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From Booms to Bankruptcy

SIXTH OF A SERIES

Sam Levin

THE YEAR is 1929. Unemployment? Nonsense! Only the shiftless are out of jobs. Poverty? Ridiculous! We're the richest country in the world. Look at the crowded theaters, the jammed beauty shops, the busy department stores. Didn't we turn out five million motor cars last year? Didn't we construct six billion dollars' worth of buildings and manufacture five billions' worth of clothing and shoes?

Suddenly a great shudder . . . then . . . an economic hurricane! Within a few days after October 29, 1929, a staggering deflation wiped out the equities of tens of thousands of investors. Banks and factories by the thousands closed their doors. Job queues lengthened. Purchasing power of millions of consumers melted away. From isolated murmurs, the complaints of employment seekers swelled into a mighty roar of frustration.

Dumb-founded, sober Americans asked: Why? What had caused this vast and deadly stoppage of production? Is there any rational explanation for the so-called "business cycle?" Is there any cure?

A flood of explanations hit the newsstands and bookstores. Desperation gave credence to anything propounded, from the sun-spot theory—revived by Prof. Henry L. Moore of Columbia—that depressions are caused by increased solor activity—to the "income theory" advanced by Prof. William Foster of Harvard.[1] This economist noted that businessmen generally save a part of each year's net income for expansion, dividends and emergencies, thus leaving insufficient in wages for employees to buy back the equivalent of their production. As a result, he asserted, there gradually accumulates supplies of goods in excess of the purchasing power of the public. This excess production eventually gluts the market and has to be sold at bankrupt prices. [The only thing he failed to explain is why production does not resume long after the public has eaten up, used up and worn out all the things they brought home from the big bargain sale.]

The classic "over-production" and "over-consumption" theories are widely accepted even today. The "over-production" theory runs somewhat as follows:

A watch manufacturer produces so many watches this year and sells them all at a profit. Next year he produces twice as many. While his rate of profit might drop somewhat, his total profit still rises, and the following year he produces four times as many. Since some of his competitors do likewise, the output of watches rises to the point

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where the public no longer needs or wants watches. Whereupon all watch manufacturers have to shut down for awhile.

WHILE IT IS true that failure to judge the market correctly may sometimes cause this type of "relative over-production," and that consequently temporary unemployment does occur until workers make an adjustment, this situation cannot account for widespread involuntary unemployment.

This country has never suffered from "general over-production." On the contrary, there are millions who lack even the bare necessities, let alone the luxuries, to which human willingness to labor should entitle them. In our Southern states where anemia, pellagra and other deficiency diseases are prevalent, there are those who go through life without oranges, beef or wheat, while these foods are supposedly over-produced. In Georgia alone, in 1933, fifty per cent of the deaths were due to entirely preventable diseases, caused by lack of proper diet and clothing.[2]

"Over-consumption" theorists hold that depressions result from the extravagance of the public. The average person, they maintain, is at heart simply an installment-purchaser and a spendthrift. Unless checked by some such disaster as a depression, he is apt to buy himself poor. And once his cash and credit are gone, unsold goods accumulate in warehouses.

Tell this to the average factory hand, and his retort would be a positive "Oh, yeah? Give me back my job and my credit, and let me at those warehouses." Tell him that depressions occur because he and his fellow-workmen "over-consume" wealth, and he probably will say, "What do you mean? My wife and I are good budgeters. We bought a radio in 1928 and paid for it on time. We had it all figured to pay for a car in '29 and we could have, too, if I hadn't lost my job."

Since these various theories patently cannot stand analysis, a realistic search which traces the business cycle through its progressive stages must be turned to as the means of disclosing the point at which weakness in our economy sets in.

Step One. Through labor, men obtain raw materials from the rich storehouse of the earth. Workers in the extractive industries — agriculture, mining, fishing, lumbering and grazing—draw materials directly from the ground. Other men then process these materials into completed articles: transforming hides into shoes, trees into boards, cotton and wool into garments, iron ore, rubber and coal into thousands of industrial and household products. Next trade and transportation take over. Shipping, railroading, financing, insurance, advertising and kindred businesses facilitate the flow of commodities to the ultimate consumer. Finally, other men offer their services in exchange for a portion of the goods produced. They are the teachers and preachers, actors and barbers, doctors and explorers—

all the professional and service-performing men and women of society.

Step Two. This economic pattern, utilizing the diverse abilities of men, repeats itself by spontaneous cooperation. Material comfort mounts steadily with man's constantly rising productive powers. Labor and capital find ready employment. New inventions and improved methods call more and more land into use. City sites are at a premium as people gravitate toward the centers of culture and exchange. A few lucky owners of choice lots cash in; and thousands of others are persuaded that they, too, can get rich quick. As an unshakable faith in continued expansion leads to an era of land speculation, vacant land is held out of use as though for ransom, and land in use is driven up in price until the cost of doing business rises substantially. This in turn results in further increases in commodity prices.

Step Three. All the symptoms of a boom period are now in evidence. "Real estate" changes hands almost daily, at higher and higher figures, as land speculation reaches a frenzy. With the rise of the stock market, steady plodders turn gamblers. The uninitiated purchase indiscriminately, never looking behind the scenes to ask whether their holdings are based on inflated land values, or whether the fantastic interest rates are an indication that the company offering them—pinched by the ever-increasing outlay of its cash assets to pay for raw materials and operating location—desperately needs to borrow money.

Step Four. When speculative land value rises to the point where labor cannot pay the prices demanded and continue to live at the old standard, and capital cannot engage itself profitably, production is paralyzed. Manufactured goods, with high fixed costs, are most vulnerable, and curtailment of production is deepest in this field. No field, however, remains unaffected, and a depression sets in.

Step Five. The long period of inactivity has exactly the same effect upon land values as would a deliberately designed long-time sit-down strike arranged between capital and labor. Land recently in demand tumbles in price, and its holders have no choice but to sell at deflated values. And as this trend becomes general, production is at last resumed.

The following history of Chicago's land values demonstrates this sequence.[3] Chicago covers 211 square miles.

1830—The price of any land in that area was $1.25 an acre; land value of the entire region now covered by Chicago, $168,800.

1832—Those who knew the history of the Erie canal, and its effect of increasing land values, bought land along the proposed course of a Chicago canal and then induced the Federal Government to construct the canal. This land was then advertised for sale, and a land boom started.

1836—Land values reached $10,-500,000.

First Major Depression

1842—Land values had shrunk to $1,400,000, or slightly less than one-seventh of their inflated value. Business again began to improve.

1848—The Chicago canal opened.

1854—Chicago had become the railroad center of the West. Plank roads, street lighting and sewers were installed. Land values rose again.

1856—Land values had increased to $126,000,000.

Second Major Depression

1858—There had been many bank failures and 15 railroad failures. There was great unemployment everywhere, and consequently land values shrunk enormously.

1860-65—Civil War. By 1864, 96 bank failures had occurred in Illinois. But the European need for wheat, and our own war demands sent hog and grain prices up, and land costs began to increase sharply.

1871—Chicago fire and a post-war boom. Parks and boulevards were built by the city; $76,-000,000 worth of building construction carried on over a seven-year period.

1873—Land values had increased to $575,000,000.

Third Major Depression

1876—21 bank failures in four years. Land values dropped to $250,000,000; rents were 30% lower than at the peak.

1884-90—Building of sky-scrapers began; many new manufacturing enterprises and 7 new railroad lines were built. The World's Fair was projected and there was wild land speculation.

1892—Land values estimated at $1,-000,000,000.

Fourth Major Depression

1909—Land values, after many industrial failures and great unemployment, shrank to a point only half as high as in 1890, although the population of Chicago was twice as great. Business began to improve and unemployment to decrease.

1917—World War I, followed by post-war boom. Business was stimulated by apartment building and enormous American and European expenditures for food and war materials.

1921—Land values $200,000,000 and still rising.

1928—Land values reached $5,000,-000,000, with records of increases as high as 1,000% between 1915 and 1928.

Fifth Major Depression

Even with our modern industrial methods, labor could not pay this price for land and continue to live at its accustomed standard.

1932—Foreclosure suits in Chicago involved more than $2,000,000,000 of land value; apartment rents were approximately half of those prevailing in 1922. There were 30 bank failures, also great unemployment and all the other symptoms of a great depression.

Looking at this record, it is not surprising that during 1934-35, when the outlook for capital and labor was still dark, the Chicago Title and Trust Company could strike the following note of optimism in its advertising:

> Every major financial crisis—1837, 1857, 1873, 1893, and 1929—caused land values to depreciate. But panic, war, and fire have never destroyed these values nor permanently depressed them. Within four to six years, land values always have turned upward again . . . and thereafter have never again gone so low as in any previous depression.

This story of Chicago is but one example of what has happened in large cities all over the United States in the course of the past one hundred years. A similar picture could be drawn of New York, San Francisco, New Orleans, Detroit or any other growing city. In each case, a period of feverish land speculation, initiated by enhanced business activity, has been followed immediately by a crash. In 1837 it was canal building; in 1857, 1873 and 1893 it was railroad expansion; and in 1929 it was extensive automobile and road building.[4] The particular relationship between extended transportation and speculation in the lands it brings into use is marked.[5] In our time we have seen how the advent of the automobile has resulted in the subdivision of farm lands adjoining our cities. Lots unserviced by public transportation rose to a value comparable to that of city lots, on the strength of the fact that they could be reached in one's own car.

THE YEAR is 1944. At which point in the so-called business cycle do we stand today?

As late as 1939 the wages of capital (i. e. interest) were the lowest in history. *Business Week* for April 11 of that year stated:

> Perhaps the nearest thing to true interest is the rate on Treasury bills. . . . Frequently there are instances where loans yield nothing.

It is doubtful whether, during the period from 1929 to the outbreak of the present war, enough deflation of land values had occurred to make for genuine recovery. Government loans, F. H. A. and loans to farmers had the effect of bolstering up farm and home mortgages based on inflated values. As long as these contracts stand, payment continues to be made on a pre-depression value, with the result that an undue proportion of total wealth produced goes to pay merely for the use of land.

The Farm Tenancy Report of the President's Committee, National Resources Committee, February, 1937, says:

> The equity of operating farmers in their land is little more than one-fifth. Nearly four-fifths is in the hands of landlords and mortgage owners.

Today history is repeating itself as the demands of war create a parallel to the trend of 1915-20. The Department of Agriculture's national index of the average per-acre value of farm land and improvements, on July 1, 1943, showed it to be 23% above what it was in 1935-39. The average rate of the rise, throughout the entire country, has been about 1% a month during 1943, the highest rate of increase on record except in 1919-20, at the crest of the boom.[6]

AS WE FACE the future, it should be with the realization that depressions, cataclysmic though they be, are only an intensification of evils which we accept year in and year out as natural. Seen in their real economic perspective, they may be compared to acute stages of a chronic disease. Even during normal times, the rent of land rises with and absorbs the benefits of every advance gained in man's struggle toward a world of equity and material well-being.[7] The steepening price demanded for the chance to labor relegates a growing proportion of our population to poverty, and at all times the margin of safety it leaves for doing business is so small that the average life of business enterprise is only 66 months.[8] Poverty and depression are merged as one phenomenon.

The times through which we are living impel thinking men and women to take cognizance of the gravity of our social and economic problems. Some of us have our own pet remedies and solutions. But knowledge of the causes of poverty and depressions, as now revealed, enables us better to test the effectiveness of any proposed remedy. In considering a solution of these problems, we must keep in mind that only as it strikes at the source of the trouble, can it hope to cure; only as it secures to all a stake in the country they help to build can it permanently succeed.

The next article in this series on Fundamental Economics will illustrate the righteousness of property ownership, and raise the question as to how labor can secure its full reward.

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