



## Interview with Price Fishback

The term “uncharted territory” is getting a workout these days. The recent recession was so deep that many have found themselves at a loss trying to predict the way forward. In thinking about the future, it’s often useful to recall lessons from the past.

Economist Price Fishback has made a career of that practice. He has become one of the nation’s go-to experts for explaining the differences and similarities between the Great Depression and the Great Recession. He’s blogged about it for the *New York Times* and been quoted by many other news outlets on the same topic. His latest research delves into the microeconomics of the New Deal, examining the myriad programs introduced in the 1930s and ferreting out which ones worked, and which didn’t.

For all the doubts about the nation’s ability to recover from this recession, Fishback is firmly in the optimists’ camp. If history is any guide—and Fishback certainly believes it is—then the evidence points in favor of a healthy economy for generations to come.

Fishback is the Thomas R. Brown Professor of Economics at the University of Arizona. He serves as a research associate with the National Bureau of Economic Research and as co-editor of the *Journal of Economic History*. Mark Sniderman, chief policy officer at the Federal Reserve Bank of Cleveland, interviewed Fishback at the Bank on August 26, 2011. An edited transcript follows.

**Sniderman:** *Let's start by having you characterize for us the period that we now refer to as the Great Depression. What was it like from an economic perspective; its impact on people?*

**Fishback:** At the time, people thought it was going to be a normal recession, and then it just kept on sliding downward. They didn't know exactly what was going on. There were all sorts of differences of opinions on when the economy would start to improve. Real output in the economy dropped by 30 percent over four years. In other words, in 1933 they were producing only 70 percent of what they had produced in 1929. It was as if you had cut off the western half of the United States in terms of output.

Unemployment levels that started out around 2 percent in late 1929 went up to 10 percent in 1930, then to 16 percent in 1931. And then they were over 20 percent for four years, from 1932 to 1935. The rates dropped back down to 14 percent in 1937, and then they skyrocketed back up to 19 percent in 1938. We don't see less than 10 percent unemployment until 1941.

Here you have this economy that is totally falling apart. However, if you could hold onto your job, you actually did reasonably well during the Depression because of the tremendous deflation. The price level dropped 30 percent between 1929 and 1933. People could buy a great deal more with a dollar in 1933 than in 1929. But the problem was holding onto your job.

The Depression lasted so very long that there were people unemployed for five or six or seven years. It devastated some household heads. Many people moved back in with their families or friends. People reverse-migrated back to rural areas and lived with family on farms. There was a surge in the number of "hobos" and people just traveling around. Somewhere between 1 and 2 percent of the population became common vagrants. People were sleeping underneath their "Hoover blankets," or newspapers they found on the street.

The Depression just destroyed people's confidence in what was going to happen. In the United States in most time periods, people have been very optimistic about what is going to happen in the future. There are always some people who are in trouble, but generally we've had an average growth rate in per capita income of 1.6 percent per year since 1840. That includes all the depressions.

Given that kind of growth, the Great Depression is very unusual in American history. People kept expecting that things would get better because income typically has doubled about every generation or so. But 10 years of depression with millions of people who thought they had done everything right finding themselves unemployed will shake anybody's confidence.

**Sniderman:** *At the time the Great Depression set in, was there much expectation about the federal government playing a role?*

**Fishback:** Before the Depression, welfare policy and labor policies were all the responsibilities of the local and state governments. What was so unusual about the 1930s was the idea that the federal government would get involved in providing relief to the poor and unemployed. It was the first time that federal officials thought of the economy as being more than a group of local economies. They argued that the federal government should get involved because this was a national emergency.

The federal government's primary role up to that time had been to provide national defense. We created a central bank in 1913 with the Federal Reserve. There was some federal regulation for interstate commerce like railroads and various foods and drugs traded across state lines. But there wasn't really a sense that the federal government was going to come in and use spending to stimulate the economy. Those were Keynesian notions that developed with John Maynard Keynes' writings in the early and mid-1930s. The typical person's attitude toward government was quite different in 1900 than it is today.

The federal government was probably spending about 4 percent of GDP in 1929. State and local governments were probably spending another 10 percent of GDP. It was a whole different time.

**If you could hold onto your job, you actually did reasonably well during the Depression because of the tremendous deflation.**

Bob Higgs, my thesis adviser, wrote a great book, *Crisis and Leviathan*. He argues that there was a real change in attitudes toward government associated with three major crises. World War I was the first big crisis, followed by the Great Depression of the 1930s, and then World War II. In each case people wanted [the government] to respond quickly. They did not want to trust the markets to help them move quickly because it is really expensive to try to produce things quickly.

Armen Alchian [emeritus professor of economics at the University of California, Los Angeles] pointed out that every time you do something fast, it raises the costs. To avoid imposing these costs on taxpayers, they imposed a draft where they put young men in the army but paid them poorly. During the wars, the federal government and the military took over the economy, chose how to allocate all of the key war materials, and established wage and price controls. Meanwhile, they rationed all sorts of goods to the general public.

The government was very active in each crisis. Then after the crisis was over, the federal influence dropped back down. When people first started dealing with the crisis in World War I, they thought, "We don't know if we can do this." But over the course of a two-to-three-year period, they developed all sorts of techniques for solving the problems that came up. They were learning by doing. As a result, they concluded that trying to run a command economy was not quite as bad as they thought it would be—even though they still were not very good at running it.

**Between 1933 and 1935, the federal government spent a tremendous amount of money providing direct relief to people who were not readily able to work.**

So when the next crisis hit, they brought back a lot of the same programs, and the government ratcheted up again, often to new heights. In fact, there really was not much time for the government to ratchet down between the Great Depression and World War II. During World War II the federal government's control of the economy really escalated. Basically, the military was running half the economy. They eliminated unemployment by drafting roughly 10 percent of the work force. There were wage and price controls and rationing—meat once a week and limited access to sugar. Forty-five percent of income was being spent on munitions and hardware that was eventually going to be blown up.

After the war, the federal government dropped back down but not to anywhere near what had been before.

**Sniderman: So it's a ratchet effect.**

**Fishback:** Yes, like those ratchet wrenches. It never came back down to the old level. You can see this dynamic later on. The crises have been smaller, but we had the Great Society in the 1960s, and you can actually see it today. With the problems we saw in 2007 and 2008, those problems led to a huge increase in activity with the stimulus packages.



**Sniderman: Let's go back to the 1930s a bit. The federal government isn't all that practiced in interventions to deal with the Great Depression. Is it fair to characterize all of the various programs and efforts to deal with it as experimentation of one sort or another?**

**Fishback:** To some extent it is. What happened is the federal government built upon what the states had been doing. For example, the welfare system went through one of its major long-term changes during the 1930s. The first response was a short-run response. We need to get people back to work! Between 1933 and 1935, the federal government spent a tremendous amount of money providing direct relief to people who were not readily able to work. They then provided relief with a work requirement for people who were able.

In 1935, Harry Hopkins, who had been running the Federal Emergency Relief Administration (FERA), was not satisfied with how that administration had been running. The FERA was giving money to the states, which then largely determined how it would be spent. The administration had very little control because the only

way they could change state internal distributions they didn't like was to threaten to take all of the money away. Hopkins actually made that threat to some states, but having to use such a big threat was not very effective.

In 1935, the federal government rearranged the relief programs. They passed responsibility for direct relief back to the states for people who could not be employed very easily. The FERA was replaced with the Works Progress Administration (WPA). When Hopkins ran the WPA, the federal government had much more control over each project. The states just told them who was eligible to obtain work on the projects.

There was another side to relief. The Social Security Act was passed in 1935. It included the old-age pensions we all know as Social Security, and that program was, and still is, run at the national level. The Act also added three public-assistance programs, in which the federal government provides matching grants to the states.

Another big change with the Social Security Act was the introduction of unemployment insurance. Wisconsin had actually started a program before 1935 but had not paid benefits yet. The federal government provided about 3 percent of the cost for administration and each state set its own benefits. The unemployment insurance funds were run like an insurance fund where all the employers paid into it. When someone became unemployed, he was paid out of the fund collected from employers.

## Price V. Fishback

### Position

Thomas R. Brown Professor of Economics, University of Arizona

### Education

Butler University, BA with honors, 1977  
University of Washington, PhD, 1983

### Research and Teaching Interests

Economic History, Labor Economics, Political Economy,  
Law and Economics

### Selected Publications

*Government and the American Economy: A New History*, editor and co-author, 2007, University of Chicago Press.

*Prelude to the Welfare State: The Origins of Workers' Compensation*, with Shawn E. Kantor, 2000, University of Chicago Press.

"The Influence of the Home Owners' Loan Corporation on Housing Markets During the 1930s," with Shawn Kantor, Alfonso Flores-Lagunes, William Horrace, and Jaret Treber, 2010, *Review of Financial Studies*.

"The Dynamics of Relief Spending and the Private Urban Labor Market During the New Deal," with Todd Neumann and Shawn Kantor, 2010, *Journal of Economic History*.

"Births, Deaths, and New Deal Relief During the Great Depression," with Michael Haines and Shawn Kantor, 2007, *Review of Economics and Statistics*.



**In most periods of American history, people have pretty optimistic views because things have been going well for quite some time.**

The 1920s were very prosperous. Radio arrives, people are buying automobiles and new appliances. There are flappers out there doing the Charleston dance, great new jazz music is flowing out of the speakeasies. Babe Ruth is hitting home runs, and Jack Dempsey is punching people out. It's a fast-paced era. Even when things started going down halfway through 1929, people think it's just going to be a short recession, not a big deal.

**Sniderman: What do you think are some major misperceptions about the New Deal period?**

**Fishback:** For the last 10 years I've been working with a number of co-authors on the microeconomics of the New Deal. Almost all the work had been on the macroeconomic side, the money supply and government spending. During the 1930s, the federal government did not really run big deficits. It's not a Keynesian period at all. They increased government spending—Hoover raised it quite a bit, by 58 percent in nominal terms over a three-year period. Given the deflation, it rose 88 percent in real terms, which was a faster pace than anything Roosevelt did—but both groups believed in balanced budgets. So they raised tax rates and tax revenues just as fast.

**Sniderman: What was the public reaction to all these new programs?**

**Fishback:** There were thousands of letters written to President Roosevelt, which you can find in the national archives. Many of the letters describe how grateful people were that Roosevelt had actually found a way to provide them with some help. There were also letters to specific agencies complaining about the way people were treated on some programs: some complaints of corruption and politicking. Investigations of these typically found that about one-fourth of the complaints were valid.

**Sniderman: Today, of course, the sluggish housing market seems to be continuing to hold back the recovery. What was going on during the 1930s on that front?**

**Fishback:** The situation today has some great similarities with the 1920s and 1930s. There was a huge housing boom in the 1920s. Housing prices peaked in the late 1920s, and then they dropped like a stone between 1929 and 1933. In surveys of cities, the typical drop in housing prices was about 30 percent from 1930 to 1933. The overall drop from 1930 to 1940 averaged about 45 percent.

As a matter of fact, around 1933 or 1934, there were a huge number of people who were two-and-a-half years behind on their mortgage. More than half the states had passed mortgage moratoriums, which allowed people to stay in their house without paying the mortgage payments. Most of the people also owed a large amount in property taxes.

That is when the federal government came up with an idea of the Home Owners' Loan Corporation [HOLC]. There were all these lenders with toxic assets on their books, all these mortgages that could not be repaid. So the HOLC bought all these mortgages for pretty close to the full value of the loan, including the unpaid interest. In the modern jargon, the lenders did not take a "haircut." Basically, the HOLC gave the lenders a good deal

by replacing their toxic assets with good assets. They also gave the homeowner a good deal as well.

**Sniderman: How does that compare with today's Home Affordable Modification Program, or HAMP?**

**Fishback:** The problem with the situation today is they've been trying to refinance the loans with the lender keeping the loan. Often the HAMP program has involved the lender taking a pretty substantial haircut. It is a voluntary program, so you have to attract the lenders, but not many of the lenders thought that the program was a good deal for them. As a result, the HAMP was projected to refinance about 3 to 4 million loans. But a year after the program started, they were well short of a million.

**Sniderman: Could you talk a little about the Progressive Era and compare it to the period leading up to the 2007 recession?**

**Fishback:** Sure. I'm involved in writing a book with University of Arizona PhD student Carl Kitchens about booms and busts in American history. And really the story of American history is far more boom than bust. Seventy percent of the time the U.S. economy has been in booms. Then the other times we have had these short recessions. Then there is the occasional big bust, like during the 1890s and the Great Depression. As I said before, per capita income has risen 1.6 percent per year on average over the long haul, even while including bad times like the Great Depression.

As a result, in most periods of American history, people have pretty optimistic views because things have been going well for quite some time. The Progressive Era runs from 1890 to the 1920s. During most of this period GDP was growing. The typical worker was doing better. The typical wage in real terms rose 50 percent in the time period, maybe a little bit more. You saw huge surges in immigration into the United States, just gigantic surges of immigration. U.S. annual earnings in manufacturing and mining were often two to three times as high as the wages the immigrants had made in their home countries.

There were enormous variations in how much the federal government spent in state and local areas. We've been collecting information at the individual level, at the county level, and at the city level, and using that variation in how much they spent over time and across place to try to see the local effect of these programs. It's not the same thing as the macro effect; it's the local effect.

## The speed with which Bernanke and [then-Treasury Secretary Hank] Paulson responded during this period was drastically different than the Fed's response during the Depression.

The most successful programs as far as we could tell were the relief programs and the public works programs. The relief programs included the Federal Emergency Relief Administration and the Works Progress Administration (WPA). They also had a series of programs like the Public Roads Administration and the Public Works Administration that built public works. The public works programs were more generous than the relief programs because they actually hired people at full wages. These programs combined seemed to do some really positive things. They put people back to work.

**Sniderman:** *In the 1930s, it seemed like the Federal Reserve was a teenager relative to the current era. What do you think of that characterization?*

**Fishback:** The Fed was formed in 1913. The founding legislation stated that the Fed was supposed to provide an "elastic currency." Many people thought what this meant was the Fed was supposed to provide liquidity to stop banking panics. But it wasn't necessarily clear how they were supposed to do that. When you get to the late 1920s, the Federal Reserve has a notion of what's known as the "real bills doctrine." The focus was to provide more credit at a time when businesses were seeking more credit while they were expanding.

But that left the Fed as a passive responder to what was going on with the economy. So, many leaders in the Federal Reserve were following this passive model of the real bills doctrine. They were saying that unless they see demand for liquidity that's going along with businesses, then they won't do that much in terms of buying bonds and trying to expand the money supply and stimulate the economy.

By 1931 the economy was in serious trouble. There were three waves of bank failures between 1930 and 1932. The Fed policymakers were thinking that they were providing good liquidity to the system. They had cut the discount rate, at which the Fed lent to banks, to as low as 1 percent. That's really low, historically. Therefore, they concluded that they had done what they needed to do. But they were not taking into account the enormous deflation of the time period.

Carnegie Mellon University Professor Allan Meltzer, who has written a multi-volume history of the Federal Reserve, could not find any evidence that they were looking at "real" interest rates in the way we think of them today. The discount rate might have been 1 or 2 percent, but the deflation rate in the early 1930s was about 8 to 12 percent. So if I'm a borrower and I see a 1 percent interest rate and a 12 percent deflation rate, that means when I pay back the money, I'm paying back much more valuable money. In purchasing power my interest rate would have been 13 percent instead of the 1 percent nominal rate. That 13 percent rate was twice as high as any real interest rate we've seen since the 1930s.

The first time the Fed made a big purchase of bonds through open market operations was in the spring of 1932, when they bought about \$1 billion over several months. That's like \$1 trillion today. But the problem was that they had already been through a series of bank failures before. In their book,

*A Monetary History of the United States*, Milton Friedman and Anna Schwartz described it as acting "too little, too late." The Fed's leaders were in this position where they thought they were doing the right thing, but the economy was falling apart and the money supply was falling and banks were failing.

One of the key problems the Federal Reserve leaders faced was that they were trying to meet two sets of goals that often did not align well. The policymakers wanted to focus on the U.S. economic problems, but they also wanted to help the world maintain the gold standard. For example, in September and October of 1932, the Fed had to worry about a series of bank failures at the same time that Great Britain left the gold standard and all this gold was flowing out of the United States. The Fed leaders were then between a rock and a hard place. They could either buy a bunch of bonds to help out the banks in the United States, or sell a bunch of bonds and prevent the gold from going overseas. They decided to focus on the international side and prevent the gold from going overseas, but this did not help the U.S. banks at all.

Essentially, the Fed from 1930 to 1933 was like a teenager born in 1913. The policymakers were learning on the job. They were still trying to figure out what to do, then the Depression hit. Few of the policymakers had seen anything like this set of problems.

But the Fed finally did change its policy. Barry Eichengreen of Cal Berkeley and Peter Temin of MIT have both written about the change in policy. When Roosevelt stepped into office, the U.S. went off the gold standard. The Roosevelt Administration started announcing that its goal was to raise prices, and the Fed started to follow a more expansionary monetary policy. These policies helped shift people's expectations toward inflation rather than the extreme deflation that they had been experiencing. That helped turn the tide.



**Sniderman:** You referred to Milton Friedman's research on the Fed's failure to shift policy in the Great Depression. On Milton Friedman's 90th birthday, in 2005, Federal Reserve Chairman Ben Bernanke in so many words said to Milton, sorry about the Great Depression, but we won't do it again.

**Fishback:** And thank goodness. Because when the Fed finally made that big open market purchase in the 1930s, annual real income had dropped by 20 percent, there was a nasty deflation, and the unemployment rate was over 20 percent. That's when they finally made that move.

Think about the difference: There we were in the Depression, and the Federal Reserve waited three years to make a bold move. Not until the unemployment rate was 20 percent and annual output had dropped by 20 percent did they really make a big move to purchase bonds. In the recent crisis, the unemployment rate at the time Bernanke and the Fed started the expansion in liquidity hadn't even gotten past 7 percent yet. And real output had only been dropping for about three quarters. That's a huge difference in responses.

It's clear that Bernanke thought that's what needed to be done. And actually I believe he was right. In the end, it didn't cost us that much because we were backstopping situations and did not have to pay out that much, although we still don't know the story about Fannie Mae and Freddie Mac. The speed with which Bernanke and [then-Treasury Secretary Hank] Paulson responded during this period was drastically different than the Fed's response during the Depression.

**Sniderman:** Perhaps it's not surprising during periods such as we have now when times are tougher, and when we see a number of other countries around the world emerging and growing at very fast rates, that a number of people have said that it's time for the U.S. economy to realize that it's not going to be as pre-eminent. What would you say to people who think we should be scaling back our aspirations?

**Fishback:** I think we should not be disheartened. As a matter of fact, I'm pretty optimistic. I would bet that over the next 50 years, per capita income is going to continue to grow about 1.6 percent per year; that's just my expectation.

Here's why I say that: It's really easy to look around at what you're seeing and the problems—and we've had plenty of problems in the last three years, they just seem to keep coming—and be discouraged. Almost anyone you can talk to has a litany of things they can point to as being a terrible problem that is going to prevent the economy from growing. But we've seen that over, and over, and over again in the last 200 years. The Club of Rome [a global think tank] was talking about how the world was going to fall apart and run out of all sorts of commodities in the 1960s, and then we had a big boom in commodities. The reason I think this is going on is that we don't know what's going to come next, because there are all sorts of entrepreneurs out there who are coming up with new ideas that you and I and most people don't know about. It's hard to tell which ones will be the winners, but there will be winners.

Look at the growth in incomes in many developing countries. I am betting that there will be a huge increase in technology change in developing countries. As more people have higher incomes and better educations in those countries, they will be willing to buy from us. Not only that, they will be developing new products and services that we will benefit from. I am very optimistic even though I study the

Great Depression. Well actually, it's probably because I study the Great Depression, because it was so bad that everything else looks good.

**Sniderman:** It's clear from the conversation that you're quite passionate about economic history.

**Fishback:** To say the least!

**Sniderman:** Who were some of your mentors in that realm?

**Fishback:** I was really lucky that I got to go to graduate school at the University of Washington, where they had five economic historians, which is pretty unusual. Bob Higgs, Douglass North, and Morris D. Morris all shaped the way I think about economic history in very diverse ways. They created a wonderful and challenging environment. Bob was my thesis advisor and a group of us wrote the book *Government and the American Economy: A New History* in his honor.

Milton Friedman certainly had a big impact on me. He was just a great economist in all sorts of dimensions. Certainly a number of colleagues in economic history—Claudia Goldin at Harvard, she's just an amazing labor historian. John Wallis at Maryland was in graduate school with me, and he has done great work on the New Deal, federalism, and studies of long-term changes in the role of government.

The great thing is, when you're doing research and teaching and reading the work of my colleagues in the profession, there are hundreds of economists and economic historians that have had influence on what I think. I'm the co-editor of the *Journal of Economic History* right now, and every time I get a new paper, I get to learn something new and it adds to my understanding of what's going on. ■



Watch video clips and read the full interview  
[www.clevelandfed.org/forefront](http://www.clevelandfed.org/forefront)



#### Recommended reading

Robert Higgs. 1987.  
*Crisis and Leviathan: Critical Episodes in the Growth of American Government.*  
New York: Oxford University Press.