1929 Stock Market Crash Essay, Research Paper

The 1929 Stock Market Crash

In early 1928 the Dow Jones Average went from a low of 191 early in the year, to a high of 300 in December of 1928 and peaked at 381 in September of 1929. (1929?) It was anticipated that the increases in earnings and dividends would continue. (1929?) The price to earnings ratings rose from 10 to 12 to 20 and higher for the market?s favorite stocks. (1929?) Observers believed that stock market prices in the first 6 months of 1929 were high, while others saw them to be cheap. (1929?) On October 3rd, the Dow Jones Average began to drop, declining through the week of October 14th. (1929?)

On the night of Monday, October 21st, 1929, margin calls were heavy and Dutch and German calls came in from overseas to sell overnight for the Tuesday morning opening. (1929?) On Tuesday morning, out-of-town banks and corporations sent in $150 million of call loans, and Wall Street was in a panic before the New York Stock Exchange opened. (1929?)

On Thursday, October 24th, 1929, people began to sell their stocks as fast as they could. Sell orders flooded the market exchanges. (1929?) This day became known as Black Thursday. (Black Thursday?) On a normal day, only 750-800 members of the New York Stock Exchange started the exchange. (1929?) There were 1100 members on the floor for the morning opening. (1929?) Furthermore, the exchange directed all employees to be on the floor since there were numerous margin calls and sell orders placed overnight. Extra telephone staff was also arranged at the member?s boxes around the floor. (1929?) The Dow Jones Average closed at 299 that day. (1929?)

On Tuesday, October 29th, 1929, the crash began. (1929?) Within the first few hours, the price fell so far as to wipe out all gains that had been made the entire previous year. (1929?) This day the Dow Jones Average would close at 230. (1929?) Between October 29th, and November 13 over 30 billion dollars disappeared from the American economy. (1929?) It took nearly 25 years for many of the stocks to recover. (1929?)

By mid November, the value of the New York Stock Exchange listings had dropped over 40%, a loss of $26 billion. (1929-1931) At one point in the crash tickers were 68 minutes behind. (1929-1931) An average of about $50,000,000 a minute was wiped out on the exchange. (1929-1931) A few investors that lost all of their money jumped to their deaths from office buildings. Others gathered in the streets outside the Stock Exchange to learn how much they had lost. (Black Thursday?)

The Cause

There are five proposed reasons as to why the stock market crashed. One of the reasons was that stocks were overpriced and the crash brought the share prices back to a normal level. However, some studies using standard measures of stock value, such as Price to Earning ratios and Price to Dividend ratios, argue that the share prices were not too high. Another reason is that there were massive frauds and illegal activity in the 1920?s stock market. However, evidence revealed that there was probably very little actual insider trading or illegal manipulation. (1929?)

Margin buying is another reason why people believed that the crash happened. Though it is not the main reason, there was very little margin relative to the value of the market. The new President of the Federal Reserve Board, Adolph Miller, tightened the monetary policy and set out to lower the stock prices since he perceived that speculation led stocks to be overpriced, causing damage to the economy. Also, in the beginning of 1929, the interest rate charged on broker loans rose tremendously. This policy reduced the amount of broker loans that originated from banks and lowered the liquidity of non-financial and other corporations that financed brokers and dealers. Lastly, many public officials commented that the stock price was too high. Herbert Hoover publicly stated that stocks were overvalued and that speculation hurt the economy. Hoover?s statement suggested to the public the lengths he was willing to go to control the stock market. These kinds of statements encouraged investors to believe that the market would continue to be strong, which could be one of the causes of the crash. (1929?)

The Crash and The Depression

After the crash, production fell nearly 50% from the business cycle peak in August 1929 to March 1933. Meanwhile, the overall price level of stocks dropped by about 1/3. Many people blamed the crash for the economic collapse. Some people held responsible, fairly or not, were President Hoover, brokers, bankers, and businesspersons. The cause of the depression cannot be linked to one individual or even a group of people. It is also unlikely that the crash of the market would have been large enough to lead the US economy into the depression by itself and to sustain the downward spiral in business activity. (1929?)

Why People Invested in the Stock Market

During 1929, people invested in the stock market for five major reasons. The first was that the market was considered an easy way to get rich quick. Although about four million Americans, a small amount, invested in the stock market at one time, the constant influx of new investors coming in and old investors moving out ensured that new money was always flowing around. (1929?)

Another reason was the higher wages of the ordinary workers. This meant that everyone in America had extra money to put into savings or invest in the market. The third reason was that at this time, money was made more readily available from banks, at a lower interest rate, to more people. Some economist debated that this influenced the stock market, and it is conceivable that people took loans to buy more stock. (1929?)

The fourth reason is that industry was over-producing products, in anticipation of selling the surplus. Profits were put right back into the industry, by investing in factories, new machinery, and more people. This led to even more surplus. An aura of financial soundness was created by this, and Americans were encouraged to buy more stock. (1929?)

Lastly, there were no guidelines or laws concerning the market. Investors began buying on ?margin? or buying stock on credit. Investors had high expectations that they would receive large returns in a few months, so they could pay the balance and have money left over in return. In reality, most of the money that was being invested in the market was not actually being put into the market. (1929?)

Government Reaction

After the crash there was criticism of the Federal Reserve policy. Between October 1929 and February 1930 the interest rate was lowered from 6% to 4%, and the money supply increased immediately after the crash. Commercial banks in New York made loans to security brokers and dealers, which in turn provided liquidity to the non-financial and other corporations that financed brokers and dealers prior to the crash. (1929?)

Monetary policy became ambiguous between February 1930 and 1932. Government security purchases in the open market continued to decline until 1932. This reduced liquidity by lowering non-borrowed reserves. Although the interest rate was reduced between March 1930 and September 1931, it was raised twice in late 1931. This made loans more expensive and deterred people and corporations from borrowing. (1929?)

Government Regulations After the Crash

Before the crash, investors were not protected at all from fraud, hype and shoddy stocks. Investors did not know if a company actually doing as well as it was said to be doing and if the financial reports were reliable. After the crash, the Securities and Exchange Commission (SEC) was established to lay down the law and to punish those who violated the law. (1929?)

Also during the crash 4,000 banks failed, for the simple reason that the banks ran out of money. Four years later, Congress passed the Glass-Steagall Act, which essentially banned any connection between commercial banks and investment banking, to ensure that this would never happen again. The Federal Reserve and other banking regulators have softened some of the Act?s separation of securities and banking functions by letting banks sell certain securities through affiliated companies. (1929?)

1. Black Thursday: The 1929 Stock Market Crash. www.letsfindout.com.

2. 1929 Stock Market Crash. www.arts.unimelb.edu.

3. 1929-1931. Annals of America. Encyclopaedia Britannica Inc. Volume 15: 32-39