FOREWORD

On November 28, 1978, the Center for the Study of American Business at Washington University and the Federal Reserve Bank of St. Louis sponsored a conference on "Alternative Policies to Combat Inflation." Designed to examine the full range of public policy approaches to fighting inflation, the conference featured Karl Brunner of the University of Rochester, Beryl Sprinkel of the Harris Trust and Savings Bank, Sidney Weintraub of the University of Pennsylvania and Robert Nathan of Robert R. Nathan Associates, Inc. Over 65 guests -- university, business and Federal Reserve economists -- participated in this third annual jointly sponsored conference.

Additional short presentations were given by Paul Craig Roberts of the Wall Street Journal and Murray Weidenbaum of the Center for the Study of American Business. Discussion papers were presented by Charles Webster of Washington University and Denis Karnosky of the Federal Reserve Bank of St. Louis.

All papers are included in this proceedings volume in their entirety. Summaries of the four major papers are included in this foreword and follow.

"The Commitment to Permanent Inflation"

Karl Brunner of the University of Rochester stated that the waves of inflation that have swept over the U.S. since 1965 have been answered each time, by design or accident, with substantially lowered monetary growth. Each time, however, political pressures or serious

misconceptions deeply embedded in the policy making procedures of the Federal Reserve System produced a reversal in policies. He contended that these reversals ended in every case the gradual decline of inflation and initiated a new surge of prices with a deeper commitment to permanent inflation.

Regarding the President's intentions of reducing the budget deficits, Brunner stated that the President's emphasis on government expenditures is probably highly appropriate with respect to a more productive use of our resources and a correspondingly higher real income. But he viewed it as a peculiarly ineffective and cumbersome approach to curtail inflation.

Brunner was skeptical of the "non-control guidelines" proposed by the President. Political processes exhibit apparently an inherent propensity to respond to inflationary waves with an array of specific political institutions recorded under a shifting set of names (controls, income policy, guidelines, etc.). This disposition, he noted, is particularly remarkable as no evidence would seriously support the contention that incomes policies ever contained inflation in the absence of proper controls over monetary growth. According to Brunner, the experience accumulated with controls from diverse historical conditions overwhelmingly establishes their ineffectiveness as anti-inflationary instruments.

Brunner also criticized the logic of those who advocate a policy of "permanent inflation." In his view, such a policy results in alternating waves of increased inflation and retardation of economic activity expressed by a decline in output and rising unemployment. "An

accommodating inflation policy may thus easily produce two or three recessions, combined with continued inflation, over a ten-year span," he stated.

Brunner disagreed with President Carter that the only alternatives to his anti-inflation program are recession or mandatory and sweeping controls. Brunner stated, "This line is either fraudulent or illusionary... There is indeed only one way to lower inflation and that is to lower monetary growth over a long time." He noted that this instrument of an effective anti-inflationary policy unfortunately induces a temporary recession. But a policy of permanent inflation supplemented with incantations and partially mandatory controls, i.e., guidelines, he maintained, yields the social costs associated with erratic inflation, sluggish output, and higher than normal unemployment. "The promise of permanent inflation at a negligible social cost is a dangerous illusion," Brunner concluded.

"Inflation -- Causes, Cures and Placebos"

Dr. Beryl Sprinkel, Executive Vice President and Economist at Harris Trust and Savings Bank, Chicago, Illinois stated that the solution to breaking the inflation-recession cycle with its ever-increasing peaks and valleys is conceptually simple: conduct our nation's financial affairs in a manner designed to increase total spending in line with the increase in total production. Throughout the post-World War II period, he pointed out, spending increases have persistently exceeded output increases and inflation has become a way of life. Dr. Sprinkel cited three causes of the current rapid rate of monetary growth: 1) the large and growing federal budget deficits (resulting in the national

debt rising from $31 billion in 1965 to $148 billion in 1975 to nearly $322 billion by fiscal 1978); 2) the bias of the political process toward commitment to short run growth; and 3) the attempt by the Federal Reserve to choose a federal funds target consistent with money growth targets (an attempt comparable to trying to shoot a running rabbit by lagging, not leading). Dr. Sprinkel further stated that if appropriate monetary-fiscal policies are pursued, controls are not needed, and that if policies are too expansive, controls will not work.

"TIP For Inflation: Why and How"

One of the foremost proponents of tax-based incomes policy, Dr. Sidney Weintraub of the University of Pennsylvania, presented his arguments for using the government's taxing authority in order to control inflation. Weintraub disagreed with Sprinkel regarding sole reliance on monetary and fiscal policy solutions to inflation, stating that a stable price level and minimal unemployment will elude us if traditional monetary policies or the less efficient fiscal policy are solely relied upon.

Stated in a nutshell, tax-based incomes policy (TIP) is designed to levy an extra corporate penalty income tax on firms that exceed a governmentally determined average rate for wage and salary increases. Labor would be allowed to reap some of the benefits of a superior gain in productivity via what Weintraub termed the TIP-CAP (corrected average productivity) plan. One-third of any productivity increase above the national norm could be paid to the worker in wage increases over and above the governmentally pegged wage rate increase.

Weintraub applauded President Carter for his "better late than never" commitment to subdue inflation, but stated that the program was too bureaucratic for his tastes. "Monitoring prices and costs smacks of price controls," he noted.

"Inflation: Imperfect Markets and Government Policies"

Robert Nathan, Chairman of the Board of Robert R. Nathan Associates, Inc., supported President Carter's inflation proposals "except for the degree of harshness of the monetary restraints." Nathan saw the tight money proposals as increasing the odds of a recession, but doing little to reduce inflation.

He contended that it was unfortunate that the response to the President's program from the press and the financial community focused exclusively on the guidelines for wages and prices. Believing that the guidelines could have a positive impact, Nathan also stated that, equally or more important were the policies and measures announced by the President concerning government spending, taxation, regulations, competition, productivity, and trade policies.

Nathan challenged those who pay "lip service" to free enterprise and competition but practice monopoly and restraints on competition. He concluded, "If we are going to win the war on inflation and preserve the great free enterprise system, we must take seriously the efforts needed to make the market economy function more effectively."

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