

Recession and the great depression: a historical perspective



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The current recession in global economy is the most dramatic episode in the recent economic history of the world. With its all encompassing character it has affected all the major economies, whether industrialized, emerging or developing. The American, European and Japanese economies are in recession all at the same time. For long the Japanese economy, the worlds second largest was in recession, but the impact was cushioned by good American growth rates and modest European ones. Such cushioning is not available now within the Industrialized North.

second, unlike in the past when solutions to such crisis were found within the tight circle of the industrialized economies, represented by G-7 or G-8, this time, the emerging economies, especially China and India who are predicted to grow at 6 to 7 percent still, are expected to help mitigate the severity of the down turn even though their share of the global economy is still much inferior to the combined share of the U.S.A. Europe and Japan. As against this, China holds almost two trillion dollars of foreign exchange reserves, a large part of which is invested in U.S. securities. Its role therefore, in injecting critically needed liquidity into the global system, besides providing a safety net to the U.S. economy is most important.

A broader G-20 summit (including India and China) scheduled to be held in London on April 2 is 2011 is expected to seriously address the issue of reforming the global financial architecture.

The depth of the crisis has not been fully plumbed yet. Neither the previous U.S. administrations 800 billion bailout package nor Obama's 780 billion stimulus package has worked, with Citi Bank of America and AIG continuing to post huge losses. The U.S. Govt. is faced with the highly unpalatable decision of nationalizing them. Britain's Gordon Brown quickly nationalized collapsing banks.

The French Govt. has announced a rescue package for its car manufactures to prevent job loses and ensure that future capacity expansion is in France itself and not else where within the European Union, raising concerns about protectionist policies as Govt. face hard choices pitting commitments to open markets against protecting national economies. The aim of bail outs and stimulus package is to shore up those sectors of the economy most affected, restore consumer confidence, provide liquidity, encourage the banks to lend, protect employment and so on.

However because of the overall uncertainties ahead, public confidence is low and the market sentiment remains fragile.

The source of the crisis is the country that has been the biggest protagonist internationally of good governance, transparency and sound financial management, besides being the strongest votary of free markets and entrepreneurial initiative. In a sense U.S. hegemony since the nineties allowed its financial sector to do the kind of freewheeling, it has done in pursuit of egregious profits and bonuses for financial managers and corporate heads. Globalization and the toxic effects of the pervasive culture of greed spread the contagion to Europe too.

It is not only that sentiments against globalization itself are now hardening as affected countries try to protect local manufacturing and jobs from foreign competition it is the risk taking, market oriented, minimally regulated model of the Anglo-Saxon type of capitalism that is being questioned.

That market mechanisms, regulatory bodies, rating agencies auditors should have failed, has dissipated the aura of the market economy. The public mandate for governmental intervention derived earlier as counter productive has grown.

Barrack Obama's step to cap the annual remuneration of the CEO's of the bailed out corporations to only half a million dollars testifies to public revulsion at the manner in which the corporate sector has handled its system of incentives, unmindful of social consequences.

The global economic crisis is rearranging the international diplomatic chequerboard. For Obama of foremost concern is the domestic agenda relating to energy, health-care and education as well as the economic crisis gripping the country, his February 25th, 2009 speech to the Congress was overwhelmingly devoted to these themes, with only passing references to foreign policy including terrorism. Unilateralism is no longer a feasible policy.

Now if we revert to the Great Depression of the early 20th century, to be precise the depression of (1929-1933), it was attended by momentous consequences in the economic as well as in the political sphere. It induced Great Britain to disassociate her national currency from gold – her example in this being followed by the whole world and to reverse her traditional fiscal policy by abandoning free trade. It induced the U.S. where the dying system of Laissez-faire had found its last asylum, to throw her cherished dogmas to wind subject economic enterprise to an unwanted degree of official direction. It induced the German people to substitute an authoritarian Govt. for the political regime established by the Weimar constitution.

There had been speculations as to the causes of the 'Economic Blizzard'. In a general sense it takes its place in the sequences of booms and depressions which follow each other in our productive processes with unfailing regularity.

Leaving aside the enigma of the trade cycle we may observe some contributory factors which throw light on the reasons for the severity of the blizzard. The war of 1914-18 left behind it an economic legacy which imposed a heavy mortgage upon the resources of all the belligerents. For the unparalleled destruction of wealth there was nothing to show beyond national debts of unprecedented magnitude. Moreover, the normal equilibrium had been disturbed by the substitution of a war economy for peace economy.

The root of that recession lie deep embedded in the global capitalist economy.

From the beginning of the 20th century U.S occupied the pivotal position in the global economy that Britain had held over a century. As early as 1902 European were talking about an American invasions as U.S corporations- having achieved monopolies at home- cast their eyes hungrily overseas for new markets and as U.S financiers looked for sites to invest surplus capital. By 1914 the U.S direct investment abroad amounted to about 7 percent of U.S GNP, the U.S generated 42 percent of the world's industrial output, with Germany Britain and France amounting to only 28%. The passing of global capitalist hegemony from the U.K. to the U.S was also accompanied by an intensification of economic interconnectedness. International order was integrated to an unprecedented degree: the economically civilized world tied together by credit and commercial contact. The Wall Street stock market crash of 29 October 1929 revealed not only the fragility of post war economic regeneration but also in the devastating impact of the depression on much of the world. Its impact was beyond doubt global. The results of the great depression in America and Europe are familiar to European readers.

The drying up of U.S. loans and the sudden shrinkage of trans Atlantic

trade generated spiraling inflation and a decline in manufacturing industries as consumers had ever less disposable income to spend, and as foreign markets disappeared. This in turn occasioned massive unemployment. In the era before social welfare provision was widely established as a social compact between state and citizens, unemployment, utter destitution and grinding poverty for millions. Even for those remained employed, hyper-inflation- and some countries complete collapse of currencies- led to the over night elimination of savings, and to paper money becoming virtually worthless as in Weimar Germany.

Perhaps less well known in Europe or America are results of the depression elsewhere in the world. Every country that participated in international trade was affected- whether they were independent states (as in South America) or colonial territories under the rule of western European powers. Precipitous drop in the western world's demand for luxury goods, food stuffs and raw materials did not just mean unemployment for workers in factories in the industrialized states of Europe and North America. It also spelled ruin for the producers of primary materials from which consumer goods were manufactured. For instance Japanese silk farmers suddenly found their livelihood ruined as Americans ceased to buy silk stockings in the depression of the early 1930's. Brazil's coffee growers attempted to prevent the coffee price from collapsing by selling it to Brazilian railway companies as an alternative fuel to coal.

In economic terms the result of the depression was that the globalization of the world economy stuttered, as states attempted to reverse the process. Rather than a global free trade system continuing to develop, the major capitalist states now sought to isolate their national economies as far as possible from the vagaries of the international market and cross-border capital flows. Free-trade was abandoned in favour of protectionist policies and high tariff barriers, as states attempted to make their economies as self-sufficient as possible. As a result the volume of international trade got America lead the way in protectionism being in the fortunate position of needing other countries products less than did Britain and many other industrialized states.

Since the industrial revolution a global capitalist economy had been developing, drawing all parts of the world into transnational flows of finance and trade.

The 1st World War disrupted this development with a profound negative impact on the international economic system, which was initially marked by the vibrancy of the U.S economy in the 1920's.

In 1929, the Wall Street stock market crash induced the great inter war depression, illustrating the degrees to which national economies were enmeshed in a global system.

Depression in many countries around the world resulted in extremist political movement gaining strength and more generally in an upsurge of introverted nationalism and the pursuit economic autarky. Affinities these between there two depressions are apparently visible if we delve into its background, happenings and consequences.

“Globalization is not the panacea of all the economic problems” gets the affirmation once more by the fiscal policies adopted by the great powers of the world.

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