**How could this help cause a Depression?**

When wealth piles up the hands of just a few people, it essentially becomes useless wealth. Imagine ten million dollars distributed between 10,000 people (so that each person gets $1,000). In this scenario, those 10,000 people will probably go out to dinner, buys some clothes, and spend their money. In doing so, they’ll help employ people at restaurants, clothes factories, and so on. However, if that $10,000,000 is given to just one person, that person probably won’t find good ways to spend it. He or she will just put a lot of it in a bank. Instead of helping the economy, all that money becomes useless. At the same time, poor people are forced to borrow—a problem that will be addressed by another group.

**How could this cause a depression?** This can only happen in a time period of relaxed monetary policy. In a time of relaxed monetary policy, it is very easy to borrow money because interest rates are low. Under a strict monetary policy, interest rates are high, so people borrow very little. The Federal Reserve Bank can set interest rates and control monetary policy. In any case, the rise of private debt and the relaxed monetary policy caused a problem. With so many people taking out credit, banks loaned out more money than they could afford. Banks found themselves in debt, and had to close down. When a bank closed, it took with it all the savings of its users! Before the Great Depression, banks were ready to collapse.

**How could this cause a depression?** As people clamored for stocks, the prices of stocks rose. Why? Imagine one person buying an orange from a grocer. The grocer and the buyer have to agree on a price. Now imagine 100 people buying an orange from a grocer. Wow! That orange is a hot item! The grocer may charge more, even though nothing changed about the orange. This is how it went with stocks. Their prices soared. But the rising value of stock didn’t come from actual increases in the value of the companies selling them, but only from the increased demand. In October, 1929, investors suddenly realized that their stock was actually worthless—the illusion of stock value had come from speculative investment. Stock prices plummeted and bottomed out at 90% of their high. People who had thought of themselves as rich were suddenly broke.

**How could this cause a depression?** It is simple. When more is produced than people want or can buy it throws prices out of whack. Furthermore, businesses in the 1920s did not respond to decreased demand and continued to pump out a massive supply. To counter the costs, businesses began laying-off workers. As more and more workers were let go people lost their buying power because they did not have money to buy the products that businesses were producing. This caused a circular chain reaction that ultimately lead to economic collapse and depression.

**How did this cause the Great Depression?** The US was counting on the money that was owed and thus made economic decisions dependant on the money from European war debt. Because Germany struggled to pay reparations and our European allies were trying to rebuild their war-torn countries a post-war recession spread through Europe. When the money was not paid the US, the European recession trickled over the Atlantic Ocean. Because European countries could not afford to buy US goods, the contraction of the US economy due to overproduction, speculation and the absence of payments of WWI war debt, demand for US products dropped significantly and the US economy plunged into recession.