



As Dire as the Times May Seem, History Isn't About to Repeat Itself

A long streak of speculative lending got out of hand as banks and even staid industrial companies made a stream of risky loans. Consumer spending on cars and clothes was slipping, but no one was paying attention. The stock market grew shaky in September, and then in October, the bottom fell out.

Suddenly, everyone seemed to want to sell. But there were few buyers, and over six bleak trading days, the Dow Jones Industrial Average lost a third of its value. It was a panic, said a senior New York Stock Exchange official, "where all at once, the inconceivable terrors of the unknown and the unfamiliar are thrust upon the public mind; confidence is paralyzed, and until it is restored, chaos reigns."

The year, of course, was 1929, though it sounds just enough like today to make us wonder if we should stock up the pantry, take the cash out of the bank and hunker down for a 21st-century Great Depression. No doubt, the parallels are stark and frightening. But the differences between now and then are even greater.



Getty Images Depositors crowd outside a failed New York bank in 1931.

Let's start with lending. In the late 1920s, as the stock market took off, banks expanded their loans for those most unpredictable of assets: stocks. Investors could easily borrow up to 75% of the value of a stock purchase. By 1929, almost \$4 of every \$10 in bank loans went to buy shares. In addition, Chrysler, General Motors and Standard Oil of New Jersey all made tens of millions of dollars available for stock loans. In one of the most egregious examples, an energy company called Cities Service sold stock and then used the cash to make loans for people to buy more shares.

When the market started to fall, however, brokers had to call clients for more cash to secure their loans -- a so-called margin call. Because they had seen short downturns before, customers weren't eager to bail out. The entertainer Groucho Marx borrowed from the bank, against his life-insurance policy and against his house to come up with cash to meet his margin calls. But it wasn't enough. During that dark week in October, his broker sold all his stocks, wiping out his life savings of \$240,000 and leaving him deeply in debt.

"I would have lost more," he said later, "but that was all the money I had."

When those stock assets evaporated, an already weak banking system was crushed. In the first half of 1929, well before the crash, more than 300 banks had closed. More than 1,000 banks closed in 1930. Without a Federal Deposit Insurance Corp., depositors lost everything.

Initially, the Federal Reserve did nothing. To try to keep speculative borrowing on stocks from continuing, it declined to reduce interest rates, choking off credit. Unemployment climbed toward 25% at a time when there was no unemployment compensation. In the Prohibition era, those without jobs couldn't even legally drown their sorrows in beer.

Most striking was the long reluctance to acknowledge a serious problem. During the crash, President Herbert Hoover insisted that "the fundamental business of the country ... is on a sound and prosperous basis." With far fewer players in the stock market than today and with greater volatility, few saw the

crash's potential long-term impact. In fact, the New York Times declared Cmdr. Richard Byrd's first flight over the South Pole as the biggest news story of 1929.

The years after the crash told a different story. By the middle of 1932, the Dow had dropped 90% from its peak in September 1929. By the end of 1933, an estimated 44% of all first mortgages were in default. Only in the depths of that crisis did the government truly step up to address the many underlying problems.

Today, our mortgage mess looks like a disaster, too, but at least banks made loans against houses, assets that should continue to have at least some value. In the second quarter of this year, according to the Mortgage Bankers Association, 6.4% of mortgages were at least one payment behind and 2.75% were in foreclosure -- modern-day records, to be sure, but not depression levels. The long-term impact remains to be seen, but the acknowledgment and quick action by the Federal Reserve and Congress truly set this crisis apart from 1929.

Admittedly, that doesn't erase the ache of watching our life savings shrink or ease the fear of what might be ahead. Clearly there are repercussions yet to come. But here are a few suggestions for coping.

Remember that we've been through tough times before. The Internet bust was almost as extraordinary as the 1929 crash: Between early 2000 and late 2002, the tech-heavy Nasdaq index fell almost 80%. You may recall the speculative real-estate lending that resulted in almost 2,000 bank failures between 1987 and 1991, and the Dow plunging 22.6% in one day in 1987. While none of those were pleasant, you're still here.

Stay the course. You know this, but it's a time to return to the basics. Live within your means. Reduce your debt. Keep saving -- and investing. When the cycle turns, and it will, you'll be glad you did.

Put your losses in perspective. This isn't easy. I know: I'm feeling genuine pain after losing my entire investment in Washington Mutual and watching a mutual fund I bought in March for one of my retirement accounts drop by 36% -- and that's before this week. I absolutely cannot bear to tally up all my losses.

This is my reality check: For more than a decade, I have gone to my local elementary school to tutor. There I spend time reading with children who own no books of their own, whose families can't afford school supplies and who have never been to a dentist. For the price of 45 minutes a week, I return to my desk feeling as wealthy as any one person needs to be.

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