The U.S. and World War I

- War started in Europe in August 1914
- US joined in April 1917
- Background to U.S. entering the War
  - By 1914 the US was the world leader in mfg
  - U.S. gained new markets; we acquired a huge trade surplus
  - Both Germany and Britain tried to blockade our goods
  - Britain blockaded German ports and seized cargo destined for neutral countries
  - Germany had a policy of unrestricted submarine warfare around British ports
U.S. Entry and siding with the British

- 1) people of English heritage in US positions of power
- 2) private loans $2.5 billion to allies and $45 million to central powers
- 3) against war: German and Irish Americans, militant labor groups and pacifist elite groups
Mobilization

- **Manpower**
  - 1) 4 million American men drafted – 1/6 of labor force
  - 2) 117,000 Americans killed, 200,000 wounded
  - 3) European deaths: Germany 2 million, Russia 2 million, France 1 million, Britain $1 million
  - 4) 1918 influenza kills 25 million (ahead of AIDS as the worst disease of the 20th century)
Industry

- 1) 20-25% of US GDP to War effort (total cost $35.5 billion)
- 2) unprecedented government controls over the economy
Nature of Government control

- July 1917
  - War Industries Board, clearing house for government demands; headed by Bernard Baruch

- Initially relied on voluntary cooperation – over time more boards and regulation – government wanted direct control
Regulatory Boards: heads came from the private sector

1. businessmen/regulators believed that they would gain by collusion: business always wants to get rid of competition

2. By the end of the War: 5000 distinct boards
   - National Food Administration (Herbert Hoover, head) – food rationing
   - National Fuel Administration – coal rationing
   - Shipping Board: began to build a navy
   - Direct government control of railroads, telephone, and telegraph
   - Price and wage controls: conceal costs instead of taxes

Why Regulate? “Belief that markets would not work fast enough”
   - FedEx vs. the post office?
Price controls: selective

- Controls were meant to be temporary. Designed to prevent relative price increases in “essential” goods and war supplies

Costs of controls

- 1. bureaucracy – direct costs of implementation
- 2. black markets: undermines civic society
- 3. inefficiencies – if $S < D$ prices don’t allocate resources efficiently
- 4. rationing – cost of waiting, queuing
- 5. deterioration of product quality
Growth of expenditure and taxes

1. Revenue
   - before 1917 never > $762 million
   - 1920s never < 3640 million

2. Expenditures
   - before 1917 never > $747 million
   - during 1920s never < $2800 million

3. National debt
   - 1917 $1 billion
   - August 1919 $26.6 billion

Only half the increase can be explained by trend growth or inflation

4. After the war: interest on debt exceeded cost of running the entire government prior to the war
Total Financial Cost of the “Great War”

- $35.5 Billion – including the $9.5 billion of loans to allies

- War finance – taxes, bonds and inflation
  1. Taxes: 1/3 of revenue raised by taxes
     - Income tax adopted in 1913 – rates: 6-63%
     - 2/3 of total taxes
     - War profits tax 15-60%
     - Excise tax on alcohol and luxury goods
     - Taxes on public utility services
     - Increased estate taxes
  2. War loans – liberty bonds $21 billion
     - War Saving Certificates of $5 denomination
     - War Saving Stamps of $0.25 denomination
3. Inflation

Gold was flowing in: by 1919 we had ½ of the world supply

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The Legacy of World War I

- Population became accustomed to government intervention “we won the war, therefore the strategy must have been right”
- The post-war scale-back of controls was not complete:
  - Ratcheting upwards of government intervention
- Next crisis: call in the government?