconomic aggregates such as GDP or GNP tell a different story because they include the large increase in government expenditures that characterized this period. If the goal of depression policy is to increase GDP, then government spending programs will do so virtually by definition. However, if one is concerned with how to improve the performance of the private sector, then one needs to look at the relationship between that government spending and private sector performance. The wisdom that has come down to our own time is that government spending can "stimulate" an increased flow of private sector spending through various multiplier processes. Higgs turns this story on its head.

The interaction between the public and private sector is somewhat more complicated than C + I + G might indicate. Public policies can have a definite effect on the way in which the private sector behaves. Private investors are most willing to take on the long-term investments necessary for economic growth when they perceive that they operate in an environment in which their property and contracts will be respected, where the rules of the game are known and relatively stable, and where they expect relative stability or predictability in the value of money. Higgs argues that these elements were not only significantly weakened during the 1930s by a whole variety of policies associated with the New Deal, including the expansion of government spending and unshackling of the money supply from gold that Eggertsson celebrates, but that private actors knew not when the barrage of changes would end, or what the rules would be just a few years forward. Again, "private investment" does not appear in Eggertsson's article.

The most ambitious of the early New Deal programs, such as the NRA and AAA, were particularly disconcerting, as they were perceived as establishing powers that would continually threaten the property rights of industrialists and farmers. In these programs the reform and planning mentality was on full display. Using public-opinion data Higgs shows that many Americans anticipated continual movement toward fascism. Hugh Johnson, who was in charge of the NRA, was particularly aggressive in his attacks on big businesses as well as his decisions to target various smaller entrepreneurs who violated NRA codes. Johnson, as well as Roosevelt, used war rhetoric to drive support for various programs, especially the NRA (Shlaes 2007, 151). Johnson compared the way in which housewives expanding their spending would be as heroic as the troops at the Argonne in World War I. He also referred to those who refused to participate in the NRA's codes as "Judases" who have "betrayed the confidence of the President and the people of this nation" (Johnson 1935, 264). Such statist programs and propaganda continued to retard the recovery of private investment.[9]

Beyond the early New Deal, the later programs, along with Roosevelt's increasingly shrill anti-business rhetoric starting in the 1936 campaign, continued to make private investors very nervous about what was to come. They had also seen the more systematic destruction of private property rights in Russia, Italy, and Germany, and were well aware that the Roosevelt crew had spoken admirably about elements of the economic policies of all three societies (Shlaes 2007; Goldberg 2007).[10] The polling data along with data on the spread between short and long-run interest rates, masterfully assembled and integrated by Higgs, strongly support the view that aggressive and unrelenting reform and statist attitudes were the cause of the low levels of private investment throughout the 1930s. Private-sector actors were very fearful of what the future might hold and consistently unable to commit to long-term investments when policies changed from day to day and when crucial data such as the price of gold were being decided on mere whim. The very factors that Eggertsson points to as being virtues of Roosevelt's policies are among those that Higgs sees as their vices. Government activism, busting forward under Hoover and gaining momentum under Roosevelt, spelt regime uncertainty and it prolonged rather than cured the Great Depression. Eggertsson spins a tale about renewed expectations bringing recovery by 1937; Higgs suggests a much more learned and sensible story about expectations made murky and dreadful by surging statism, making real recovery impossible.[11]

Higgs' other argument suggests that true recovery from the depression did not occur until after the conclusion of World War II, casting further doubt on Eggertsson's model and its defense of Roosevelt's shift in policies. Higgs (2006b) offers a number of powerful arguments for his claim that a standard reading of the

9. Cole and Ohanian (2004) make the argument that the New Deal programs might have extended the Great Depression by as much as seven years.

10. As both Shlaes and Goldberg note, admiration in the United States for the fascist experiments, especially Mussolini, was hardly unique to the political left, as a good number of conservatives and businessmen admired them as well.

11. In a study of the causes of the Great Depression published in 1937, Phillips, McManus, and Nelson (1937, 242) wrote: "[C]onditions in the investment market are still [early in 1937] such that extensive long-term investment is not being made." Contemporary observers saw the problem Higgs points to and recognized that neither private investment nor employment could be described as "recovered" by 1937.

typical macroeconomic measures vastly over-rated the health of the economy during World War II. I will not sketch all of the arguments, which were originally published in the *Journal of Economic History* in 1992 and have never been challenged by any scholar.

Higgs computes an alternative measure of real personal consumption per capita using Friedman and Schwartz's Net National Product deflator. That alternative measure tries to take into account the effects of price controls and other elements of wartime. Using that deflator, Higgs (2006b, 71) shows that real personal consumption per capita was essentially flat from 1939 to 1945, rising only a total of 6.8 percent over the 6 year period. Only in 1946, with the conclusion of the war, does it start to rise significantly. Combined with the continued low level of private investment during the war, it is hard to make the case that even if Roosevelt's New Deal policies did not end the depression that his war spending did. Neither seems plausible if Higgs is correct.

Higgs offers a war-adjusted concept of GNP that builds from Kuznets' "peacetime" GNP that deleted all war outlays and then further subtracts "gross war construction and durable munitions" (Higgs 2006b, 65). By this measure, GNP in 1945 was just 5 percent higher than in 1939, hardly evidence of true economic recovery. By 1949, GNP had improved 47.5 percent over 1939, as many of the wartime controls were removed, military spending slacked off, and returning soldiers added their production back to the economy. So even as World War II might have increased traditional measures such as GNP and employment, it is not at all clear that it led to a revitalization of the private sector in the process any more than did the New Deal spending. The ultimate recovery of the private sector in the US economy took place when the federal government stopped trying to cure the disease. The interventions circa 1939 were largely retained, but by the late 1940s people regained confidence. They knew what to expect in terms of the rules that would apply in the future. The Hoover-Roosevelt-wartime chaos seemed to have passed. Real prosperity finally returned.

In addition to rules uncertainty, another simple and powerful explanation for the protracted high unemployment rates of the 1930s is, as most fully developed by Vedder and Gallaway 1993, a work sometimes unfairly neglected, the various actions and policies that prevented wages from falling in the face of the monetary and price deflation. During his presidency, Hoover put into practice his 1920-21 idea of trying to forestall wage cuts during a recession. Now as president, he did so by gathering major industrialists at the White House and pressuring them to maintain wages and thereby purchasing power. One can also view the Smoot-Hawley Tariff as an attempt to protect labor in industries facing lower-wage competition from abroad. These Hoover-years policies certainly help to explain the quickly rising unemployment rates documented earlier.[12] Forward into the

Roosevelt years, the NRA policies as well as other New Deal legislation such as the Wagner Act, continued the Hoover tradition of government activism to support wages, with unemployment rates lingering in the 15 to 20 percent range for most of the 1930s.[13] When combined with Higgs' work, the wage/price-interventionism argument (which is also offered by Cole and Ohanian 2004) fits the judgment that there was very little actual recovery, and that the cause of the ongoing malaise was a combination of obstruction and rules uncertainty, created by a variety of government policies and the ideological tone of official speech and action.

Here, regarding the genuine recovery and the ideological shift coming out of the Second World War, I might add a historical speculation of my own, a speculation that surely is not both sound and original with me: Despite its uneasy and pragmatic alliance with the Soviets' communist regime, the war against Germany's national socialist regime, Italy's fascist regime, and Japan's totalitarian regime was mobilized and waged to a significant degree as a contest of freedom versus tyranny, despotism, and collectivism. It was not only the passing of Roosevelt in 1945, but also the ideological drama of the war that likely quieted American trends toward statism and rehabilitated rules certainty, confidence, private investment, and American economic vibrancy.

Conclusion

Gauti Eggertsson characterizes the period 1933-1937 as an economic recovery, but such characterization does violence to the idea of recovery as return to economic normalcy. The construction of a sophisticated model and the apparent need to demonstrate the efficacy of Roosevelt's purportedly different-than-Hoover's policies eclipsed the duty to mind the historical truth of the matters in question. The paper is full of technical wizardry but terribly wrongheaded in its presuppositions, claims of relevance, economic analysis, and policy implications. Two of the "policy dogmas" that Eggertsson attributes to Hoover were neither apt descriptions of Hoover's own views and actions, nor were they "almost universally accepted." Hoover was no devotee of small government and was not afraid of budget deficits, at least not moderate ones. Yes, he was committed to

12. In a paper forthcoming in the *Journal of Economic Theory*, Ohanian (2009) offers both extensive documentary evidence from Hoover's memoirs and the historical data to argue that Hoover's interventions in the manufacturing labor market "substantially depressed the economy, reducing aggregate output and hours worked by about 20 percent" (p. 3). He bluntly claims that Hoover was responsible for starting the Great Depression.

13. See the excellent discussion of the effects of New Deal labor laws in Powell (2003, ch. 14).

gold convertibility, but contrary to Eggertsson's presupposition, abandoning "the" gold standard was not necessary to avoiding the monetary collapse, nor to curing it. Roosevelt had dogmas of his own, but within them came a hodge-podge of ad hoc policies that could hardly be called a coherent regime and, in any case, was not even focused on recovery per se. Finally, the statism that ramped up under Hoover and grew to virulence under Roosevelt was the basic reason recovery never came during Roosevelt's lifetime. True recovery did not take place until after World War II when certainty of the rules, albeit now much more statist, was restored.

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About the Author

Steven Horwitz is Charles A. Dana Professor of Economics at St. Lawrence University in Canton, NY and an Affiliated Senior Scholar at the Mercatus Center in Arlington, VA. He is the author of two books, *Microfoundations and Macroeconomics: An Austrian Perspective* (Routledge, 2000) and *Monetary Evolution, Free Banking, and Economic Order* (Westview, 1992), and he has written extensively on Austrian economics, Hayekian political economy, monetary theory and history, and the economics and social theory of gender and the family. His work has been published in professional journals such as *History of Political Economy*, *Southern Economic Journal*, and *The Cambridge Journal of Economics*. He has a PhD in Economics from George Mason University and an AB in Economics and Philosophy from The University of Michigan. He is currently working on a book on classical liberalism and the family. His email is sghorwitz@stlawu.edu.

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