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The American Economy: A Historical Encyclopedia

Volume One: Short Entries

edited by

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A new Republican Party, founded in 1854, competed strongly with the Democrats from the beginning and achieved hegemony in the late nineteenth century that endured until 1930, when Democrats assumed control of the U.S. House of Representatives. The competitiveness of the Democratic Party was dampened because of an economic downturn during the second administration of President Grover Cleveland and the populist campaign of 1896 Democratic presidential nominee William Jennings Bryan, who supported helping alienated city dwellers—mostly underpaid workers and immigrants who operated outside the mainstream political system—in a rapidly urbanizing nation. Following the economic crash of 1929, which came during a period of unified Republican control of the national government, the Democratic Party gained favorable recognition. Although Americans continued to perceive the Republican Party as better able to conduct foreign policy during most of the twentieth century, the Democrats had the edge on handling the economy, and this doubtless contributed to the pattern in U.S. politics after the 1930 midterm elections. For the remainder of the century, the Republicans controlled both the presidency and both houses of Congress for a total of just four years—whereas the Democrats dominated Congress for 32 years running at the end of the twentieth century. Key to Democratic success was disproportionate support for its candidates by members of the working class, many of whom lived in large urban areas. In presidential elections where class polarization existed, such as in 1936, 1940, and 1976, Democratic candidates emerged victorious. In the presidential election of 1972, when the correlation of voter choice with class status approached zero, Republican Richard M. Nixon handily defeated Democratic U.S. Senator George McGovern. Interestingly, Nixon identified himself as a Keynesian, a theory of economics more closely identified with Democratic policies than with Republican ones. The Republican Party continues to define itself as a party that recognizes Keynesian economics but within a balanced budget.

—Henry B. Sirota

References
See also Volume 1: Great Depression; Republican Party.

Depressions, The
See Great Depression.

Depression of the 1890s
Severe economic downturn after cotton-growing regions of the South and agricultural areas of the Great Plains began experiencing significant decline in prices, increases in expenses, and a precipitous spike in farm foreclosures. The depression of the 1890s arrived at Wall Street on May 5, 1893, when stock prices declined in the face of uncertainty about the gold supply and the failure of the Philadelphia and Reading Railroad. This economic crisis reached its nadir in 1894 but endured until mid-1897. A depression in Europe, low agricultural prices, deflated monetary prices, watered railroad stocks, and a lack of government regulation precipitated this economic crisis. The Panic of 1893 began because of a financial crisis in the railroad industry, the most important component of the national economy, and quickly affected virtually every sector of American economic life. The unemployment rate reached 20 percent, 156 railroads and 400 banks failed, and 16,000 businesses went bankrupt.

This economic crisis revealed class differences when Jacob Coxey’s army of unemployed Americans marched toward Washington, D.C., in March and April 1893 in search of jobs and government relief. The desperation of union members became evident in Chicago during the Homestead (1892) and Pullman (1894) strikes.

—James T. Carroll

References
See also Volume 1: Pullman Strike; Railroads; Volume 2: Labor.

Depressions
Sustained periods of economic contraction, characterized by high and persistent levels of unemployment accompanied by falling prices, investment contraction, financial crises, reduced demand, and general decline in business activity.

Although some economists view depressions as random aberrations, most agree that they remain inherent to capitalist economies. Throughout the long-term evolution of capitalism, the type and nature of depressions has changed. The structural and institutional development of the economy has played an important role in the types of depressions that have emerged. The United States has experienced six major depressions in its economic history since the early 1800s—all similar in length and severity. Prior to that, economic declines had occurred largely because of wars, natural disasters, and other non-economic factors.

During the early nineteenth century, merchant capitalism, in which depressions remain largely commercial and speculative in character, ended. Small proprietorships made up the economy at this time. This raw-materials economy resulted in depressions accompanied by speculation and sharp declines in prices for agricultural and raw materials. With the advent of the Industrial Revolution in the late nineteenth century and diminished contribution of agriculture to economic growth, crisis became associated with the rise, expansion, and financing of industrial activity. The profit incentive became even more important in an era of increased demand
and mass production. Corporations replaced proprietorships, and new financial institutions emerged to facilitate factory production. The development of competitive markets frequently led companies into price wars, which undermined profitability and hence firms’ ability to meet financial obligations. This uncertainty led to the emergence of a different type of company— one with great market power and control characterized by cartels, trusts, and mergers. Investment banking evolved to service these organizations, acquiring a large stake in their control by securing a large number of firm shares and positions on governing boards. The depressions in the era of what may be called “banker capitalism” during the 1920s occurred as a result of the aggressive expansion of these firms and accompanying financial speculation. The authority of investment banking over the firms and lack of internal control are closely related to the massive financial speculation that brought about market instability and played a pivotal role in the deepest and most severe depression of our time, also referred to as the Great Depression, in the 1930s. In the post–World War II era, financial sector development and innovation, increasing globalization, and increasing financial instability have triggered several global financial crises or recessions, but no depressions.

Although economists disagree on the exact causes of each depression, the nature of depressions has changed with the evolution of capitalism. Whether linked to a collapse in agricultural prices or speculative financial attacks, all depressions include a sharp decline in demand. Each of the six major U.S. depressions has followed periods of sustained government surpluses and sharp debt reductions, thereby stifling aggregate demand. Price shocks, stock market crashes, and banking-sector crises act as catalysts that bring about the fast, sharp decline in economic activity that is typical of depressions.

Depressions are protracted and severe because it takes a while for business confidence to return. Sharp declines in demand or overinvestment (or both) lead to cutbacks in production, involuntary inventory accumulation, and massive layoffs. Declines in employment further depress aggregate demand, leading to a downward spiral in economic activity. Business confidence falls so that expected future returns do not warrant any new investment, even in the face of falling prices, wages, and interest rates. As markets fail to bring about a recovery, policy proposals have emerged for governments to implement countercyclical measures. The suggested remedial policy responses include “priming the pump,” large public infrastructure investment, public service employment programs like those of the New Deal era, and job guarantee schemes, such as making the government an employer of last resort or making public service employment available. The emergence of big government, in which the federal government assumes control over a major portion of the U.S. economy, has contributed to the lack of depressions since World War II.

—Pavla R. Tcherneva and Mathew Forstater

References


See also Volume I: Captains of Industry; Great Depression.

Deregulation
The loosening of government controls over vital industries such as the airline, utility, and communications industries.

The legal cartel theory (in which some companies control pricing and supply although competitors exist), increasing evidence of waste and inefficiency in regulated industries, and the contention that government was regulating potentially competitive industries all contributed to the deregulation movement of the 1970s and 1980s. Since 1980, important legislation has been passed that deregulates in varying degrees the airline, trucking, banking, railroad, and television broadcasting industries.

Deregulation has proven controversial, and the nature of the controversy remains quite predictable. Basing their arguments on the legal cartel theory, in which certain companies control a near monopoly but some competitors exist, proponents of deregulation contend that it will result in lower prices, more output, and the elimination of bureaucratic inefficiencies. Some critics of deregulation, embracing the public interest theory, argue that deregulation will result in the gradual monopolization of the industry by one or two firms, which in turn will lead to higher prices and diminished output or service. Other critics contend that deregulation may lead to excessive competition and industry instability, and that vital services (for example, transportation) may be withdrawn from smaller communities. Still other critics stress that as increased competition reduces each firm’s revenues, companies may lower their standards with respect to safety and risk as they try to reduce costs and remain profitable.

Perhaps the most publicized case of deregulation involves the airlines. The Airmail Act of 1925 provided for the encouragement of the air carrier industry; the Civil Aeronautics Act in 1938 established economic and other regulations upon which the industry matured and developed. Many factions and individual representatives of the industry, government, and the general public continued to express dissatisfaction after Congress passed the Civil Aeronautics Act in 1938 and again after the Federal Aviation Act became law in 1958. Dissent against and criticism of federal aviation regulation continued with increasing force until the 1970s. As early as 1975 a law was passed that was also known as the Federal Aviation Act. Congress did not pass the act, but opposition grew regarding the economic regulation of the aviation industry. In the early 1970s, many academic economists questioned the need for economic regulation of air carriers. As a result, President Gerald Ford began to press for deregulation. Then President Jimmy Carter appointed Alfred Khan as Chairman of the Civil Aeronautics Board, and he moved quickly toward deregulation in areas of pricing, entry, and exit.