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THE *NEW* NEW DEAL FRACAS: DID ROOSEVELT'S "ANTICOMPETITIVE" LEGISLATION SLOW THE RECOVERY FROM THE GREAT DEPRESSION?

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Introduction

As recently as 1980, Michael M. Weinstein stated, "Most of those who have considered the macroeconomic impacts of the [1933 National Industrial Recovery Act (NIRA)] codes have either dismissed their importance or considered them to have been weakly salutary" (Weinstein, 267). NIRA, which President Franklin Roosevelt called "the most important and far-reaching legislation ever enacted by the American Congress" (quoted in Hawley 1966, 19), called for industry codes that would ban child labor, end unfair business practices, limit the length of the workweek, facilitate union organization, and regulate wages and prices. NIRA was followed by the National Labor Relations Act (NLRA) of 1935, which put the right to organize on a firmer footing. But in the 25 years following World War II, most economists and policymakers believed that these laws had little to do with the speed of the recovery from the Depression.

This view is now being challenged by a wave of revisionist work claiming to show that NIRA and NLRA slowed the economic recovery from 1933 to 1939. Amity Shlaes, in her controversial work *The Forgotten Man* (2007, 8), states that rules written under NIRA "were so stringent they perversely hurt businesses. They frightened away capital, and they discouraged employers from hiring workers." She also blames continuing high unemployment in the mid and late 1930s partly

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on strikes that were made possible by NLRA. Shlaes concludes that "government intervention helped to make the Depression Great" (9), a claim that she repeated in *Time* and *Forbes* earlier this year (2009a, 2009b).

Economists have also weighed in with articles on the deleterious effects of "anticompetitive" New Deal legislation on the speed of the recovery (Cole and Ohanian 1999; Prescott 1999; Bordo, Erceg, and Evans 2000; Chari, Kehoe, and McGrattan 2002; Cole and Ohanian 2004). Lee Ohanian has argued, again in *Forbes,* that "the Depression lasted far longer than it should have," and that "government policies that restricted competition" such as NIRA and NLRA appear to be the "main culprit" (Ohanian 2009c, 1; Ohanian 2009a). Eric Rauchway (2008b) and Benjamin Friedman (2007) have argued in defense of NIRA, NLRA, and the rest of the New Deal in articles in the *American Prospect* and the *New York Review of Books.*

These debates have continuing political relevance. It is likely that the recession (or at least an extremely weak job market) will wear on for some time, and Washington is pondering a second stimulus bill. No one is proposing legislation similar to the parts of NIRA that enabled industries to form cartels, but the Employee Free Choice Act, an important prolabor bill in the spirit of both NLRA and section 7(a) of NIRA, is being drafted. As a result of the new New Deal fracas, the revisionists' theories will be at the back of lawmakers' minds as they consider this proposal and others to help bring about recovery and lasting reform. A vindication of NIRA and NLRA—even one that acknowledges deep flaws—would help buttress the reputation of government intervention in the economy at a time when lawmakers should be turning to the New Deal as a model for a new economy.

The Purpose of NIRA

When he sent the recovery bill to Congress shortly after assuming office in 1933, Roosevelt stated its goals: "to obtain wide reemployment, to shorten the workweek, to pay a decent wage for the shorter week, and to prevent unfair competition and disastrous overproduction" (quoted in Roos 1971, 41). Critics have focused on Title I, which authorized the president to endorse or amend codes drawn up by trade or industrial groups, and to impose such codes in industries where no agreement could be reached. Section 7 specified that each code "had to contain an acceptable provision for maximum hours, minimum wages, and desirable working conditions. In addition, it had to include a prescribed section 7(a), which outlawed yellow dog contracts [which forbid workers who sign them from joining unions] and guaranteed the right of laborers to organize and bargain collectively" (Hawley 1966, 32). "The act…was designed to promote cooperative action, eliminate unfair practices, increase purchasing power, expand production, reduce unemployment, and conserve natural resources; but there was little to indicate the type of code provisions that might be used to achieve these laudable objectives" (32).

Critics claim NIRA had the effect of allowing firms to work together to set prices, resulting in lower output. (Although the law prohibited codes that allowed collusion, it also exempted the new codes from antitrust laws, one of numerous contradictory parts; see Bellush 1975, 29.) Many historians and economists believe that in practice the bill increased the monopoly power of large firms. New Deal critics also fault NIRA's minimum wage and collective bargaining provisions, on the grounds that they increased wages above competitive levels, reducing employment.

What led politicians, in the midst of the Depression, to support measures that most economists now regard as antigrowth? First, many economists and others believed that the Depression's root cause was overproduction (Wolfskill 1969, 62–63; Weinstein 1980, 3). As policymakers saw it, the modern economy produced more goods than consumers were able to purchase. As a result, prices were falling, and firms were drastically cutting wages and payrolls in an effort to stay in business. The new codes would deal with this situation by preventing sales at below cost, among other unfair practices. Also, the bill would shorten the workweek so as to spread work hours among more workers and boost the purchasing power of workers by raising wages.

While NIRA was designed to speed recovery, the portion of the bill calling for industrial codes was not envisioned mainly as a stimulus to economic growth. Beyond its economic purposes, NIRA was intended to address social issues, such as child labor and exploitative employment. Moreover, the administration and others had in mind the idea that the U.S. economy had reached a "mature" phase in which significant, sustained growth was no longer possible. Other policy objectives were now more relevant, including the "less dramatic business . . . of adjusting production to consumption, of distributing wealth and products more equitably, of adapting existing economic

organizations to the service of the people" (Roosevelt, quoted in Kennedy 1999, 373).

Were NIRA and NLRA to Blame?

The articles cited in the introduction argue that NIRA and/or NLRA impeded economic recovery in a number of ways. This brief focuses on the *cartelization* hypothesis—the idea that "cartels" (industry groups and unions) formed under NIRA and NLRA were the culprit—which is considered in academic work by Harold Cole and Lee Ohanian (2004, 2009) and popularized in congressional testimony and magazine articles by Ohanian (2009a, 2009b, 2009c). Cole and Ohanian begin by describing what they regard as a subpar recovery after the economic collapse of 1929–33 (2004, 779–81). Despite some favorable "shocks" to the money supply, productivity, and the banking system, real GDP per adult was still 27 percent below trend in 1939. The total number of hours clocked by U.S. workers was also well below trend. Using a standard macroeconomic model, Cole and Ohanian find that in the absence of some interference with the "competitive" economic system, output and employment would have returned to trend by the late 1930s.

Some economists believe that the economy performed well in the years after 1933 (e.g., Romer 1992, 757). Cole and Ohanian do not agree, even leaving aside the severe recession of 1937–38. Using a model intended to capture certain key effects of NIRA and NLRA—a suspension of the antitrust laws that permitted collusion in many industries, and provisions that promoted collective bargaining, which allegedly caused unemployment by raising wages above competitive levels—they find that "cartelization policies" account for about 60 percent of the gap between actual and potential GDP (2004, 781).

Models similar to Cole and Ohanian's are now the norm in mainstream academic macroeconomics, and they have shortcomings that cannot be adequately addressed here. Instead, the brief considers the present-day implications of the cartelization hypothesis, the applicability of Cole and Ohanian's model to the Depression era, and some neglected aspects of the New Deal, challenging a key revisionist claim that is not necessarily tied to any particular modeling methodology.

What Did NIRA and NLRA Do?

The cartelization hypothesis, as advanced by Cole and Ohanian, depends on the claim that in the absence of NIRA and NLRA, perfect competition would have prevailed in all markets. Instead, these laws strengthened the monopoly power of firms and resulted in an increase in the number of workers represented by unions. Cole and Ohanian also rely on the theory that these effects could be expected to reduce economic growth. Indeed, many historians believe that NIRA allowed "the large corporations which dominated the code authorities [to use] their powers to stifle competition, cut back production, and reap profits from price-raising rather than business expansion" (Leuchtenberg 1963, 69).

Cole and Ohanian measure the effects of NIRA versus a baseline model with perfect competition. Though it is impossible to ascertain whether industry would have been perfectly competitive without NIRA, one can infer what would have happened by comparing the 1930s with the previous decade. If monopoly power was already widespread in the 1920s, it is unlikely that perfect competition would have existed in 1933–39 in the event that NIRA and NLRA had not been passed.

There is some empirical evidence of a lack of competition in many industries in the 1920s and earlier (Stigler 1950, 46–59; Chandler 1990). Throughout the 1920s, large businesses, with the cooperation and help of the federal government, were forming "trade associations" that had the effect of diminishing competition. When the Depression began, cooperation among firms began to break down amid pressure to cut prices. At the same time, antitrust officials began to challenge many trade-association codes. The NIRA codes represented a response to these new difficulties and were "largely a direct offshoot of the trade-association system" (Bellush 1975, 44; see also Himmelberg 1976). Hence, NIRA cannot be seen as a government imposition of cartels on a purely competitive system.

In addition to the industrial cartels, Cole and Ohanian's model includes bargaining between industry and unions, which is meant to represent the pro-union effects of NLRA and section 7(a) of NIRA. In essence, unions are viewed as "monopolies" for workers. Cole and Ohanian find that labor's newfound bargaining power accounts for a large portion of the negative effects (e.g., lower employment and output) of New Deal anticompetitive legislation on GDP. However, while the new collective-bargaining laws were a crucial step forward for the union movement, their immediate effect was rather weak,

largely because the National Recovery Administration (NRA, the agency charged with implementing the codes) had a probusiness bias (Hawley 1966; Bellush 1975; Biles 1994, 83–102; Leuchtenberg 1963, 69–70). Less than 10 percent of the authorities that administered the codes had some labor representation (Bellush 1975, 47), and many corporations evaded the labor codes required by section 7(a) (Conkin 1975, 33).

Things did change somewhat in 1935 after the passage of NLRA and the Supreme Court's ruling that NIRA was unconstitutional. Cole and Ohanian state that "union membership rose from about 13 percent of employment in 1935 to about 29 percent" in 1939 (2004, 785). Hence, their assumption that union negotiating power was elevated by the New Deal is more plausible for the period from July 1935 to 1939 than for 1933 to July 1935. Nevertheless, even after 1935, the union movement advanced gradually and with strong opposition.

Cole and Ohanian clearly do not pretend to engage in a thorough evaluation of the social costs and benefits of unions, focusing instead on the unions' "monopoly" function. To the extent that NLRA helped the unions organize more workplaces, it produced benefits not just for union members but for American business and society (see Freeman and Medoff 1984). There were certainly costs, too, but an argument can be made that unions actually help create jobs in nonunionized industries by enlarging the working-class market. These facts put into context Shlaes's statement that Roosevelt "systematized interest-group politics . . . , ministered to those groups [including "labor" and "unionized workers"], and was rewarded with votes" (2007, 11).

In sum, Cole and Ohanian base their assertions on results from a careful modeling exercise that says little about the overall economic effects of NIRA and NLRA. Monopoly power may have hurt consumers in the 1930s by raising prices and reducing output, but NIRA cannot be blamed entirely for cartels and monopolies that dated to the 1920s and earlier. NLRA and section 7(a) of NIRA were major steps in the rise of the union movement, but even if labor's bargaining power was somewhat increased, it is important to avoid the impression that Democratic "interest groups" such as labor were running rampant in an economically counterproductive manner.

What Is Left Out of the Cole and Ohanian Model?

Cole and Ohanian have included in their model one of the most flawed, least effective, and most weakly enforced pieces of New Deal legislation: NIRA. The codes required by this law were not intended primarily to boost economic growth. Though it would be a daunting task, we wonder what would happen if Cole and Ohanian's model were modified to take into account all of the major New Deal laws, or at least those thought of as progrowth.

Many historians have written about what the New Deal accomplished (e.g., see Kennedy 1999, 363–380; Rauchway 2008a). In the South, agricultural programs provided money for the mechanization of agriculture, perhaps helping to bring an end to the exploitative and inefficient sharecropping system (Biles 1994, 56–57). Public works programs yielded not only paychecks but also national parks, roads, bridges, and post offices (Leighninger 2007), and federal deposit insurance all but eliminated old-fashioned bank runs. Social Security remains perhaps the most popular federal program, helping many seniors avoid poverty. The economic effects of the New Deal were vast and far-reaching. A demonstration that NIRA and NLRA inhibited economic recovery does not amount to an argument that the New Deal slowed recovery or failed to increase output over the long run (Rauchway 2008b, 2).

Some Other "Forgotten Men"?

The title of Shlaes's book is *The Forgotten Man,* a phrase remembered in connection with the New Deal because of a speech in which Roosevelt appealed to his audience on behalf of "the forgotten man at the bottom of the economic pyramid" (quoted in Shlaes 2007, 12). Shlaes sees her book in part as the story of many other forgotten men. Among numerous examples, she cites the case of Martin Schechter and his family, butchers who were prosecuted for violating NRA codes and who ultimately prevailed in the Supreme Court. More generally, she counts the consumer and small businesses among those forgotten by the NRA (Shlaes 2007, 226–27). One scholarly account argues that NIRA's representing "a triumph of big over small business is accurate only in a limited and special sense" (Himmelberg 1976, 221). Nonetheless, the claim that NIRA often helped large corporations at the expense of small enterprises is not without merit.

Shlaes also mentions many of the problems experienced by African Americans during Roosevelt's presidency, yet she does not point out that they suffered unfair treatment under NIRA. Biles reports that "NRA codes exempted from coverage agricultural laborers and domestics, two categories that accounted for three-quarters of southern black workers" (1994, 111–12). Some codes for mainly African American regions and occupations imposed wages that were lower than pre-NIRA levels (75–81). NLRA, in its original form, replicated some of NIRA's inequities. To mention racial disparities in NRA codes is not to criticize *The Forgotten Man* or to deny that many others suffered injustice under NIRA, but it helps round out Shlaes's reckoning of the impact of early New Deal legislation, not to mention our very favorable view of Roosevelt's first 100 days.

Conclusion

Cole and Ohanian, in a recent article in the *Milken Institute Review,* conclude "that the primary test for judging the value of [government] intervention should remain a familiar one: would the change preserve (or improve) market-based incentives to work, save, invest, and innovate? By this measure, the New Deal plainly came up short" (2009, 25). This brief suggests that any adverse effects of NIRA and NLRA on incentives were probably so inconsequential as to be overshadowed by the obvious benefits of legislative accomplishments such as Social Security and federal deposit insurance. NIRA, and to a lesser extent NLRA, admittedly had many flaws, but these should not obscure the fact that the New Deal helped the country through a desperate time and lay the basis for a quarter century of relative prosperity following World War II. Business interests that oppose a new New Deal would do well to remember that it was not only labor that prospered: the inflation-adjusted, after-tax profits of corporations rose 377 percent from 1935 to 1970.[1]

Like Roosevelt's "first New Deal," President Obama's early legislative achievements will not suffice to bring lasting prosperity, especially to those who struggled to make ends meet even before the current recession. But Obama still has a chance to stiffen financial regulation, reform the health care system, safeguard labor rights, and alleviate the effects of the recession. The New Deal can provide some of the inspiration needed for these efforts.

Note

1. Computed from the implicit price deflator (Bureau of the Census 1975, 197) and total profits after taxes (236).

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