

**THE POLITICAL ECONOMY OF THE NEW DEAL. BY JIM F. COUCH AND WILLIAM F. SHUGHART II. CHELTENHAM, U.K.: EDWARD ELGAR, 1998.**

**W**ith another U.S. presidential election nearly upon us, it is almost certain that Democratic party candidates (and some Republicans) will evoke the name of Franklin Delano Roosevelt, the president whose administration gave America the New Deal, which historians and all-too-many economists believe was an appropriate response to the Great Depression. Since Time Magazine named FDR as one of the greatest men of the century, we shall once again hear how Roosevelt and his “New Deal” lifted the country from the depths of the depression and once again gave us hope—and the kind of government that could respond to whatever crisis would ail our body politic.

The New Deal did no such thing, of course, but politicians and academic scribblers are fond of telling their audiences that Roosevelt’s creation of a gaggle of alphabet-soup programs was an “innovative” and “compassionate” response to the economic calamity caused by the “collapse of capitalism.” If winners truly write history, then the dearth of books by economists critical of the New Deal—despite the fact that the Great Depression has been studied more than any other economic event in U.S. history—clearly demonstrates where free markets rate with much of this country’s intelligentsia.

Economic literature that challenges the New Deal orthodoxy is fairly scant. Murray Rothbard’s *America’s Great Depression* (1963) successfully refutes the charge that the economic collapse was a failure of the free market. However, Rothbard stops his historical analysis at the end of Herbert Hoover’s term and does not deal directly with Roosevelt’s programs.

The *Political Economy of the New Deal* by Jim F. Couch and William F. Shughart II is an addition to the literature which dissents from the intellectual zeitgeist. The outgrowth of Couch’s doctoral dissertation at the University of Mississippi, the book takes a public-choice approach as it examines the policies of the Roosevelt Administration. The authors demonstrate how raw politics drove the New Deal programs, as opposed to the common conception that such programs were simply a response to the “genuine need” facing millions of unemployed or underemployed Americans. In fact, as the authors point out on numerous occasions, the states with the least economic distress often received the lion’s share of New Deal money, as opposed to those areas of the country hit hardest by unemployment and poverty.

Couch and Shughart's book brings together a number of public-choice studies by other authors which have appeared in various journals, but have never been formally connected to each other in a single book. The authors also perform their own statistical tests, using data discovered by Leonard Arrington in 1969 that lists detailed New Deal expenses across states. Because *The Political Economy of the New Deal* depends upon interpretation of numerous statistical tests, it is not exactly the book you might want to give to your favorite history professor who insists that Roosevelt saved the country.

Before examining the strengths of this book, we first criticize its most glaring weakness from the Austrian point of view: the inability to pinpoint causes of the economic downturn. In defense of the authors, this is not a book on business cycles, nor do they claim any special knowledge of what triggers boom and bust. However, they fail to even mention Rothbard's work, although they cite Vedder and Gallaway several times.

Couch and Shughart unwittingly come close to explaining the cause of the crash (p. 12) when they refer to the disastrous attempts by Britain's Chancellor of the Exchequer Winston Churchill to return the pound to its pre-World War I standard. As Rothbard pointed out in *America's Great Depression*, Churchill convinced the Federal Reserve to follow an easy money policy, which led to the stock-market bubble which ultimately collapsed in 1929. Instead of continuing with this theme, the authors enlist the explanations of John Kenneth Galbraith to dismiss it.

They then turn to the monetarist explanation, that the Federal Reserve failed to keep the banking system afloat by lending through its discount window. They are on more solid ground here, especially when they examine the issue from a public choice point-of-view. According to Friedman and Schwartz, the Fed's failure to bail out the troubled banks resulted from myopia on behalf of the central bankers, who were engaged in a power struggle in the vacuum left behind by the death of New York Fed Governor Benjamin Strong in 1928. Anderson, Shughart, and Tollison (1988) demonstrated that the Fed's policy was rational in that it ultimately strengthened the position of member banks, not to mention greater monetary powers given by Congress to the Federal Reserve itself.

Rothbard disputes the "dastardly Fed" argument in *America's Great Depression* by pointing out that the central bank did, indeed, try to pump up bank reserves from 1930 to 1932. The problem was not that the Fed was failing in its attempts to increase the money supply, as economically unsound as the policy may have been. Rather, the Fed's efforts were thwarted by banks who increased their excess reserves and currency holdings, and the public who did not respond to the lowering of interest rates by borrowing more money.

Rothbard's explanation for why this phenomenon occurred is simple. The malinvestments brought on by the Fed's earlier policies of monetary expansion could not be propped up by new injections of credit, no matter how attractive

interest rates may have been. In fact, Rothbard argues that the central bank, instead of trying to inflate the currency, should have been following a policy of deflation and the ending of the fractional-reserve banking system.

While Couch and Shugart seem to stumble over what caused the stock market crash, they do point out the damage done by interventionist policies of President Herbert Hoover, often referring to Vedder and Gallaway's *Out of Work* (1993). Vedder and Gallaway pointed out (as did Rothbard) that the Hoover administration engaged in open "jawboning" of business leaders to keep prices and wages at high levels, thus forcing up real wages in a time of declining productivity. They also note the damage done by passage of the Smoot–Hawley Tariff of 1930, which quickly accelerated the U.S. economy's downward spiral. The Higgs thesis that the anti-business pronouncements of the Roosevelt administration created great uncertainty in the private sector also receives strong mention. They write:

There are a number of reasons why American economic policy failed. One is the First New Deal's wrong-headed strategy of responding to the colossal decline in real output by implementing programs designed to reduce production even further. Another is a series of disastrous monetary policy initiatives, beginning with a sharp contraction in the money supply at the depression's outset and ending with a doubling of required reserve ratios at a time (1936–37) when recovery seemed to be underway. Yet another is the uncertainty created by the brain trust's anti-market rhetoric, especially so during the Second New Deal, which seemed to put private property-rights in jeopardy.

As Couch and Shugart move away from causes of the depression to the Roosevelt response, the book becomes stronger in its analysis. Their theme is two-fold. First, they accurately note that those who shaped the New Deal were strongly anticapitalist in their outlook. For example, they write that Rexford Guy Tugwell, called the "architect" of the First New Deal, was an institutionalist economist from Columbia University who believed that the price system was both inefficient and a major cause of "speculation" by greedy people. In other words, the ideology of the New Dealers did matter.

Second, they point out how politics determined the actual distribution of New Deal funds. One example they give is the dispersal of Works Progress Administration (WPA) projects. Given the supposed "compassionate" nature of the Roosevelt administration, one would think that those in the most dire need would receive the most help. Under the leadership of Roosevelt deputy Harry Hopkins, however, the WPA discriminated among states according to the political needs of the Democratic party, as government dollars were distributed according to their marginal political benefit.

Compensation was tied to area incomes. For example, an "intermediate" WPA worker in Tennessee would earn 23 cents per hour, while his counterpart in New York received \$1.57. Skilled laborers working on WPA projects made 31 cents an hour in Tennessee and Alabama and \$2.25 in New York. Professional pay was 34 cents per hour in Alabama and \$3.03 in Pennsylvania.

Hopkins, who uttered the infamous phrase, "We're going to tax and tax, and spend and spend, and elect and elect," justified the wide differentials in pay on regional differences in cost of living. Couch and Shughart, on the other hand, write that Hopkins was seeking maximum political returns and that marginal dollars spent in the wealthier northeastern and western states were far more effective in electing New Deal Democrats than in the South, where voting patterns had been solidly Democratic since the Civil War.<sup>1</sup>

Both the first and second New Deal programs were attempts to throttle movements of free markets, as the authors point out. The centerpiece of the First New Deal, the National Industrial Recovery Act (NIRA), was an unsuccessful attempt to organize nearly the entire U.S. economy into a series of cartels with codes governing output, wages, and prices. Even before the U.S. Supreme Court in 1935 declared it unconstitutional along with the infamous Agricultural Adjustment Act, the NIRA was tottering under the weight of its own contradictions.

Unlike much of the doomed legislation passed during the FDR administration's first "100 days," the Second New Deal contains legislative dinosaurs which still wreak havoc with the economy. Laws like the Social Security Act and the National Labor Relations Act, which firmly set the powers of government behind labor unions, still take center stage at every election.

One should not be able to read this book and come away with a belief that Roosevelt saved the country, or even saved capitalism. Couch and Shughart demonstrate too many times that the New Deal inhibited economic growth and thus needlessly continued the misery first wrought by the policies of Herbert Hoover.

One hopes that someone in the future will write a definitive Austrian view of the Great Depression, from its beginnings to its post-World War II end. Rothbard began the process; Couch and Shughart, while not Austrians, continue the analysis in a way that should be pleasing to most Austrians and fellow-travelers. We now await someone to take the next step and tie everything together.

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#### REFERENCES

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- Vedder, Richard K., and Lowell E. Gallaway. 1993. *Out of Work: Unemployment and Government in Twentieth Century America*. San Francisco: Independent Institute.

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<sup>1</sup>The authors, unfortunately, fail to mention one of Hopkins's political master strokes: placing hundreds of writers and photographers on the WPA payroll. Many of these writers, including Studs Terkel, later rose to places of prominence and continue to write pro-FDR propaganda to this day.