# E Appendix E:

The purpose of this appendix is to expand the discussion of possible historical endogeneity in the main paper. This section looks at the long term potential endogeneity issues. The main paper highlights potential endogeneity issues between the Great Contraction and ensuing depression and WWII. The greatest endogeneity concerns steaming from possible fiscal and monetary phenomenon, starting around 1937 likely to be correlated with WWII spending starting in 1940.

However, there may also be longer term endogeneity issues. To this end, I run the basic, backwards looking fixed effects specification used to test for historical endogeneity in the main paper, but include the whole period from 1900-1945.

Figure 1 shows the results of this endogeneity test for total assets, demand deposits, total investments , government investments and total reserves, the main variables of interest in the main text[1] What emerges is a picture that is somewhat similar to the "short run" endogeneity test in the main text. The main text discusses in some length the idea that the changes in bank balance sheets at the begin on the thirties that are correlated with WWII spending is likely do to the fact that The collapse of output from 1930-1933 and WWII contract spending are correlated shocks to manufacturing. When the pre-war period is expanded out to 1900 it is quite clear that the First World War also, perhaps unsurprisingly, emerges as a correlated shock. It is perhaps more obvious why WWI and WWII would emerge as correlated shocks to the banking system. What is interesting about these results is that lending seems to be the driving force of overall asset decline during WWI, rather than paper assets as in WWII. One hopes that a similar state level panel of WWI contract spending may emerge one day so that this could be explored further.

For completeness it should be pointed out that total reserves and Treasury holdings both show some endogeneity, similar to that discussed in the maine text. As well, there is some pre-WWI endogeneity in total assets. However, this is small (roughly 2 cents) and does not persist after 1930. It is hard to interpret the relationship between assets in the 1910s and war spending in the 1940s given the major monetary regime changes that took place over that 30 year span.

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[1]The Korean War spending, manufacturing nad income controls have been dropped from this analysis for lack of data, so the reader is advised that there is some obvious omitted variable bias for the post 1940 periods
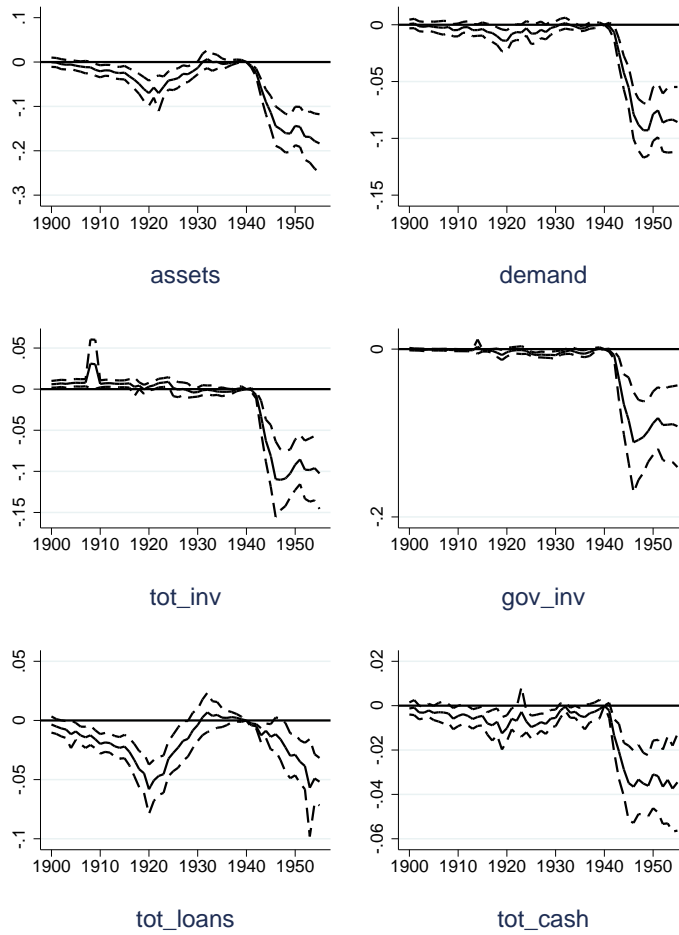
Graphs show the estimated dollar response to $1 of war spending per capita.
Dashed lines are 95% confidence intervals.

Figure 1: Long Run Endeognity Test for Selected Componets of Bank Balance Sheets