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PRESENT AND FUTURE PLANS FOR PRICE STABILIZATION

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Mr. Harold Leventhal, Chief Counsel for the Office of Price Stabilization, was born in New York City on 5 January 1915. He was graduated from Columbia University with the B.A. degree in 1934. He was elected to Phi Beta Kappa and received the Green Prize for scholarship. In 1936 he received the LL.B. degree from Columbia Law School. He served as editor-in-chief of the "Columbia Law Review." In 1936-37, he was law secretary to Supreme Court Justice Harlan F. Stone; 1937-38, with the Office of the Solicitor General; 1938, law secretary to U. S. Supreme Court Justice Stanley Reed; 1938-39, Solicitor General's Office under Robert Jackson; 1939-40, chief of litigations, Bituminous Coal Division, Department of the Interior; 1940-43, assistant general counsel, OPA; 1943-46, lieutenant commander U. S. Coast Guard Reserve; 1945-46, assigned to Justice Jackson's staff at the Nurnberg Trials; 1946, adviser to Price Decontrol Board; 1948, executive officer on Hoover Reorganization Commission. From 1946 to 1951 he was engaged in private practice as the senior partner in the law firm of Ginsburg and Leven in Washington. He withdrew from this service in January 1951 when he became Chief Counsel for the Office of Price Stabilization.

PRESENT AND FUTURE PLANS FOR PRICE STABILIZATION

2 May 1951

COLONEL BARNES: Our series of talks on the economic mobilization program continues this morning with a discussion of our present and future plans for price stabilization. For the talk this morning our speaker is Mr. Harold Leventhal, who is Chief Counsel for the Office of Price Stabilization.

Mr. Leventhal has held a number of important executive posts in the Federal Government. They are given in his biography. Therefore, this morning he ought to be in a position, if anyone should, of being able to tell us what plans are being devised to make everything cost less when everything costs more.

Mr. Leventhal, it is a great pleasure to present you to this audience.

MR. LEVENTHAL: General Vanaman and gentlemen: I think an appropriate story about any stabilization program is that which the grand old master in this field, Mr. Baruch, tells: "What is inflation like? It is like the fellow who jumps out of the window of a 50-story building. As he passes the twenty-second story, somebody calls out to him, 'How do you feel?' He says, 'So far so good.'"

In an inflationary situation, while it is still going on, people are rather happy about it. But, of course, the time of reckoning is bound to come. I said they are "rather" happy about it. They are not completely happy, because they have some uneasiness about the situation. We have had enough experience with price and wage increases in this country to know what is going to happen. Certainly the general public realizes that, while these prices and wages are still going up, a day of reckoning must take place sometime.

I think it is true that we have seen in the last year--at least since June of 1950--a situation of widespread uneasiness over the kind of troubles that will come about with price and wage increases and an inflationary situation, an uneasiness that makes the country in general, indeed, all segments of the country, more nearly ready for the kind of controls that they think are necessary to prevent inflation than they have ever been before.

It is interesting to note, as I did, that your college calender shows that you have been studying the problem of procurement and economic stabilization in the period between 20 November 1950 and 26 January 1951 which by happenstance is largely the base period of the general ceiling price freeze. Certainly, if there was ever a time to study the subject, when history was in the making, that was the time. It was the time, roughly, after the Chinese intervention abroad and the bidding for materials at home. The price increases that took place during November and December 1950, January 1951, and since then, have borne out very sharply the fundamental wisdom of Bernard Baruch's proposal that as of some time like 24 June 1950 or at least whenever a major crisis developed, there should be some kind of price and wage freeze.

I may add that I disagreed with Mr. Baruch on that proposal in World War II because I didn't think the situation called for it at that time, though it did in 1950. The country was already producing at top levels and already operating with a maximum of employment and a minimum of unemployment. In addition to those conditions of labor and its implications as to wage rates, there was obviously going to be thrown upon us this gigantic defense effort--I say "gigantic." Obviously, its actual scope was not known at that time and still is not known. Committees of the Defense Department are still engaged in determining what the proper scope of that effort is. It must be balanced against estimates of what the civilian economy can stand. But if the present estimate of 50 billion dollars a year holds up--and at the present time contracts are being let in excess of that--we obviously have a situation in which money will be pumped into the system in payment for these goods and services and where the amount of civilian production will decline, perhaps not so seriously as at first we thought it would decline, but enough so that we will have a fundamental imbalance brought about by a demand for goods and not enough goods available to meet the demand. Such a situation under uncontrolled conditions will mean price increases, leading in turn to wage increases and the familiar inflationary spiral.

The situation that has developed in 1950 reflects an interesting variation. The classical inflationary situation is that of an unbalanced government budget, where, as I say, a tremendous amount of money is being pumped into the economic system at a rate faster than it is being taken out by the Federal Government. But in the period from June 1950 to the close of the year you had an overbalanced budget. More money was being taken out by the Federal Government than was actually being pumped in. Nevertheless, you had a very fast increase of prices. There was an 8 percent increase in the cost of living index and a much higher percentage in the wholesale price index.

This sounds like a contradiction of ordinary theories, but, in fact, it is not. It is merely the result of the fact that there was an anticipation by businessmen of the shortages that they knew would occur. They knew that there would be an imbalance between demand and supply with the excess of money that was going to take place when the defense program really got rolling. Of course, the timing was important, because things were going to be tight. Some people jumped in a little too fast and too far with their purchases. But they were making what were reasonable business predictions about what was going to take place when the defense program got rolling.

The situation in 1950 also saw a tremendous increase in the volume of bank credits. Businessmen were being loaned money by their banks with which they could both finance expansions and acquire large inventories of goods. So, even though there was not any large amount of borrowed money being pumped in by the Federal Government, the banks by increasing the amount of dollars available for spending, produced exactly the same effect on the market and on prices.

But let us leave the mechanics of the way in which price pressures build up, with the excess of demand over supply, and consider what the fundamental purposes of the economic stabilization program are. I will leave out of consideration over-all defense mobilization and such matters as production controls, and confine myself to the economic stabilization controls and to our attempts to keep price and wage levels relatively steady.

One aspect of the purpose of such a program--and a familiar one, I think, to you in the services--is the way in which price increases virtually wipe out part of the appropriation that is given to the services. Mr. Charles Wilson estimated that out of a 10-billion-dollar appropriation, the amount of 2 billion dollars in fact has been canceled out by price increases since 1950. On individual items the rate of increase has been staggering. It reached as high as 600 percent on some strictly military items. Even for an item like shoes it was 100 percent. It meant an increase from five dollars to ten dollars in the basic price that the military has to pay for a pair of shoes.

That feature, the disappearance of the appropriation, although very dramatic, is not the most important of all the factors in this program. For if we could proceed all along the line into a higher price level, and, if there were no unfortunate consequences, it would not make too much difference. It would be relatively easier to get a given amount of military appropriations.

A major difficulty in the situation of a rising price and wage level is the large part of the American public who are on incomes which cannot be increased. Their incomes are not flexible and do not go up in times like this. Therefore they are caught in a squeeze, a hardship situation. They ordinarily include people on pensions or on social security, and people who have jobs where they cannot get more salary. I am not talking about the really tragic inflations, such as the inflation in China, or the German mark inflation following World War I. I also mean the kind of inflation that took place in France following the First World War, or even that is taking place in France now after World War II.

The greatest hardship falls upon people in the middle class or middle classes. Their standard of living is wiped out by price increases. I think if there is any great source of political stability in this country, it is in that class; and that is the class that is hardest hit by price and wage increases. They are hit much harder than the workers who are relatively able in this country to adjust their wages by negotiation or by strike and so on. The dangerous consequence of inflation is not only the damage that it does while it is going on, but the long-term consequences upon the middle class. They lose their place in the social structure. They are subjected to hardships. I think it promotes a lack of political stability. In the long run that is perhaps the most dangerous consequence of this inflation that we are now engaged in trying to prevent or at least slow down.

Apart from the consequences to this middle class, in a time when prices and wages are moving up rapidly, as contrasted with the slow movements of prices and wages that take place in normal times, there are increased stresses and strains between the different parts of the public—between business, labor, and agriculture—as to how much of the total national income each is to get. Whatever the result, meanwhile there is a lot of working at cross purposes and conflicts, which, it seems to me, have a tendency to divide the country and bring about a sense of disunity at a time when this country is in peril and unity is one of the most important national objectives.

I say these words at a very curious time. But it is my hope and expectation that this kind of strife now going on up on the Hill—and it will go on for another month—will sooner or later disappear, and we will get some agreements on a basic program of this kind; that they will see the importance in the over-all mobilization objective of the economic stabilization.

There remains a question, which I wish only to mention, and that is: What is the role of direct price and wage control and what is the role of so-called indirect controls, such as controls over the amount of bank credit and the amount of money that is going to be taken out of the system in the form of taxes? If we had a very firm program, which prevented any bank credit except where actually necessary for war plants, and if we had a very tight tax program which brought back to the Federal Government at least the amount of money that was pumped into the system in the form of payments for materials and services, we would broadly have that kind of system in which you could do without direct price and wage controls. You wouldn't have to meet a situation in which there would be more money in the system than there are goods available, because you would be taking this money out through taxes and through clamping down on the absolute ability of banks to make loans.

Canada, for instance, is now engaged in trying a tight program which will actually put a limit on the amount that banks can loan. They can do that more easily than we can, with our Federal Reserve banking system. It remains to be seen whether it will be effective there or not.

But all this is, it seems to me, a theoretical approach, because we are not likely to get in this country to that kind of really tight tax and credit controls that hurt, that really prevent money from coming into the system.

Such controls also have some consequences which have never been fully measured. Tightening up credit controls may lead at least to widening the areas of unemployment. If your objective is to promote general unity, how much will you accomplish by allowing areas of unemployment, due to inability of industry to get enough credit, to come in.

Moreover, there is a political element in the whole question of inflationary controls. The real question is, What makes people willing to pay higher prices? Part of that is due to fear that goods are going to go off the market. That is what caused some of the price rise in 1950. Part of it is the question of whether they have basic confidence that the Government is going to stabilize the price situation. If they don't have that basic confidence, and if they have the resources with which to pay the substantial increases in prices, they will do so, no matter what kind of tax and credit controls you put into effect, especially since the end of World War II the American public has had a tremendous amount of liquid reserves, including savings bonds, which they could rush into the system and put into goods if they had the fear that the dollar is going to wind up without being worth very much.

As part of the over-all situation I think it is true that a system of direct controls constitutes some assurance to the public that the Government is taking action to stabilize the value of the dollar. So it has what you might call a political and psychological value in any event. And certainly with the kind of program we are likely to have in this country on the tax and credit side, it will be necessary in economic terms to do that.

One of the objections that have been raised to direct tax and price controls is that the direct price control program interferes with production. If it were to interfere with production, there would be a very serious question as to whether we should have such a program.

One way that a price control can interfere with production is that if the price control is not handled right, it will be more profitable to produce some goods than others. If you don't get a higher price for producing the goods that are in demand and that are necessary, you are very likely to produce goods that are not so necessary, because you have a higher profit margin.

I might say that it is ordinarily true that a price-control program cannot make it equally profitable to produce every single item. It is physically impossible to administer a program and make the kind of cost determinations that would be necessary so as to make it equally profitable to produce one item as another. As a matter of fact, in business normally there are very different rates of profit which businessmen operate under while they are producing a full line. Yet businesses continue to produce full lines for various reasons. They want that reputation. They don't examine every single element of costs and production against every other.

I think it is noteworthy for the record that during the years 1942 to 1945, when we had a relatively firm system of price and wage controls in this country, you still had the most massive productive effort that the world has ever known. That experience in itself shows that price control need not interfere with production.

I think it could be said, on the contrary, that because you have brought about stable conditions, you have improved the over-all incentive to produce, the willingness of workers to produce, over what otherwise it might have been. To some extent, because you make it unprofitable to hold materials for a rise in price, you prevent speculators from putting money into materials. All that encourages production rather than interfering with it.

Basically the success of a price-control program depends upon its administration; and I therefore might speak very briefly about the kind of administrative program that we have and something about what is in the wind for the future.

The administration of the price-control program was established on 26 January 1951 by the general price freeze regulation. There was before that a regulation on automobiles, which was just a freak situation. It is largely a psychological thing and does not in any way have any impact on the basic program of the agency.

The first thing that you have to know about the freeze regulation is that it is only a very temporary measure. I think it has had a considerable effect on prices. I am convinced that there were many manufacturers and wholesalers and retailers who would have kept on going up with price increases if they had not been stopped on 26 January. But the nature of the price-freeze order in terms of administration is such that it has only a very temporary value.

One reason for that is the problem of new goods. The freeze order says: "You shall not charge more for goods than the price charged in the base period." That is all right as long as the man is producing the same identical thing. But in a situation like this he has been able to change what he is manufacturing in terms of shoes, sleds, mops, and so forth. So you have to provide him with a price formula as a calculation of the price on the new item. It is possible to set up a price formula for that new item; but that means that you are getting away from the freeze and you are getting on to some kind of formula control. So long as you stay with a freeze, with just freeze regulations, the industry quickly gets away from the freeze and produces new goods. So the freeze begins to cover less and less of the total production. You find that you are on a formula control basis.

Then, immediately after the freeze, we set up what we have called our interim administration. We are working it out so that on the day when we have a realistic system of price-control regulations, we can tell the businessman very quickly just what the prices are on his commodities. We have gone in this interim system of regulations largely to margin regulation.

At the basic levels we have had three programs in effect. To some extent we have been able to roll prices back. That was possible in steel scrap, for example, and in fats, oils, and hides. Steel scrap and hides have been the items of particular interest to the production planners in the Army because a lower cost for hides means a lower price for the shoes, and shoes are a pretty large part of the Army's buying program. We were able in those cases to roll back the prices because prices had risen fantastically, to a level that was totally unreasonable under any standard.

To a large extent our price regulations since the date of the freeze have been translating the freeze levels as of 19 December 1950 to 26 January 1951, the base period of the freeze, into equivalent dollars and cents ceilings. We have already done that on oil and, in fact, in the whole field of petroleum products.

To some extent we have granted increases since 26 January to compensate for cost increases that we knew could not be absorbed by the industry. A dramatic example of that was bituminous coal. The very day following the general freeze we granted an increase of between 25 and 50 cents a ton on bituminous coal to take care of this tremendous wage increase which took place in January before the wage order became effective. The bituminous coal industry being what it is, there were several small mines operating on a narrow margin, as well as a small number of comfortably large mines. We had to let that wage increase travel on into the price.

At the retail level, we have something like two million sellers. To handle the freeze regulations which were generally conceived was very difficult for them to do. So we put out a series of retail regulations which have given pricing instructions to the retailers. We had a soft-goods regulation, Regulation 7, which required them to prepare a pricing chart; you may have read about this in the papers. They put down on their pricing chart what their costs and prices were on the list date, 24 February. We are going to use, from now on, that pricing chart as a measure of what their permissible prices will be as the new goods come in.

You may appreciate some of the administrative problems in the whole field, for example, of house dresses, shoes, and all consumer soft goods and furniture, trying to find out, when a new item comes in--new items come in by the thousands, because of the style demands--just what item that corresponds to in the base period, and then to set the same price as was in effect for the corresponding item in the base period. It would be an impossible task for our investigators to enforce. It would be almost impossible for the retailers to apply, because you simply don't have that definite correspondence between the new item and the item that they sold in the base period. The retail trade of this country flourishes and thrives on change.

What we have done in effect is to set up a pricing chart in which we say, "Regardless of what this item is, we look at its costs, the cost of the new item. Go to your pricing chart and pick out some item that you had in the base period in the same category, which cost the same amount. Whatever the price was for the base period will be the price ceiling for your new item." That is, because of the difficulty of pricing by identity of items, we base our prices solely on the cost of the new items coming into the retailers' hands. That cost corresponds to a ceiling price as determined from the pricing chart. We must put our main effort on controlling the cost to the retailer at the manufacturing level and the wholesale level.

That is one technique that has been used. In the food retail regulations, we have specific percentage markups set forth in the regulation for each item. In the case of restaurants we currently have a system of over-all gross margins. It is not possible today under our present regulation to tell whether a restaurant is violating the ceiling on some particular meal. Our requirement is that over a four-month period the restaurant's total margin of prices over food costs should be no larger than the margin specified in the base period. That means that it is very difficult to enforce on our part. As I say, it is impossible to know on any particular meal whether the ceiling is being violated. It is necessary to get the total records for a three-month or four-month period and find out whether the restaurant is in compliance. With that kind of technique we are giving the restaurants some freedom in their prices on particular occasions and are exercising price control in a very broad and general way.

It is just an experiment so far as we are concerned, and we can't say now whether it will work. If it does work, it may be that it will be extended to other fields. If it does not work, we will have to abandon it. If it does work, it will hold a lot of promise as a price-control system. If we work price controls by means of gross margin controls, we will have the best possible method. You can then let the individual businessman decide what his particular price will be. You don't get yourself involved in a complicated administration of particular prices. You check in the price level through the over-all gross margin. But, as I said, because you can't enforce any particular ceiling, there is a question whether that kind of program can work or not.

In some cases, although we have allowed prices to go up at the manufacturer's level because we had to, we haven't let the retailer take the same percentage of markup. We have only allowed them to take the actual amount of dollars and cents increase of cost. For example, we let the price of automobiles go up at the manufacturer's level 3.5 percent a couple of months ago. But at the retailer's level we told the dealer that he could take only the exact dollars and cents amount of that cost increase to him in his business. That meant that his margin was squeezed somewhat. It also meant that the ultimate cost to the consumer went up less than 3.5 percent. It went up only 2.75 percent instead of the 3.5 percent that it went up at the manufacturer's level.

We have done the same thing with carpets. We have allowed the price of carpets to go up. There was a tremendous increase in the price of imported carpet wool. We didn't allow the retailer to increase his price by more than the dollars and cents increased cost. Our large program at the moment is the manufacturers' regulations. The manufacturers' regulations broadly provide that you take your prices that were in effect 24 June 1950, and you add the amount of your labor and materials cost increases since that date. The regulation is somewhat complicated, because we have manufacturing companies in this country that keep their cost records in very different ways. So we have a provision giving them an option as to how to calculate the increase in cost over the base period. That is the basic principle of the regulation.

One reason wht we have put that regulation into effect was this: On 19 December 1950, Dr. Valentine, who was then the Administrator of ESA, put out a voluntary appeal to manufacturers not to increase their prices. He promised in making that appeal that nobody would be disadvantaged because of his compliance with that appeal. It was only voluntary, after all. But on 26 January 1951 we put the price freeze into effect and all manufacturers were frozen at the prices which then were in effect. So those who had refused to comply with the voluntary appeal got the benefit of higher ceiling prices than those manufacturers who had complied with ESA's voluntary appeal. Those who cooperated got it in the neck, as usual.

We felt that we couldn't continue to operate a price-control program if we were going to violate that kind of assurance that had been given to manufacturers--that they would not be disadvantaged if they complied with it. That would mean that any time we put out an appeal from now on out--and even a formal program must work to a large extent by voluntary compliance--they would just not believe our assurances and we would never get anywhere.

The formula type of regulation has the very same basis whether or not the manufacturers complied with our voluntary standard. Therefore, if there is some inequality, there will be some price rollback in the case of manufacturers who increased their prices faster than their costs and there will be some roll forward in the case of manufacturers who did not increase their prices as fast as their cost went up. We don't know where the balance is going to be. Some of our staff believe, and there is some basis in the general economic data for so thinking, that the balance will be a rollback.

In addition to the action that we have taken at the manufacturers' and retailers' level, we are working now on the problem of what to do about wholesalers. That is a problem of tremendous administrative complexity. There is more variation between different wholesalers than there is between manufacturers and retailers. The complexity in the functions which they perform and in their distributive systems is hard to imagine. Although we are working out something on that, it is a problem that OPA never did really get hold of.

I think that in a quick survey of our OPS program we have to talk for a moment of what has been done by Mr. DiSalle on the farm level. The price ceiling we are putting on cotton sold by producers is the first that has ever been put on that commodity at that level. Mr. DiSalle had quite a going over by the senators and congressmen from the agricultural states. But we believed that it was essential for our over-all program.

The program that has just been announced on meat is a very interesting one. We have found that since January the price of livestock has advanced about 10 percent. We were unable to put a ceiling on livestock in January; it was just too complicated to do it. The grading problem on livestock meant that we couldn't spell out the freeze regulations. So we had to let it alone, and the price went up about 10 percent.

Our program first calls for a rollback of the price on livestock to where it was before this 10 percent increase. That means we will be able to set a specific dollars-and-cents ceiling for packers, processors, wholesalers, and retailers, which will correspond generally to the January level. Then on the first of August we are going to have another rollback in the prices of livestock and a reduction of about four cents a pound at the retailers' level. On the first of October we are going to repeat the process once more and have another four-cent rollback across the board. The effect of that will be that it will come to something like meat at the retail stores as of the first of October which will be approximately eight cents, and possibly more, below the present level of meat prices.

I should make a note that at the time we put the general freeze regulation into effect we did not do what so many people were urging on us to do. That was to roll back prices very sharply. There was a lot of general popular and political pressure, you might say, for a very sharp rollback in prices. But people wanted to keep the wages that had increased after June 1950 and they wanted to see prices go back to June 1950. As you know, that is an impossibility. The wage increases that had already taken place had appeared in the cost structure throughout the economy. It would have been impossible to have any substantial rollback from the 26 January level. In fact, it would be good enough to be able to tack them where they were.

However, in the case of particular items, like livestock, where even after we finish all the rollbacks they will still have more than 120 percent of parity, we should be able to make that kind of selective rollback. We have achieved some price reductions that I think the workers will regard as significant. We hope they will have an important effect in dampening any pressure for wage increases from here on out.

The whole process that I have described has been rather technical, and I think you will be better able to understand it when you have the notes of the presentation rather than by listening to me state it. We will have a system of ceiling prices at about the level I have described, that is, the period from January to June, plus cost increases to 14 March. That is for manufacturers who have had no cost increases beyond 15 March. If there are any cost increases after that, the question will be what standard we should use in determining whether those cost increases should be allowed as price increases. Such increased costs may take the form of increased transportation costs, or increases through inefficiency of labor, which may creep into the system when new and unskilled labor comes on the scene.

Mr. Johnston, as Administrator of ESA, tendered us a directive a week ago in which he laid down one basic standard. He said that a price increase should be allowed for an industry if its costs have increased since 15 March to such a point that the industry's over-all profits are less than the excess-profits tax base. That is 85 percent of the highest three years from 1946 through 1949. The industry can pick out the best three years of those four and take 85 percent of its average profits for the best three years. It is entitled under that formula to an increase in price sufficient to return those over-all profits if costs have increased.

That formula still has to be worked out in a lot of details. What will we do about increases in net worth? What about companies in a "growth" position? What about companies in a depressed position in the base period? We are working on implementing the formula now. That basic formula, we feel, even if there are some cost increases, will enable the system to hold the price levels firm, at least for some time to come; and that is an important and necessary part of the program. If we were merely to permit every cost increase to go into effect as a price increase, we would not have really checked the increase in prices.

I might say briefly that the question of how far the price-control program is to extend to the prices of military goods is up for discussion at this time. In the last war there was an instrument known as the Henderson-Forrestal Agreement, under which a long list of items were regarded as strictly military and were exempted from OPA price control. On the other hand, those items which the military buys which have civilian counterparts, which include basically the food and apparel purchasing program, were regarded as under OPA price control. That allowed certain strictly military items of apparel, like uniforms, to be exempted, while things like undershirts and shirts were subject to control. We thought this time of picking up where they left off the last time, with that very carefully drawn agreement that had been worked out.

There is, I may say, some pressure from the Munitions Board to have all military purchases taken out of OPS control. We feel that from the point of view of the success of our program, we would not be able to hold a price ceiling on civilian apparel or on food if the military people were free to jump in and pay higher prices because of their pricing methods. We do have a provision in the regulations where in an emergency delivery the military representatives can pay higher prices if they send in an immediate report to us what that emergency was and why it was necessary to pay higher prices. This matter is up for discussion at the highest levels.

I think, however, it is fair to say that our people have been in very close contact with the officials of the Munitions Board. They are very agreeable and hard-working gentlemen. We are trying to iron out our problems under our present directive; and I think there is a large chance that they will succeed. I also have met with the Quartermaster Generals, and we have solved most of our problems that have arisen up to now.

In conclusion I would like to say--perhaps I should have said it before--that Mr. DiSalle is most regretful that he couldn't be here today. He had a long-standing invitation, which he accepted, to address the Economic Club of Chicago, where he is today. But he is most interested in presenting this program to you. He realizes how important it is to have as broad an understanding as possible of what we are trying to do in the civilian sector of the over-all mobilization effort on the part of you gentlemen, who have a major responsibility, as we well know, in the over-all mobilization effort. Thank you very much.

QUESTION: Mr. Leventhal, during your lecture you mentioned that in the period from 1942 to 1945, despite very strict controls, our country put out a terrific production effort; that the controls really had no effect. But don't you think that during that time, with a real war with a recognized enemy and a job to do, we had a different situation from what we have today; and that fixed-price control, cost control, profit control, and that sort of thing will be hard for certain people to take when you don't have a real war to fight? Most people don't recognize it as such right now. Isn't the comparison between today and 1942 to 1945 a little different?

MR. LEVENTHAL: I think that point is well taken. I was speaking more to the abstract argument that you run into, that runs as follows: The greatest indicator in our economy is prices. That is the indicator of what people want. The great motivator in production is profit. Without that kind of force at work, you have to substitute some kind of government decision, which in a rough way is what price control is. Government decisions can never be so accurate or so sensitive as individual bargaining on prices. It therefore must interfere with production. That is a very quick outline of the argument.

And the argument is not wholly specious. I think it is true that the Government works slowly. We have particular problems in understaffed and underofficed organizations. We may in certain areas, because of inability to reach quick decisions, interfere somewhat with the sort of things that would go on in a free-enterprise economy. But I think it is also true that if we lay down general ground rules, as we have laid them down, we can have sufficient flexibility so that we can work out individual problems and still get rapid enough decisions that we don't interfere with production.

It is more a question of administration than anything else. I think the success of a price-control program depends just as much on its administration as on its conception. Of course, that is true of any important program. It is like saying that the personnel is more important than the organization chart. It is just one of those self-evident truths.

With good administration you can do a lot; with weak administration, with confused administration, you can interfere, perhaps in all sorts of unintended ways, with production. But I would say that, certainly judging from experience in this country, it is possible in general to have effective administration.

Now, on the problem of incentive, since our general profit standard is the excess-profits tax standard, we believe that there should be enough profit on the over-all basis to encourage production to the full. It may be that there are particular items where we will now have to grant increases in order to get production in those areas where during a war a man would produce from patriotic motives, even though the margin of profit was narrow. I don't think we will be able to find them out until we are up against that situation.

My personal feeling is that there is really a great deal of unity among businessmen in favor of this price-control program, in terms of the necessity of it; that it is not only important in terms of profit, but important to the over-all productive effort. I think that is something that is going to act as some incentive for production.

In my opening remarks I passed over any mention of what we do for individual companies as contrasted with what we do for a whole industry. OPA started off with a very tight standard. It would do nothing for an individual company even when it was operating at a loss if the company was not operating out of pocket. If it was only operating at a bookkeeping loss, it didn't get any consideration. We now recognize that we cannot expect an individual company to produce at a loss, even though it is just a bookkeeping loss. We think that increases must be granted to individual companies even where the regulations are fair and equitable in their general application to the rest of the industry. So we are starting with a more realistic view of control, I think, since we are not in an all-out war situation so far as individual companies are concerned.

QUESTION: I didn't get the full import of your formula with respect to price ceilings and the excess-profits tax. If I understand it at all, it is that the person will not get a controlled ceiling price if he is not in the excess-profits bracket. Is that right?

MR. LEVENTHAL: No. That is not what I meant to say. I will state it in this way: After we get our price program working for the interim period, we will have a framework for price-control ceilings covering, not all industries, but most industries, and specific ceilings so far as we can. That would be set roughly on the level depending on what part of the industry is classified, either the January 1951 prices, or on the level of the June 1950 price-plus-cost increases, depending on which type of regulation the industry happens to fall under. In any event, however, we will have a price ceiling. Then the question will arise, Has this industry granted any wage increase which was approved by the Wage Stabilization Board? If so, what are you going to do on the price side to cover that increase on the cost side? The ICC has announced transportation rate increases which will be effective on the third of April. It has granted the rail carriers an increase. That is going to increase everybody's cost. What are you going to do to the manufacturers in the industries that are affected by that increased cost?

The formula says you do nothing. You hold them at their present price level under the ceiling. You make no allowance for increased cost of labor, you make no allowance for increased cost of transportation, unless they show that as an industry that approach will put them in a position where their general profits will be less than they were in three of the years between 1946 and 1949 adjusted by 85 percent.

All that this standard does is to say how much of a price increase, if any, you are going to grant in order to compensate for a cost increase.

QUESTION: That is to say, 85 percent of their three best years?

MR. LEVENTHAL: The excess profits tax law says 85 percent of the three best years between 1946 and 1949 inclusive.

QUESTION: We are charged with making a critical analysis and evaluation of the action taken since Korea. As I remember it, last year the emphasis was all upon the efficacy of indirect controls, such as voluntary cooperation, as opposed to direct controls. Don't you think we would have had a better chance of putting a price-control system into effect if we had started it at the time that Mr. Baruch recommended it to be started? Or do you think Mr. Baruch's plan would have interfered with production at that time?

MR. LEVENTHAL: I think we would have much better stabilization prospects now if we had taken hold in June 1950 than by capturing it, as we did, in January, when so much water had gone over the dam. When so many price increases had gone into effect, we just could not unscramble them.

On the question of whether or not Mr. Baruch's plan would have interfered with production, there are those people who say, if you are going to wind up ultimately with a price and wage program, it is a good idea to let the prices run up a little bit at first. We did that in the case of the nonferrous metals. There was a tremendous increase, but it resulted in a lot of new mines being put into operation in this country.

I am not really qualified to make a judgment as to whether or not Mr. Baruch's plan would have interfered with production at that time. That charge has been made. I think I am qualified to make the judgment that it would have meant a firmer stabilization.

The problem, however, was that Baruch didn't really handle the question of administration. It does take time to set up an administration. It does take time in a representative democracy for Congress to debate a defense production act.

A very curious phenomenon took place, it seems to me, last summer and early fall. I would venture that if President Truman had proposed a defense production act with a provision for price and wage controls, there would have been a furore about it. But, because he did not, it was initiated by a coalition of Republicans and Democrats.

It might well have been that, if there had been an attempt to carry out the Baruch plan at that time, there would have been opposition to the act on political grounds. But certainly the impression that I get at the highest level among the staffs that I have to deal with, the White House staff and others, is that if they could have put that program into effect right away, it would have eliminated a lot of the difficulties that the Administration has had to go through in the last three months. Obviously, it would have meant better stabilization controls.

Now, taking that situation into account, as you have to, I am not sure that there was serious delay until the last couple of months. I think that about November or December was the time when the situation started to slip.

Also before that, you remember, and until the time of the Chinese intervention I think we had a very different atmosphere in this country. We were winning the war in Korea. Everything was looking good. It looked as though this limited engagement would be over very quickly. It might have been possible to get over this crisis without the kind of price and wage controls that eventually we came up with. At the time of Baruch's proposal the situation was confused. It was not clear until the Chinese intervention. But after that it does seem to me that we should have tightened up on the over-all ceilings or have been ready to do so.

Ready or not, they should have put some kind of ceilings on. I think Dr. Valentine made a serious error when he said, "I can't put on these ceilings now, because I don't have the staff." I am very sympathetic with his difficulties, but I don't agree with his basic apprehension that he could not put the ceilings on because he didn't have the staff. I think the only way to get a staff is to have a hard-hitting program and then build the staff around it.

QUESTION: Have there been any plans made for controlling production in the event of an all-out war, so that we will get production of low and medium cost items and not just luxury items, as we had the last time, where everybody wanted ordinary shirts, but there was nothing available but sport shirts because the manufacturers could get higher prices for them?

MR. LEVENTHAL: That is under planning now in a very elemental way by ODM and OPS. I think that was a very serious criticism of OPA's effort--that, although the cost of living index included cheaper items, very few of the cheaper items ever got into the market. We are relying on production controls to remedy that.

To the maximum extent possible this time we are trying to set up price formulae which do not provide an incentive to produce higher-priced items, and which provide relatively sufficient incentive to produce low-cost items.

Generally speaking, manufacturers like to keep on producing low-cost items. They like to keep in the fields where they know there are going to be large markets later. I think it is true that you don't have to give them the same margin of profit on low-quality items as on the higher quality to make them produce the low-cost items. If the margin is a reasonable one, they will continue to produce the low-cost items.

We are trying to accomplish that by having some flexibility in our price ceilings. There is a temporary glut of soft goods now; so there is no problem. But there will be a problem when all this money begins getting into the hands of the workers. I think it will be about the latter part of this year. I think by that time soft goods will have the same kind of pressure on them that the hard goods market has now. If the manufacturers insist on diverting production from low-cost items into high-cost items, the Government will have to follow up with an allocation system, a set-aside system.

COLONEL BARNES: Mr. Leventhal, your presentation has been very frank and clear and comprehensive. I thank you very much.

(10 Aug 1951--350)S.