Government spending and taxation, lessons from the great depression and the econo...

Literature, Russian Literature

The Great Depression Government Spending and Taxation: Lessons from the Great Depression and the Economics of Social Security

The role of government is quite important during economic downturn. When there is a demand driven economy under which due to any reason the private sector fails to spend, the government needs to come up and provide support to the economy through fiscal measures (Kindleberger 1986, pp. 20 – 22)3. The New Deal is considered to be the defining moment during the Great Depression of 1930s and the government spending is viewed as the major step that improved the situation as many economists agree that at the point inadequate government spending led to the Great Depression ((Bordo, Christopher, Charles 2000, pp. 1447- 1448)1. Keynes's theory advocates that higher government spending and curtailment in taxes could be helpful in counteracting the depression (Kindleberger 1986, p. 24)3.

There is no mutual agreement on the idea of what were the main causes of the Great Depression of the USA. Reviewing its core nature, many believe that the severe contraction in early 1930s and later its slow recovery represent that fiscal policy had a minor role in this phenomena. Thinkers have come to this conclusion through theoretical and empirical studies of that period. Theorists say that even though federal government spending had risen considerably, it was not high enough to have a greater impact on the overall economy (Brown 1956, pp. 860 - 861). On the contrary, few economists believe that fiscal policy played a vital role in the emergence of the Great Depression (McGrattan 2011, p 1)4.

One of the most prominent changes in fiscal policy at that time was a sharp surge in taxes rates on the incomes of individuals which encompass

corporate dividends. Hovering taxes is one of the worst measures that government take to overcome crisis which makes the situation even worse. Increasing tax rates leave less money for consumers to spend and hence under this situation Federal Reserve suggests the government to refrain from this approach (Taylor 2002, p. 3).

The Great Depression which left many people out of pocket and discontented, ended up with the idea of social security that called for the government to take up the responsibility of economic security of its citizens. The New Deal provided people with the Social Security system in which employees give their contribution through taxes while they are on job to secure their future in economic term.

The statistics displayed in this particular representative form specifically imply that during the great depression i. e. around 1932 Private sector investments were the lowest hence taxation policies bringing revenue into the country was very small giving a lower annual GDP and in turn resurrecting a crumbling economy.

Table 1. U. S. Tax Rates, 1929–1939

With specific reference to the graphs been plotted there tabulate results are the extension of what and how the taxation policies plus the numerical figures have been determined.

Reference

1. Bordo, Michae D., Christopher J. Erceg, Charles L. Evans. 2000. Money, Sticky Wages, and the Great Depression. The American Economic Review. 90(5): 1447-1463.

2. Brown, E. Cary, 1956. Fiscal Policy in the 'Thirties: A Reappraisal. American Economic Review. 46(5): 857–879.

3. Kindleberger, Charles P. 1986. The World in Depression, 1929-1939. Berkeley: University of California Press.

4. McGrattan Ellen R., 2011. Capital Taxation During the U. S. Great Depression. Federal Reserve Bank of Minneapolis and University of Minnesota. Minneapolis, Minnesota: Research Department Staff Report.

5. Taylor, Jason E. 2002. The Output Effects of Government Sponsored Cartels During the New Deal. The Journal of Industrial Economics. 50(1): 1-10.