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The Bases for the Wage and Price Goals

Most economic observers are aware that Administration planners announced in November certain goals for their attempts to control increases in pay and prices in the United States. The planners provided little explanation or justification for the goals selected. Nevertheless, these goals apparently have been widely and uncritically accepted, as perhaps befits the subjects of an economic autocracy. In this article we shall describe the apparent bases for these goals and discuss their implications.

The Pay Board issued on November 8 a list of policies on pay increases that included the following paragraph: "On and after November 14, 1971, permissible annual aggregate increases would be those normally considered supportable by productivity improvement and cost of living trends. Initially, the general pay standard is established at 5.5 per cent. The appropriateness of this figure will be reviewed periodically by the board, taking into account such factors as the long-term productivity trend of 3 per cent, cost of living trends, and the objective of reducing inflation."

The Price Commission issued on November 12 the text of its first regulations on price increases that began as follows: "It is the purpose of the regulations hereby adopted to provide guidance and procedures for the implementation of Price Commission policies designed to achieve a goal of holding average price increases across the economy to a rate of no more than 2½ percent a year. It is expected that all persons will voluntarily comply with the provisions contained in these regulations and all orders and other guidance issued hereunder." The Price Commission did not specify how "average price increases across the economy" would be measured.

The goal of the Pay Board to restrict pay increases to an average annual rate of 5.5 percent apparently was based on several assumptions. The long-term rate of increase in productivity (output per man-hour) of U.S. processing activity has been estimated to be 3 percent annually. Members of the Pay Board evidently have assumed that this estimate warrants part of the increase in everyone's pay that they have envisioned. This assumption is questionable for a number of reasons.

Changes in productivity, particularly of providers of services, cannot be measured with great accuracy. Average productivity of those who provide services apparently has changed slowly, and that of people in different kinds of processing activity has changed at greatly differing rates. Even in similar activities, productivity of some individuals has increased while that of others has not. Basing increases in pay for all workers on a single rate of increase in productivity thus will overcompensate those whose productivity increases less, and will undercompensate those whose productivity increases more, than that rate. Moreover, changes in productivity in some activities have varied substantially from one stage of the business cycle to another. Basing all increases in pay on an average increase in productivity thus will be inappropriate much of the time.

Increases in productivity often have resulted, not from an increase in the efficiency of the worker's efforts, but from the acquisition of more effective processing equipment. Such increases warrant increased compensation for those who provided the equipment, such as stockholders, not for workers who operate it. Increasing the pay of workers in such circumstances redistributes income to them from the providers of the equipment.

Productivity sometimes has increased while the volume of things processed has decreased. For example, productivity in the private economy of the United States was estimated to have increased slightly from 1969 to 1970, but the output of things processed during 1970 was less than that during 1969. An increase in aggregate pay, together with an accompanying increase in purchasing media, clearly would be inappropriate when the volume of things processed was decreasing. The estimated long-term rate of increase in productivity of 3 percent thus is not an adequate basis for determining the appropriate rate of increase in the pay of each of the Nation's 80 million workers. Such an increase when output is decreasing would foster rising prices.

Members of the Pay Board evidently have assumed that the cost of living will increase at an annual rate of 2.5 percent. This apparently was based on the further assumption that the Price Commission would achieve its goal of "holding average price increases across the economy" to no more than that rate. Members of the Pay Board apparently have concluded that, in addition to the increase of 3 percent, everyone's pay also should increase by 2.5 percent annually to offset the expected increase in the cost of living.

Announcement of the Price Commission's goal of a 2.5-percent annual rate of increase in prices has raised some questions that the central planners have not answered publicly. What was the basis for choosing that rate? Inasmuch as the planners had successfully assumed dictatorial control over all wages and prices in the Nation, why did they not seek to stabilize prices while they were about it?

We suspect that the answers to these questions can be found in the basic premise of the Administration's economic policy: that inflating (creating excess purchasing media) is essential for economic prosperity. Like their predecessors, the incumbent central planners apparently believe that inflating is good economic as well as political policy, as long as the resulting increase in prices does not get out of hand.

The planners apparently hope to convince the public that an increase in prices of 2.5 percent annually is of little significance, especially when their pay increases at

more than twice that rate. Naturally, the planners did not point out that such an "insignificant" increase in prices would reduce the purchasing power of fixed incomes and of all savings by nearly one-quarter every 10 years. The unanswered question is, How long will the sheep stand still for such shearing?

PRESIDENT NIXON CONFIRMS THAT THE DOLLAR WILL BE DEVALUED

The international monetary crisis evidently was the principal subject of discussion at meetings of President Nixon and President Pompidou of France in the Azores last week.

A joint statement issued after the meetings revealed that these men "reached a broad area of agreement on measures necessary to achieve a settlement at the earliest possible date of the immediate problems of the international monetary system. In cooperation with other nations concerned, they agreed to work toward a prompt realignment of exchange rates through a devaluation of the dollar and revaluation of some other currencies. This realignment could, in their view, under present circumstances, be accompanied by broader permissible margins of fluctuation around the newly established exchange rates."

President Nixon thus confirmed what had been implied after the recent meeting in Rome of financial officials of the Group of Ten nations: that the gold content of the dollar would be reduced. However, questions about some crucial aspects of the situation remain unanswered at this writing. To what extent will the dollar be devalued? Will U.S. authorities restore convertibility of dollar claims into gold at the unspecified new rate by foreign official holders? If not, what will these holders do with the more than 40 billion of paper dollar claims that they have accumulated? Until answers to questions such as these are provided, the significance of the impending devaluation of the dollar cannot adequately be evaluated.

STATISTICAL INDICATORS

Among the primary leading indicators of business-cycle changes, a decrease during October in the change in the book value of manufacturing and trade inventories did not clarify the cyclical status of that series, which remained indeterminate. The net change in consumer installment debt decreased during October after four consecutive monthly increases, but this series still is appraised as expanding cyclically. Thus, the percentage of leaders apparently expanding cyclically remained at 33.

Among the primary roughly coincident indicators, manufacturing and trade sales decreased during October after increasing during both August and September. However, the October decrease did not warrant a change in the apparent status of this series, which is appraised as expanding cyclically. New data, based on revisions of sampling procedures, indicated that retail sales decreased during October, rather than increased as previously reported. However, retail sales increased during November, and this series apparently continued to expand cyclically then. Industrial production increased during November, but the cyclical status of this series remains indeterminate. Thus, the percentage of primary roughly coincident indicators apparently expanding cyclically was unchanged at 71.

During October, manufacturing and trade inventories increased, which indicated that the series still was expanding cyclically then. The percentage of primary laggers apparently expanding cyclically was unchanged at 67.

Apparent cyclical expansion of only 33 percent of the primary leading indicators is not encouraging for the future trend of general business activity.

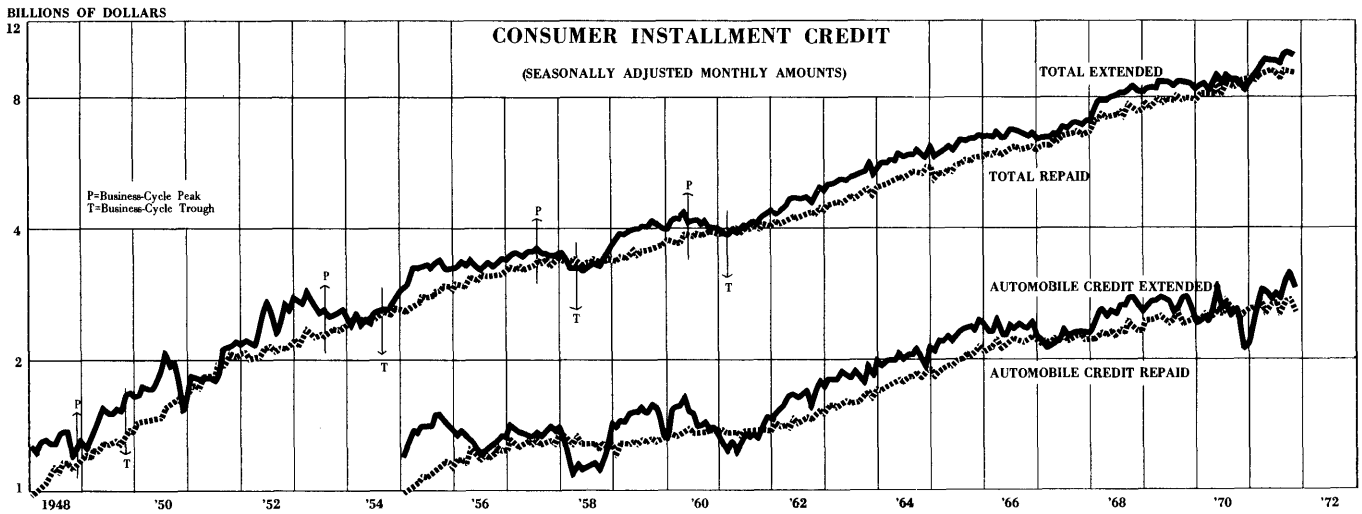
DEMAND

CONSUMER INSTALLMENT DEBT

Note: Data other than the total amount outstanding are seasonally adjusted.

The total amount of consumer installment debt outstanding at the end of October was $105.8 billion, which was 5.8 percent more than the year-earlier amount. During October the net change (extensions less repayments) in the seasonally adjusted amount of consumer installment debt outstanding was an increase of $924 million, which was almost as large as the record increase of $999 million during September. This primary leading indicator of business-cycle changes has expanded rapidly from a cyclical trough reached in November 1970.

The total amount of new consumer installment credit extended during October was 1.3 percent less than that during September but nearly 17 percent more than that during October a year earlier. Repayments of consumer installment debt decreased



0.6 percent during October to an amount 5.2 percent more than that a year earlier.

Among the major categories of consumer installment credit, extensions for the purchase of automobiles decreased a substantial 5.1 percent during October to an amount 27.2 percent more than that a year earlier. Such extensions decreased about as much during October as they had increased during September, but they continued to be relatively large. Automobile installment debt repayments during October were 3.7 percent less than those during September but 3.1 percent more than those a year earlier. The net increase of $358 million in automobile installment debt during October was smaller than the net increase of $415 million during September but still was relatively large.

Installment credit extended during October for the purchase of other consumer goods (primarily general merchandise, apparel, appliances, and furniture) was 0.3 percent more than such extensions during September and 11.6 percent more than those during October 1970. The October increase offset a 0.3-percent decrease during September; thus the October amount of extensions for the purchase of other consumer goods was equal to that during August. Repayments were 1.6 percent more than those during September and 5.9 percent more than those during October 1970.

Personal installment loans extended during October were 0.6 percent more than those during September and were 13.6 percent more than those a year earlier. October repayments of such loans increased 0.3 percent to an amount 5.5 percent more than that during the corresponding month a year earlier. The net increase in personal loans during October was $286 million, which was larger than the September increase of $266 million but smaller than the August increase of $291 million.

Installment credit extended for home repair and modernization increased 0.9 percent during October and was 25.8 percent more than such extensions a year earlier. Repayments were 1.0 percent less and 10.1 percent more, respectively, than those a month and a year earlier.

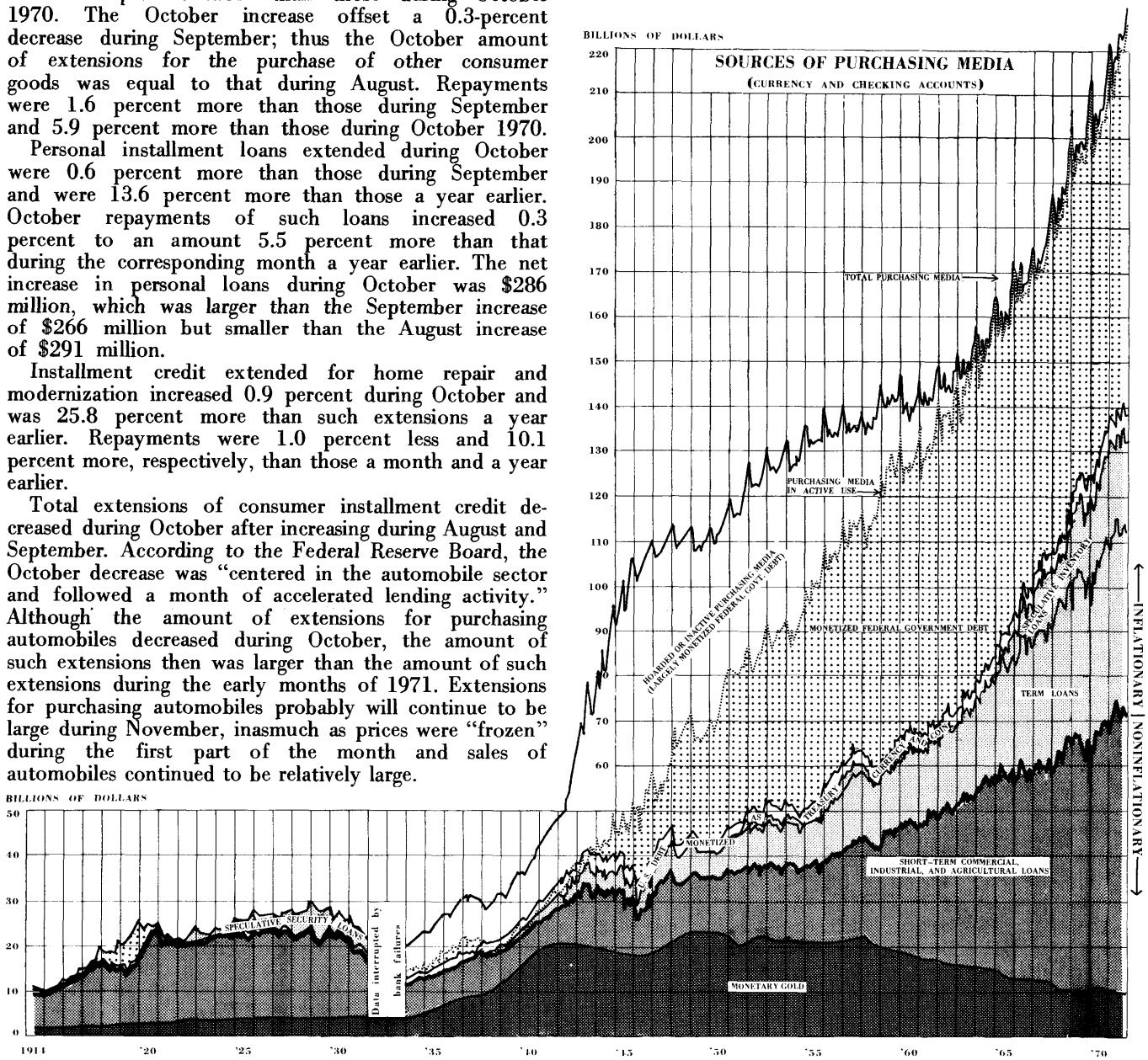
Total extensions of consumer installment credit decreased during October after increasing during August and September. According to the Federal Reserve Board, the October decrease was "centered in the automobile sector and followed a month of accelerated lending activity." Although the amount of extensions for purchasing automobiles decreased during October, the amount of such extensions then was larger than the amount of such extensions during the early months of 1971. Extensions for purchasing automobiles probably will continue to be large during November, inasmuch as prices were "frozen" during the first part of the month and sales of automobiles continued to be relatively large.

Extensions of consumer installment credit for purchasing consumer goods other than automobiles have continued at near-record amounts during recent months. The trend of this series appears to be upward, which suggests that consumers have been willing to incur additional debt for buying other things, as well as for buying automobiles.

PURCHASING MEDIA

Total purchasing media increased from the amount late in October by $3.1 billion to $228.6 billion late in November. This total was 6.9 percent more than that a year earlier. Subtraction of an estimated $2.8 billion of inactive purchasing media indicates that purchasing media in use late in November totaled $225.8 billion.*

*Although inactive purchasing media include both hoarded currency and idle checking accounts, most of them currently are in the form of hoarded silver coins. Such purchasing media are those in excess of the amount ordinarily in active use in effecting business transactions. Because this portion of total purchasing media is not used for buying things in the markets, it is subtracted from the total.



SOURCES OF PURCHASING MEDIA
Last reporting week of the month
(Billions of dollars)

	1970	1971	
	Nov.	Oct.	Nov.
F.R. Gold Certificate Account	10.8	9.9	9.9
Short-term Commercial, Industrial, and Agricultural loans	57.6	61.5	61.2
Noninflationary Purchasing Media	*68.4*	*71.4*	*71.1*
Term Loans	40.7	41.0	41.1
Speculative Inventory Loans	20.5	20.2	20.9
Treasury Currency and Coin	5.5	5.6	5.6
Monetized Federal Government Debt	78.8	87.3	89.9
Inflationary Purchasing Media	*145.5*	*154.1*	*157.5*
TOTAL PURCHASING MEDIA	213.9	225.5	228.6
Inactive Purchasing Media	2.7	2.8	2.8
Total Purchasing Media in Use	*211.2*	*222.7*	*225.8*

Note: Because of rounding, added components may not equal totals.

Noninflationary purchasing media decreased $0.3 billion during November to $71.1 billion, which was $2.7 billion more than the amount a year earlier. Purchasing media derived from monetary gold and reflected in the Federal Reserve gold certificate account remained unchanged during November at $9.9 billion, which was $0.9 billion less than that a year earlier. Purchasing media derived from short-term commercial, industrial, and agricultural loans decreased $0.3 billion during November to $61.2 billion, which amount was 6.2 percent more than that late in November 1970.

Inflationary purchasing media increased $3.4 billion during November to $157.5 billion, which was 8.2 percent more than the amount a year earlier. Purchasing media created by the commercial banks for making term loans of more than a year's duration are inflationary because they were used for buying things such as plant and equipment that the borrowers did not offer in the markets. The amount of such purchasing media was relatively unchanged during November at $41.1 billion, which was 1 percent more than that a year earlier. Purchasing media created by these banks for making speculative inventory loans were used by borrowers for buying stocks of materials and other things that they did not offer in the markets; such purchasing media also are inflationary. The amount of such purchasing media increased $0.7 billion during November to $20.9 billion, which was nearly 2 percent more than the amount a year earlier.

The relatively stable amount of inflationary purchasing media derived from U.S. debt monetized as Treasury currency and coin was unchanged at $5.6 billion during November, compared with $5.5 billion a year earlier. Purchasing media created by the commercial and Federal Reserve banks for purchasing securities issued by the Federal Government were used by the Government and other sellers of the securities for buying things that they did not offer in the markets. Such monetized Federal Government debt accounts for the largest portion of inflationary purchasing media. This portion increased $2.6 billion during November to $89.9 billion, which was 14.1 percent more than that a year earlier.

The gold stock of the U.S. Treasury was $10.1 billion at the end of November, which was $1 billion less than that a year earlier. Gross foreign short-term claims against the Treasury gold stock (including dollar claims held by the International Monetary Fund) estimated at $66.5 billion at the end of September were partly offset by short-term dollar claims against foreigners at that time of $11.2 billion. If these totals were unchanged during October and November, net foreign short-term claims would exceed the Treasury gold stock by $45.1 billion. This contrasts with $27.1 billion a year earlier.

The increase in total purchasing media during November was somewhat less than usual for the month. After seasonal adjustment by the Federal Reserve Board, the total late in November was slightly less than that a month earlier.

Total purchasing media increased less than seasonally during most recent months, and the seasonally adjusted total has changed little since July. The recent relatively level trend of the adjusted total has been in marked contrast with an increase at the annual rate of about 10 percent during the first 7 months of this year. Neither the rapid increase earlier this year nor the stability that followed was intended by Federal Reserve authorities. These marked changes in the trend indicate that the authorities have little control over the "money supply" or total of purchasing media in the short-run.

In view of the continuing highly expansionary monetary policy, substantial increases in the seasonally adjusted total of purchasing media during the next few months would not be surprising.

RETAIL SALES

Estimates of retail sales for the most recent week and 4 weeks compare with such sales during the corresponding periods a year earlier as follows:

Period	*Percent change*
Week ended December 11	+ 9
Four weeks ended December 11	+ 11

SUPPLY

INDUSTRIAL PRODUCTION

Production of steel, automobiles, electric power, and lumber (1) in the 1- and 4-week periods ended on the indicated dates in the current year and (2) in the corresponding periods of earlier years was as follows:

	1929	1932	1957	1961	1970	1971
Steel						
Ingots - million tons						
1 week: December 11	0.88	0.23	1.77	2.16	2.42	1.96
4 weeks: December 11	3.74	1.03	7.39	8.30	9.45	7.63
Automobiles						
Vehicles - thousands						
1 week: December 11	24	18	144	162	156	183p
4 weeks: December 11	95	45	549	605	471	693p
Electric Power						
Kilowatt-hours - billions						
1 week: December 11	1.8	1.5	12.6	16.1	30.0	31.8
4 weeks: December 11	7.2	6.0	48.6	63.0	116.1	123.7
Percent change from 4 weeks a year earlier: + 6.6						
Lumber						
Board feet - billions						
1 week: December 4	0.74	0.20	0.54	0.50	0.56	0.79
4 weeks: December 4	2.84	0.81	2.27	2.42	1.99	2.89

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PRICES

COMMODITY PRICES

	1970	1971	
Index	*Dec. 6*	*Nov. 29*	*Dec. 6*
Spot-market, 22 commodities*	282	276	n.a.
Commodity-futures	304	296	299
Steel-scrap	$34.83	$29.67	$29.67

*For the preceding Tuesday.

Note: The indexes are, respectively, those of the U.S. Bureau of Labor Statistics, Dow-Jones, and *Iron Age*. The spot-market and futures indexes are converted so that their August 1939 daily averages equal 100. The steel-scrap index is a composite price for No. 1 heavy melting scrap.