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THE U.S. ECONOMY DURING WORLD WAR I

Abstract: This study examines the economic impact of World War I on the United States, analyzing the mobilization of resources, financial strategies, and industrial expansion during the war period. The war, despite the U.S. suffering fewer casualties than European nations, required a large-scale economic and military mobilization. The research discusses how the U.S. transitioned from neutrality to active involvement, including changes in industrial production, taxation policies, and government interventions in various sectors. Additionally, the study explores the financial burden of the war, focusing on war bonds, taxation, and government expenditures. The paper also highlights the geopolitical and economic factors that led to American participation in the war and assesses the long-term economic consequences of the conflict on U.S. development.

Keywords: World War I, U.S. economy, war mobilization, financial policies, taxation, war bonds, industrial expansion, economic impact, geopolitical factors, military expenditures.

Introduction

World War I required the largest resource mobilization in the United States since the Civil War. Despite suffering fewer casualties than European nations, the U.S. faced significant economic and military challenges. The war transformed the American economy, leading to increased industrial production, government interventions, and changes in financial strategies. This study examines the economic impact of the war, including taxation policies, war bonds, and the long-term consequences for U.S. economic development. The paper also explores the geopolitical and economic factors that led to American involvement in the war and assesses how economic conditions influenced wartime policies.

Results and Discussion: The mobilization for war significantly altered the U.S. economy. Industrial output increased to meet the demands of war, leading to significant government interventions in various sectors. The War Industries Board was established to regulate production, and the Emergency Revenue Act of 1917 introduced an excess profits tax to fund military expenses. The study also explores the impact of international trade disruptions. Initially, the U.S. maintained neutrality, but restrictions imposed by the Allied blockade and German unrestricted submarine warfare strained economic relations. The resumption of unrestricted submarine warfare in 1917 and the interception of the Zimmermann Telegram ultimately led to U.S. entry into the war. Financially, the war was funded through taxation and borrowing. War bonds became a primary tool for financing military operations, while the excess profits tax accounted for approximately 30% of total tax revenue. Despite economic growth, the war placed a financial burden on the government, leading to long-term fiscal policies that shaped post-war economic strategies. The involvement of the U.S. military shifted the balance of power on the Western

Front, aiding the Allies in securing victory. The rapid expansion of the military, from 200,000 soldiers to nearly five million, demonstrated the nation's ability to mobilize both human and financial resources effectively. However, the study highlights that economic superiority alone did not determine the outcome of the war—organizational efficiency, technological advancements, and military strategies played crucial roles.

Methods: Historical analysis, Chronological.

The world must be a safe place for democracy. The peace of democracy must be based on political freedoms. We have no selfish motives in our service. We do not seek conquest or domination. We demand no reparations, nor do we receive any material compensation for the sacrifices we have voluntarily made.

From President Woodrow Wilson's message to Congress on declaring war against Germany, April 2, 1917.

World War I required the largest resource mobilization in the United States since the Civil War. Although American losses were relatively lower than those of European nations, they were still a heavy blow for the U.S. Approximately 53,000 Americans died on the battlefield, and another 63,000 perished due to injuries and diseases, including the influenza epidemic that spread worldwide in the final stages of the war. Additionally, 204,000 people suffered non-fatal injuries. On June 28, 1914, in Sarajevo, Bosnia, a young Serbian revolutionary, Gavrilo Princip, assassinated Archduke Franz Ferdinand of Austria and his wife, Sophie. This event triggered a strong chain reaction, leading to a violent war. First, the Austro-Hungarian Empire, possibly desiring to occupy Serbia, presented it with a list of strict demands. When Serbia failed to comply, the empire declared war on it. As a result:

- Russia initiated military actions,
- Germany joined the war on the side of Austria-Hungary,
- France entered the war in support of Russia,
- Great Britain joined the war in support of France.

Thus, two bullets fired by a single revolutionary started the bloodiest war in human history until that time. According to historian Niall Ferguson (2003), this war was not an inevitable event caused by fundamental forces, but rather a tragic, yet preventable, occurrence. However, the world was becoming an increasingly dangerous place. Several political, social, and economic factors contributed to this. Although a relative peace prevailed between the Franco-Prussian War (1870–1871) and World War I (1914–1918), numerous wars in European history demonstrated the continent's tendency toward military conflict and organized violence. The Austro-Hungarian Empire had strong ethnic tensions, leading to widespread dissatisfaction. Additionally, territorial struggles between European states, the arms race, and intense competition increased the likelihood of war: Austria-Hungary wanted to annex Serbia, while France sought to reclaim Alsace-Lorraine, which had been lost to Germany in the Franco-Prussian War of 1870–71. One of the frequently emphasized economic factors was the struggle among the Great Powers for colonies in the late 19th century. This competition for colonies in Africa, Asia, and other regions of the world heightened tensions among European states and significantly contributed to the military-naval arms race. John A. Hobson (1900, 1902), in his research, argued that the struggle for colonies was not the result of broad economic interests but rather manipulation by financiers. According to him, imperialism did not serve the interests of the entire capitalist class, nor did it bring any benefits to ordinary people—merchants, producers, farmers, and workers. In reality, imperialism was a result of investors who had invested in foreign countries seeking government support to secure returns on their investments. Vladimir Lenin (1916), in his famous work

Imperialism, the Highest Stage of Capitalism, put forward similar arguments. As a result, this theory became known in history as the "Hobson-Lenin Thesis." Some historians linked this argument to the macroeconomic demand problem. According to them, by the late 19th century, Europe had accumulated surplus capital, which needed to be directed into foreign investments. In other words, European imperialists required a large export surplus to maintain economic demand and ensure full employment. Fearing unrest due to high unemployment, imperialist states fiercely competed for colonies as investment opportunities and markets. In recent years, macroeconomic trends have weakened the foundations of the idea that imperialism arose solely to maintain full employment. Traditionally, Keynesian economists emphasized that market economies tend to fall below full employment levels and argued that state policies, such as increasing public spending on infrastructure projects, were necessary to support aggregate demand. Within this model, conducting imperialist policies to expand export markets was somewhat logical. This approach, while perhaps secondary to increasing public spending on hospitals and universities, was still considered economically justified. However, in recent years, first monetarist models and later real business cycle models have displaced the Keynesian approach. These new theories emphasize that economies have a tendency to adapt to crises and return to full employment levels. Consequently, the idea of viewing imperialism as a means to stimulate aggregate demand has been questioned within new economic models. Additionally, economic historians have analyzed new types of data and challenged the interpretation that "war occurred solely for economic reasons." In their research, Davis, Huttenbach, and Davis (1986) found that investments in the British Empire were unprofitable. Although some studies have questioned certain aspects of the Davis-Huttenbach-Davis thesis, it remains likely that Britain's rivals overestimated the actual economic value of its empire. At the same time, justifying war solely based on economic interests is difficult. Even if Germany and Austria-Hungary faced some economic difficulties due to their lack of a large colonial empire, it was evident that these states were experiencing economic growth and prosperity before the war. In fact, World War I began against the backdrop of a long period of economic growth, rising living standards, and increasing overall prosperity. Therefore, it is difficult to prove that the war was triggered by worsening poverty or economic crisis. If one were to evaluate the war only from the perspective of the resources of both sides, then a war between the Allied Powers (Britain, France, Russia, Italy, and their allies) and the Central Powers (Germany and Austria-Hungary) should have been impossible. Niall Ferguson stated that the total population of the Allied Powers was 4.5 times larger than that of the Central Powers, and their total GDP was 60% greater. However, history has shown that economic superiority does not always guarantee victory. Victory often depends on factors such as organizational efficiency, determination, access to advanced technology, and geographical advantages. Wars frequently occur due to miscalculations in assessing these factors. Therefore, explaining war outcomes solely based on economic superiority may be incorrect. Despite the dangers of the arms race, particularly the naval arms race, as well as the predictions of some forecasters about future conflicts, evidence suggests that most Europeans did not perceive or pay attention to the impending catastrophe on the eve of the war. Niall Ferguson advanced this idea through an analysis of financial markets. Historians have traditionally paid insufficient attention to financial indicators, but economic historians are increasingly turning to such sources. Not everyone owned stocks or bonds, but a significant portion of the European elite held such assets. Therefore, stock and bond prices could indicate how seriously the influential segments of European society perceived the likelihood of war. According to the data analyzed by Ferguson, the interest rates on long-term government bonds issued by Britain, France, and Germany increased slightly after 1910 but remained relatively stable 18 months before the war. This implies that: There was little evidence in financial markets that war was seen as an imminent catastrophe; Market participants did not anticipate the closure of bond markets (for several months in Britain, and throughout the war in Germany) or severe wartime inflation. In other words, the severe economic consequences of war were not widely understood by the public in advance. In fact, the U.S. entry into the war led to an overall decline in the stock market, which is surprising given that even war-related stocks dropped. Various hypotheses exist regarding the reasons for this: Investors may have believed that economic disruptions caused by the war would outweigh the increased demand resulting from military mobilization; or the rising costs of war and the possibility of higher taxes, especially an excess profits tax, may have concerned investors. President Woodrow Wilson's administration included an excess profits tax in the Emergency Revenue Act of 1917. The high costs of the war indicated that the government might rely even more on such taxes. In 1914, European states may not have fully understood the catastrophic consequences of the war, but by April 1917, when the U.S. joined the war, its devastating impact was evident. The reasons for the U.S. entering the war: The dire situation of Britain and France. German attacks inflicted heavy losses on these nations, increasing the U.S.'s desire to assist them; Protecting trade rights. When the war began, the Allied Powers blockaded European coastlines, considering even food supplies as contraband. Washington strongly criticized this action as a violation of international law; U.S. companies attempted to trade through neutral countries such as Sweden, but the Allies extended the blockade to include neutral Baltic states. This situation resembled the experience of the U.S. during the Napoleonic Wars when violations of American trade rights brought it close to war with France and into war with Britain. Ultimately, what angered the U.S. public was not the traditional blockade enforced by Allied naval ships but Germany’s use of submarines. Of course, the British blockade provoked dissatisfaction in the U.S. Between 1914 and 1915, Britain banned the export of cotton to Germany and Austria, causing widespread protest in the southern U.S. states where cotton production was a crucial industry. However, the crisis was resolved when Britain agreed to purchase the cotton that was initially intended for Germany and Austria. Differences in British and German methods Most Americans viewed the British blockade as a "civilized war." British naval ships stopped American vessels, escorted them to British ports, and treated crew members well. Additionally, if a detention was found to be unjustified, U.S. companies could claim compensation for damages. However, the German submarine warfare strategy was entirely different. German submarines launched attacks without warning, preventing civilians from having a chance to save their lives. The Germans lacked a sufficient surface fleet to impose a conventional blockade and had to rely on submarines, which increased the likelihood of U.S. entry into the war. The sinking of the Lusitania (May 1915) The first German submarine attack that provoked American public outrage occurred in May 1915. The passenger liner Lusitania was torpedoed while en route from New York to Britain. The ship carried not only civilians but also military cargo. The attack resulted in the deaths of over 1,150 passengers, including 115 Americans. Many Americans viewed this as a brutal violation of international war regulations. After the Lusitania incident in 1915, the Germans sought to avoid a direct confrontation with the U.S. They agreed to issue warnings before attacks and to allow passengers to be rescued. This truce, however, did not last long. 1917: The resumption of unrestricted submarine warfare In February 1917, Germany resumed unrestricted submarine warfare. The goal was to force Britain into surrender by starving it through naval blockade. As a result of the sinking of numerous ships, President Woodrow Wilson severed diplomatic relations with Germany in February 1917. In April, he asked the U.S. Congress to declare war on Germany. Other factors: The Zimmermann Telegram Other evidence indicated that Germany was planning military actions against the U.S. The "Zimmermann Note" was a secret telegram sent by Germany to Mexico, offering support for Mexico to wage war against the U.S. This message was intercepted by British intelligence and caused a significant uproar in the U.S. Wilson’s main statement on entering the war When explaining the U.S. entry into the war, President Wilson primarily cited Germany’s unrestricted submarine warfare as the main reason. Although the "Zimmermann Note" and other factors played a role, Wilson’s speech mainly focused on Germany’s attacks on ships as the justification for war. It is difficult to claim that the decline in U.S. exports to Europe due to the German blockade was the main reason for entering the war. In reality, U.S. exports surged during the war: In 1913: $1.479 billion; In 1917: $4.062 billion; In 1919: $5.188 billion. Even when adjusted for inflation, the real volume of exports increased significantly. If the U.S. had not entered the war and trade with Europe had completely ceased, the total loss would still have been relatively small compared to the war costs. According to calculations, at 1917 prices, export losses would have amounted to $2.031 billion, which equated to: 3.7% of U.S. GDP in 1917; Only 6.25% of the war's cost. The U.S. entered the war not for economic profit but for principles. The main reason for joining the war was not to compensate for lost revenues but to protect international trade freedom. In other words, the U.S. fought for "principle," not just "capital." This approach demonstrated the U.S.'s commitment to maintaining the global trade order and protecting its free trade interests. In 1917, the U.S. Army had only 200,000 soldiers, a small force compared to the millions of troops in European armies. A military draft was introduced, quickly increasing the army's size: A total of 4,791,172 people were drafted into military service; 2,084,000 soldiers were deployed to France; 1,390,000 soldiers participated in combat. This was a significant achievement in a short period, considering that the U.S. actively participated in the war for only a year and a half. The impact of the U.S. Army on the war's outcome: On March 21, 1918, Germany launched an offensive on the Western Front, pushing back British and French forces at the Battle of the Somme. By May and June, German forces advanced within 50 miles of Paris through new offensives. At this stage, Americans had not yet participated in large numbers. Key battles involving U.S. troops: The Battle of Belleau Wood (June 6 – July 1, 1918) → One of the first major battles involving the U.S. Army, resulting in an Allied victory. The Second Battle of the Marne (July 18 – August 6, 1918) → The addition of American forces helped the Allies halt the German offensive, marking a turning point in the war. In conclusion, the entry of the U.S. Army into the war shifted the balance of power on the Western Front, aiding the Allies in securing victory. American troops played a crucial role in a series of offensives that forced the Germans into retreat. The armistice was signed on November 11, 1918. Although the existence of the excess profits tax during wartime has often been noted, its importance in financing the war has been underappreciated. This is partly because it is difficult to reconcile different Treasury data on an annual basis. And this is not so surprising. For example, taxes may be recorded when income is taxable, recorded when paid to Treasury agents, or recorded when Treasury accounting officials are notified of the payment. In addition, taxes may be calculated with or without refunds. However, if we generalize the data over the entire duration of the war, these problems are balanced, and the importance of the excess profit tax is clearly demonstrated. If we add up all the dollars without accounting for inflation, we can see that the most important tax source in World War I was the excess profits tax, which accounted for about 30 percent of total tax revenue, even more than the personal income tax. If we adjust for inflation and exclude pre-war revenues and count only the taxes earmarked to finance additional war expenditures, the excess profits tax's share of total tax revenues reaches 40 percent, far higher than any other form of taxation.

Conclusion

The economic impact of World War I on the United States was profound, leading to significant shifts in industrial production, financial policies, and government interventions. The war demonstrated the importance of economic mobilization in modern warfare, influencing future economic and military strategies. While taxation and war bonds helped finance the war, the long-term fiscal consequences shaped U.S. economic policies in the post-war era. The study concludes that although economic motivations played a role in U.S. entry into the war, broader geopolitical and strategic considerations ultimately determined its involvement.

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