Should we fight inflation with wage and price controls?

According to a recent survey, most Americans believe that inflation is our number one problem and President Carter "isn't doing enough" to combat it.[1] The only proven way to solve our inflation problem, fiscal and monetary restraint, takes time to work. But with inflation accelerating—now back up to double-digit rates—pressure is mounting on the Administration to come up with a quick fix. And that likely means some form of incomes policy: a government policy which directly limits wage and price increases. Should we try to fight inflation this way?

Old Controls?

We have tried it before. In the early 1970s, President Nixon froze wages and prices and then imposed a program of mandatory guidelines on wage and price increases. The first article in this issue, "A New Investigation of the Impact of Wage and Price Controls," (p. 2) evaluates that program using a new technique of economic forecasting that makes this study a considerable improvement over others. The study essentially finds that these wage and price controls worked only temporarily against inflation, and they depressed output. Once controls were removed, prices rose faster than they would have otherwise, and to a higher level.

Still, the government has moved toward an incomes policy this year. In his first State of the Union address, President Carter proposed a system of "voluntary constraints" on wage and price hikes in 1978. But it seemed likely from the outset that emphasis would eventually switch from the "voluntary" to the "constraints" side of this program. That is how AFL-CIO President George Meany saw it when he termed President Carter's proposal "wishboning" and then voiced the concern of many that "it would be 'a step down the road' to outright wage and price controls."[2]

That concern was not unwarranted. President Carter recently appointed Robert Strauss as his special counselor on inflation and assigned him the task of jawboning down wage and price increases. He will launch public attacks on companies or unions which violate the spirit of the government's "voluntary" anti-inflation program. He has stated, "We will certainly be speaking out where we think there has been poor citizenship." And Barry Bosworth, director of the Council on Wage and Price Stability, issued a public reminder that his agency has the power to subpoena cost information from business.[3] This is voluntary?

New Controls?

If the government takes the next step of actually implementing an explicit wage and price constraint policy, there is a strong chance it will be the newly proposed policy evaluated in our second article, "TIP: The Wrong Way to Fight Inflation" (p. 9). "TIP" is a "Tax-based Incomes Policy" which basically would tax wage increases in an attempt to lower both wage and price inflation. As the title indicates, however, this article concludes that TIP wouldn't work that way. In fact, it says, TIP would raise prices, not lower them. And TIP would have all the distortionary and administrative side effects of more traditional wage and price controls.

So the answer appears to be "no." We should not fight inflation with either old or new types of wage and price controls—because they wouldn't work. Our only effective weapon against inflation is still sound fiscal and monetary policies.

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[1]Richard J. Levine, "Carter Inflation Battle Still Faces Problems Despite Tax-Cut Delay," *Wall Street Journal*, May 15, 1978, p. 1.

[2]Michael Ruby, Rich Thomas, and Pamela Ellis Simons, "Carter and Your Money," *Newsweek*, January 30, 1978, p. 23.

[3]Levine, p. 18.