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THE DANGERS OF PRICE CONTROLS

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The first thing to be said about wage and price fixing is that it is harmful at any time and under any conditions. It is a giant step toward a dictated, regimented, and authoritarian economy. It makes impossible arrangements that both sides are willing to agree to. It sets aside contracts that have already been made in good faith. If an employer wishes to give a man a raise in pay, and the man deserves it, he is nonetheless forbidden to do it under the new regulations. This is a grave abridgment of individual liberty.

Price fixing and wage fixing do harm even if there is no inflation. In a free economy prices are constantly changing. They are changing to reflect changes in supply and demand, in costs, and in a hundred other conditions. Some prices are going up, other prices are going down. If an effort is made to freeze these prices and wages and costs exactly where they are, it immediately disturbs the relationship of prices and comparative profit margins which decides what things will be made and what quantities they will be made in. It upsets the process by which the free market decides how thousands of different commodities and services are to be made in the proportions in which people want them.

Of course, if we are in a period of inflation, price fixing does immensely more harm. And it is never a cure for inflation. What causes inflation is an increase in the supply of money and credit. This is always brought on, directly or indirectly, by governmental policy — especially by governmental deficits which lead to an increase in the supply of money and credit.

In the last 42 years there has been a deficit in the federal budget for 33 years. In 1971 — that is, the fiscal year that ended June 30 of this year, there was a deficit of $23 billion. This was second only to a deficit of $25 billion in 1968; apart from that, it was the highest peace-time deficit in our history. We are facing in the present fiscal year an estimated deficit of $28 billion.

Now these deficits over the years have been financed by the issuance of paper money. At the end of 1939 demand bank deposits and currency in the hands of the public totalled $36 billion; today that figure is $227 billion. That is an increase of 530 per cent, in other words, a six-fold expansion of money. And this is the sole cause of the rise in prices over that same period of 195 per cent. American consumer prices have tripled in the last 32 years. What we have today is price fixing with monetary inflation. This must lead to shortages and to a profit squeeze. And it will tend to distort and to reduce production.

Sometimes people talk as if it would be possible to have universal price fixing. That is to say, the government would fix every wage, every price, every cost. This is absolutely impossible. While nobody knows how many separate prices and separate wages there are, there are good reasons for thinking that there cannot be fewer than about 10 million.

If you try to fix 10 million prices, what you are trying to fix is something in the order of 50 <u>trillion</u> cross-relationships of prices. This is something that no government is capable of determining — not to speak of policing. If they could police it, they would have to impose rationing and allocation of individual goods in order to keep prices where they were if they kept increasing the money supply. And even then, the whole project would be impossible for the simple

im•pri•mis (ĭm-prī́ mĭs) adv. In the first place. Middle English, from Latin <u>in</u> <u>primis</u>, among the first (things). . .

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reason that the government cannot control prices of imports. These are out of their control. And they would not know how to pass these increases in import prices through the economy without creating disruptions and distortions.

Now on August 15, 1971 the President did announce what purported to be a complete freeze of both wages and prices. But this freeze was purely rhetorical. There was not even an attempt to police it. In fact, nobody can police the actions and decisions of millions of employers and sellers and of 80 million workers.

It is not difficult to fix prices, or to pretend to fix prices, for a period of 90 days. But the trouble with fixing prices for a period of only 90 days is that if you continue to increase the money supply — and if all the other factors are what they were — then at the end of that period prices will jump to where they would have been anyway. So when the administration recognized this, in order to avoid the criticism that the whole 90 days price fixing was useless and pointless it had to extend the wage-and-price fixing. So we are now in Phase Two.

Nobody knows when Phase Two will end. And for a very good reason. When we get toward the end, there will again be fears: "As soon as we stop this price fixing, prices will jump, won't they?" So there's a self-perpetuating gimmick in so-called temporary price fixing. Once you hold prices down by edict, you have to keep holding them down in order to prove that you are doing some good.

If, on the other hand, the money supply were kept down, prices would not tend to rise and the price fixing would not be at all necessary. I'd like to say here, of course, that I'm simplifying somewhat in talking about the effects of changes in the money supply. There is usually a lag between increases in the supply of money and increases in prices. This may range from 6 months to a year. But everything depends on the special conditions that exist. Just let's keep in mind that it's changes in the money supply that determine changes in the level of prices.

Phase One ostensibly froze every price and wage just where it was. Phase Two is supposed to be looser and more flexible. It is supposed to allow for and prevent hardships to individual producers. Therefore, it turned things over to a board, or a group of boards, so they could use their discretion. But discretion in the hands of bureaucrats is a very dangerous thing. The members of these three boards for price fixing and wage fixing are not even officials of the American government. They are ostensibly private citizens. Now to have private citizens telling everybody what they can charge and what they can pay raises legal and constitutional questions of a very grave nature.

The administration has set up three separate boards. One is a Cost of Living Council, which is supposed to preside over the whole arrangement. Then there is a Pay Board which is supposed to take care of wages and salaries. And a Price Commission that is supposed to fix prices. What is the relationship between these three bodies? It's been purposely kept quite vague.

The Price Commission is composed ostensibly only of members of the public. The Cost of Living Council is composed ostensibly only of members of the public. The Pay Board is a tripartite group of fifteen persons, five supposedly representing labor, five employers, and five public. Now union labor constitutes only one quarter of the labor in this country, yet every one of the five members of the Pay Board is a union leader. This is a little lopsided. And then Mr. Meany made it quite clear early on that the unions would feel free to pay no attention to any ruling that wasn't in their favor. That isn't going to help.

Then the Pay Board can fix wages and the Price Commission can fix prices. But when the Pay Board fixes wages, it pays no attention to prices because they aren't within its jurisdiction. Prices are in the jurisdiction of the Price Commission. But costs have already been set by the Pay Board. So if the Price Commission doesn't follow along submissively and endorse all the decisions of the Pay Board by allowing these increased costs to pass through, or if it tries not to let them pass through, then it is going to create great disruptions in the economy.

As a result of having two bodies governing wages and prices respectively, we have two formulas: one formula governing wages and another formula governing prices. Wages are to be allowed to go up 5.5 per cent, but prices are to be allowed to go up only 2.5 per cent.

Let's look at this 2.5 per cent for a moment. It's a completely arbitrary figure taken out of the air. If we want to control prices, why not just control prices — fix them just where they are? What is the point of allowing an increase of 2.5 per cent? If we fear it would do harm not to allow price increases of 2.5 per cent, why doesn't it do harm to allow increases of only 2.5 per cent?

But why is the wage increase figure set at three percentage points above the price figure? Why is the allowable wage rise set at 5.5 per cent, and the allowable price rise at only 2.5 per cent?

The rationale for this has grown up over the years. The Bureau of Labor Statistics has long been making estimates of the "man-hour productivity" in the country. These estimates have shown an average increase of about 3.2 per cent a year over the period since World War II. The Bureau now estimates that for the 1970's this increase in productivity will

average 3 per cent a year.

This man-hour productivity, or production per man-hour, is not only a dubious average, but an average of an average. For example, it's an average of the average of man-hour-productivity rises over a series of years. But this includes one year in which the rise was calculated to average 4.6 per cent and another year in which it didn't rise at all. Then again, this figure lumps together thirty-two different industries — or rather it lumps all industries together; but if you break this down into thirty-two industries, you find a very wide disparity from industry to industry. For example, the estimated increase in man-hour-productivity in footwear has averaged only 1 per cent a year; but in petroleum pipelines, it has averaged 10 per cent a year. Of course, if you break this figure down further to showdifferences between individual firms, the discrepancy is far wider still.

And whatever validity the overall 3.2 per cent man-hour-productivity figure may once have had, it doesn't exist any longer. From 1965 to 1970, the Bureau of Labor Statistics' own figures show that the average increase in man hour productivity was only 1.8 per cent. In 1970, it was less than 1 per cent. And a recent study published by the Federal Reserve Bank of St. Louis points out that the increase from 1965 to 1970 was only seven-tenths of 1 per cent for all private business. The author of that made his calculations on a slightly different basis than does the Bureau of Labor Statistics. But this shows how tricky and undependable all these statistics are. Yet this 3 per cent "annual increase" figure has been kept. It is constantly repeated in newspaper editorials. It has become a sanctified figure in Washinton. It is an article of faith that labor productivity goes up 3 per cent a year regardless of what happens.

There are two main myths about this so-called man-hour-productivity. One is that it is labor productivity; the other is that it occurs automatically. We would get a much better idea of what we were talking about, if instead of speaking of man-hour-productivity we talked of man-machine-hour-productivity or labor-capital-productivity. This increase in productivity doesn't occur because workers work 3 per cent harder every year or 3 per cent better every year. It increases only because capital investment is increasing. It is this capital investment that increases the productivity. If a man, for example, can mow a half an acre of lawn in an hour with a hand mower, and his employer then gets him a power mower and he can now mow an acre in an hour; and then if his employer gets him a still bigger power mower and he can now mow two acres in an hour, then productivity has gone up four-fold. Suppose he then came around and asked for a four-fold increase in pay per hour? Well, first of all, the employer who bought the machine, if he had known in advance that his employee was going to demand this, wouldn't have bought the machine in the first place.

This is what is overlooked. New investment goes on in industry, increasing man-hour-productivity, first only if there has been enough profit in the past to yield the added capital to make that investment, and second, only if the outlook for future profits, for future return on new investment, remains sufficiently attractive. But if labor gets the whole gain from every increase in productivity, and nothing is left for capital, then investment will stop, and productivity increases will stop. This is a point which seems to have been overlooked.

But I don't know why I should be spending so much time examining these formulas for an allowable 5.5 per cent increase per year for labor and 2.5 per cent for prices, because no sooner were these formulas framed then they were violated. The Pay Board announced this 5.5 per cent figure on November 8. On November 19, only 11 days later, it ratified a wage increase in the coal industry that came to 16.8 per cent in the first year. This is more than triple what it said it would allow. Then on December 9, it awarded the railway signal men a 46 per cent increase over forty two months. That's at an annual rate of 13 per cent over a period of 3.5 years. Such flagrant examples are numerous.

Now let's turn to prices. American Motors was granted a 2.5 per cent increase in its prices. General Motors was granted a 2.5 per cent increase in prices. Then Ford Motors was granted a 2.9 per cent increase in prices. And then Chrysler was granted a 4.5 per cent increase in prices. What has become of equality of treatment for all? And what is achieved by this kind of hocus-pocus? After Chrysler was permitted a 4.5 per cent increase, it turned around and said, "We are only going to increase prices 3 per cent." Why? Because competition compelled them to limit their price increase to that figure.

Of course; it's competition that holds down prices — not government ukase. And it's competition that we should continue to depend on. Competition exists in this country for at least nine-tenths of the commodities and services that we daily use. And that competition is no keener anywhere than in the automobile industry. Rival cars will sell within a dollar of each other in the same district. The automobile companies produce altogether about 380 different models — the American automobile companies alone, not counting foreign imports. That sounds like a big figure, but if you stop to think that there are about ten different types of Chevrolets, ten different types of Pontiacs, and so on, even within the General Motors Company, you can see how that gets to a very high total. Each one of these companies has to price its cars low enough to meet the competition and to maximize its own sales. Nobody is compelled

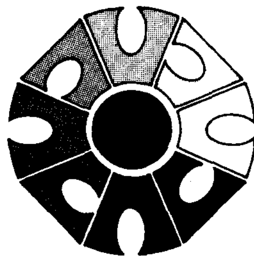
to buy one make of car rather than another. Nobody is even compelled to buy a new car rather than a second-hand car. Most of us can postpone the purchase of a new car indefinitely. But this is the kind of situation that business daily faces. And this is the kind of competition that constantly keeps down prices to a minimum in relation to the general economic situation.

What the government ought to be doing to get prices low is to free and encourage the producers — not to put them in a strait jacket. But price fixing does exactly the opposite. And it's doing exactly the opposite now. We've seen that the Pay Board gave the coal miners a 16.8 per cent increase for the first year; then when the first coal mine company asked for an increase in price, the Price Commission allowed it only a 4 per cent increase in price to meet that 16 per cent increase in wages. On the Commission's own estimate, this would at best allow the coal companies to pass through about 60 per cent of the cost of the increased wage. With this kind of whipsaw there will be a terrific squeeze on profits. The result will be to discourage investment and therefore to increase unemployment. That certainly wasn't the original object of the price control act.

Price — and wage — fixing is always harmful. There is no right way of doing it. There is no right way of doing a wrong thing. There is no fair way doing something that oughtn't be done at all. We can't even define a fair price or a fair profit or a fair wage apart from the market, apart from the state of supply and demand. Instead of talking of "fair" prices, "fair" profits, and "fair" wages, we ought to be talking about functional wages, functional prices, and functional profits. Prices have work to do. What they do in effect is to give the necessary signals to production. They direct production into the things that are most wanted socially, to provide a balance among the thousands of different commodities and services in the proportions that the consumers want them.

Price fixing destroys the signals on which this ever-changing balance depends. It always does harm. And it is never a cure for inflation. Not only is price fixing never a cure for inflation, but in the long run it prolongs and increases inflation. Quack cures divert attention from real causes and real cures. The real cause of the price rises of the inflation that we have had over the last 30 years, and that has intensified in recent years, has been the increase in the supply of money resulting from the enormous deficits that we have been piling up steadily. Yet today, when the attention of Congress, of the Administration, and of the press, is focused on whether price fixing is working well or not, we are building up the greatest deficit in our peace-time history. We are also building up an increasing money supply and intensifying the problem. False remedies drive out real remedies.

I'd like to say a final word about the morality of all this. I prefer not to make my own judgment but to quote one of the price controllers themselves. This was said by Mr. Earl D. Rhode, who is executive secretary of the Cost of Living Council. "The citizen's role in this program is to rat on his neighbor if his neighbor violated the controls." I leave the moral judgment of that to each of you.



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