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PRICE CONTROL IN WAR TIME

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PRICE CONTROL IN WAR TIME

I want to talk to you informally about the general theme of price fixing in war time I understand that what you are doing is trying to have ready when a war comes, if a war comes, a reasonable program for mobilizing the industrial resources of the country in such a way as to bring quickly and adequately to the scene of combat those things that you need, that you want, and as you do it to impose as little suffering upon the civil population as possible, and to be prepared as you should be prepared to make such dislocations in ordinary processes of industry as are needed, carefully avoiding dislocations which are going to impair the efficiency of this mobilization and such as will ruin your objectives. A military man is pretty careful, unless he is in a very desperate position, to leave himself a margin of safety as he makes plans for military action He doesn't want to overrate his resources. He won't expect a soft road to take a long train of heavy guns You have to reckon in any plans you make upon human nature and the social order and you don't want to undertake things that are going to bog down in a soft road You can overtax certain human motives, you can overtax certain industrial and trade machinery You must analyze the problem in terms of what we have available for social and economic coordination and control

Now what are the instrumentalities of social coordination and control? We have many One that is very dependable within its limit is social expectation Men try to live up to what is expected of them by their group, just an impersonal atmosphere about you, and what you get out of men depends very much upon the group. You expect different things from different groups The Army expects a soldier to be brave, the general public expects a soldier to be brave And if a very brave soldier is a little careless sometimes about meeting a note at the bank on the day that it is due and the banker has to write him about, and when the banker writes him about it he gets an unsatisfactory reply, or none, that's not nearly so bad as if a banker fails to meet his obligation on the due date We expect the banker to be strictly, scrupulously exact in money matters, but if robbers come into the bank and the banker gets rattled and hides behind the counter we don't condemn him as we would condemn a soldier under similar situations You make different demands on men in different positions and you can't expect the whole civilian population to take a war with the singleness of purpose, the subordination of everything, life included, that you naturally and regularly expect of men in the Army Don't, therefore, expect to apply Army standards or Army discipline to a civilian population You have got that Army discipline and you didn't get it in the first week in the Army or the first month in the Army Men are trained a long time before they get it

Now the instrumentalities of religion, of propaganda, of education, all these things are there, morals, law and government. Law can do things and government can do things that social expectation can't do, but if you had a people where the sheriff had to be present every time a debt was paid or every time a man performed an upright act you'd have people go to pieces very quickly. We have a great social discipline quite apart from law Take such a simple matter as making change. You go into a store, buy a pack of cigarettes, give the clerk a dollar bill, and he hands you back the change The cigarettes are fifteen cents and he hands you back a half dollar and some nickels. You look at it, it isn't quite enough You don't think he has robbed you or cheated you, you just extend your hand and show it to him, he looks at it, nods, and puts another nickel on You go away not thinking he was cheating you, just thinking he was making a mistake And he doesn't often make a mistake. That is a tremendous achievement, isn't it? We do not expect to be short-changed in our general economic life In some other countries that isn't true, but in general that is true among us. We take it for granted that men will make change correctly There is behind that a tremendous social pressure that has gotten into men's backbones.

We have going on in Wall Street all the time, every day, a volume of business that runs high into hundreds of millions of dollars, over the telephone by word of mouth, with no memoranda. Men make and lose money on those transactions. The man who loses money carries them through. There are dealings in foreign exchange all by phone On the orders that go to the stock exchange from the phone of the customer to the brokerage house and phoned to the stock exchange the broker doesn't take a written memorandum and neither does the dealer he is dealing with. Each makes his own note but the contract is made by phone or word of mouth, and disputes regarding them are very rare Tremendous discipline, tremendous body of standards in that, and the law couldn't make men do that. Law is that part of the social will which will be regularly backed up by the organized physical force of the group, but the limits of what physical force can do are very, very definite.

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Now we have further, as the most important instrumentality of social coordination and control in economic life, the market place, the money economy and the system of prices. Prices tell men what to do. Prices, wiser than any man that helps to make them because every man that knows anything has got to tell it to the prices Here is a man dealing in wheat. He knows that the chinch bug is bad in Kansas and crops are going to be short there. Well, he buys wheat, and then in buying wheat he tells it to the market. Here is another man with special sources of information from the Argentine, heavy plantings there, good prospects, and he things wheat is going to be pretty abundant He sells wheat. Here is somebody else with special information from other parts of the world, from other regions of the United States or Canada, and every day those prices go up and down, move as each man tells it to the prices, and so with commodities in general Moreover, wheat is planted somewhere in the world every month in the year and as the price goes up or down, more or less wheat is put into the ground or more or less land is diverted from wheat to something else. It guides industrial activities of men Now that great system of prices left free, left unregulated, is the best equilibrator we have, the best assurance we have that things are going to be produced in proper proportions, not too much of that, enough of this, price here going up, shortage, price here going down, excess. Very good They curtail production here, they increase there, they increase there and curtail here' equilibration. Capital moves out of industry where prices are going down, wages get down, unemployment gets bad, laborers move over toward industries where prices are rising, where there is increasing demand. We have, thus, an automatic re-equilibration, an unconscious, automatic process that does not require a social brain.

Now when governments interfere with that they take a grave risk. When they do it in peace time they almost invariably make mistakes For example, in the case of this wheat market which I have described, and the way I described it was the way it used to be before the governments ruined it. Today you have a network of tariffs and trade barriers among the countries of the world so that the international market for wheat is very greatly narrowed You used to be able to break a corner in Chicago by bringing some wheat over from Canada short order, but they have got a big tariff wall to come over now. The Government, moreover, has done so many things in the way of artificial manipulation This New Deal didn't begin in 1933 The New Deal is a matter of personally conducted business, designed partly to keep up the general activity and partly to benefit special classes.

That matter of special privileges for special classes we had a long time ago. Protective tariff is the beginning of that, but personally conducted business is newer The last orthodoxy you had dealing with the general business situation was 1920 to 1923 In that benighted day the Government of the United States didn't feel it was its business to make prosperity, or to unbalance the budget for the purpose of increasing consuming power. The Treasury had the old-fashioned policy that it was its business to protect the currency, the sound gold dollar, to reduce expenses, and to relieve business as far as it could by reducing taxes. That's all they did through the whole of the crisis of 1920. They paid down public debts, they cut expenses sharply, they didn't feel it was necessary to put people on the public payroll to give them employment, they kept reducing the public payroll. The result was that we got a quick liquidation, terrific liquidation, commodity prices broke from 248 to 138, that's a terrific break. Wages reacted not nearly so much Insolvent people went broke, and solvent ones stayed solvent. They readjusted prices and costs quickly The tide turned up in August of 1921, and we had a labor shortage in the spring of 1923 Meanwhile all the time government debt and taxes were going down

That is old-fashioned. The New Deal began, in the sense of a personally conducted market and business situation, in 1924 when the Federal Reserve System for the purpose of making prosperity bought $500,000,000 worth of Government securities, creating what was at that time regarded as a fantastically low money market, with 2% call money and acceptance rates. Commercial paper got down to 3½, maybe 3 Bankers would like to have those rates again! But it was fantastically low in our experience and the speculators responded with a great joy. There were tremendous issues of foreign bonds here, a great increase in new securities of all kinds, rising stock market issues and big agricultural exports based on the foreign bonds, and so on.

And then the Government continued personally to conduct the market. Every time the stock market would begin to flag a little bit you would hear something from Secretary Mellon or from President Coolidge, the "Capeadores of Wall Street" my friend Ralph Robey calls them in an article in the Atlantic Monthly. The Capeadore is the man who waves a red flag at the bull. And all was merry.

When the great break in the market came in 1929 Mr. Hoover began to increase the New Deal He called in the heads of business and banks and railroads, urging them to hold up wages, to hold up prices, to increase capital outlay. He got the municipalities as far as he could to increase their capital expenditures, borrow more money. Railroad presidents particularly were loyal, the poor old Frisco went home and voted preferred dividends for the rest of the year, to "create purchasing power." Mr. Hoover also had the Federal Reserve people reduce rates again, buy more Government securities, and ease off the money market, and we got another flare up, another stock market boom in early 1930, and issued a lot more foreign bonds

And then Mr. Hoover's Farm Board came into action This is the story I want to tell about that wheat market. Beginning in 1926 various countries, Hungary, Canada, the Argentine and others were artificially manipulating the price of wheat by government action or by pools sanctioned by the governments The price was held too high, with the result that between 1926 and 1929 the visible supply of wheat in the world doubled. Farmers produced more than they otherwise would have produced. People consumed less than they would otherwise have consumed, and the visible supply doubled. We hadn't done that. We had been producing wheat and selling it, but in 1929 with the break in the stock market the New Deal began to buy wheat and held up the price of wheat with the result that the Argentine, Canada, already pretty tired of holding, sold under cover of our umbrella We didn't sell to the outside world, our farmers' plantings increased in the winter, and that whole visible supply of wheat was transferred from the outside world to the United States.

Now that kind of thing happens, you see, when government interferes with prices, and when you go to do it in war time you want to be mighty sure of your reason, mighty sure of your purpose. Just why are you doing it? What are the objectives? What good can you do by it?

I became convinced as I watched what our Government did in 1917 in this matter that you could do some good in special cases if you were sure of your objectives and if you didn't overstrain human nature in the process. First of all, you know what you want in war time. In the World War you wanted just as much wheat as you could have to go to the Army, to go to Europe, and wheat was rather short. You didn't want copper roofs being put on civilian homes in the United States, you wanted all the copper you could get for the Army. Sugar you had to have on a great scale for smokeless powder. There were various definite things that you had to have, alcohol, coal, and so on. The problem in peace time is a very vague problem No government knows what should be produced, only the market knows that. But in war time the Army knows what should be produced, what you have got to have, definite things, and you don't want to pay too much for them. You don't want to have what is produced diverted to non-essential uses, and you want to have enough produced, you don't want to discourage production. Of course one of the first tendencies if you hold down a price is to reduce the incentive to production, and you have got to watch that through all stages of the game.

I studied pretty carefully during the War the retail price control of sugar in Massachusetts at first hand. I was teaching at Harvard then. Also the case of wheat and flour over the country, the case of copper over the country, anthracite coal and bituminous coal. Now the case is pretty simple with reference to the retail price of sugar in Massachusetts. Here was a very startling, sudden, new demand for sugar to make alcohol, to make smokeless powder, and that cut very sharply into the sugar available for civilian uses Moreover, transportation was increasingly commandeered for war purposes. It wasn't easy to increase the supply of sugar in Massachusetts, no matter what people had been willing to pay, by bringing it in from the sugar regions The question was, temporarily at least, how to keep the sugar supply of Massachusetts, which couldn't increase much, from all being bought up by the wealthy and leaving the poor without any, and what to do about it There was pretty general feeling over the community that the price of sugar should be kept down. It was, but when you did that you had to ration the supply. That was done, first ten pounds to one customer, then two, then one. You went into a restaurant and they wouldn't put a sugar bowl on the table, they would give you a lump of sugar or a little paper sack with a teaspoon of sugar in it, but by a bit of discussion a man could get two lumps. I think a man had trouble getting three. It was a thing that affected a very small part of the retailer's business, much easier to hold him to one price on sugar than it would have been if you had tried to regulate everything in his business. It was much easier to hold the retailers on this thing where there was a pretty fixed supply than it would have been if they had had to buy up the wholesale market to get more sugar. You have got to watch not merely the retailer temporarily but the whole chain of events leading up to the retailer. That was a short run matter, it was very easy, particularly when you had these war-time motives to play with

The problems are much greater when you undertake to regulate a whole industry It wasn't hard in copper. You had a highly concentrated industry. Most of the mining companies are very big. They were conspicuous targets for

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public disapproval if they didn't play ball. The leaders in the industry were, moreover, men of energy and ability, and were patriotic men. It was agreed that the price of copper should be cut, as I remember, from thirty cents to twenty-three cents a pound. At that price 99% of the production could go on without loss, and much of it at a good profit.

Further, in the case of mining in contrast with agriculture When you are figuring on cost of production of wheat, the old economists to the contrary notwithstanding, land rent is part of cost of production. Land rent represents the alternative use. Wherever you have got an alternative you have got a cost. You have got to pay enough for wheat land to keep it from being used for corn or for alfalfa or something else that it could be used for But in the case of copper, mine rent is not a part of cost of production in the short run. In the long run, yes, because if you are not giving them that mine rent they will just take out of it what they can get and let the rest go. They ruin the mine Bear in mind always that for the short run you don't have to pay mine rent. You must always consider what options a man has when you are trying to regulate him Now in the case of anthracite coal again, the price-fixing was not a difficult problem because there again, a few great mining companies, a few big deposits. When you got to bituminous you had thousands of mines scattered over big areas and when you got to wheat and flour you had millions of farmers, a great multitude of mills, and so on You have got a different problem.

In the case of wheat and flour, therefore, it was necessary, in order to keep the farmers producing wheat, that the fixed price should be a high price. In order to keep the millers in the trade going, and there are a lot of them, they had to be dealt with pretty diplomatically They were pretty patriotic A lot of them contented themselves with less profits But the margins were cut rather too thin in certain cases

They met one problem, that of fixing differential quality in wheat and the possibility of a variation in price, variation in differential, by providing that there should be a standard flour containing fixed percentages of different grades of wheat which helped them to keep the differential fixed in price. On the whole, that worked pretty well. There was in the winter of 1917-1918 a slight increase in the acreage of winter wheat which was a pretty good test. With it all rationed you couldn't buy a barrel of flour any more. If you had a barrel of flour you were expected to turn it back to the retailer and take less than that bit by bit and you were expected to mix your flour with barley or other things for making bread I wonder how many of you remember how bad the bread got that summer at the Cosmos Club? We carried it through, we made a sort of religion of it, and you can have a thing of that sort in war time Why? In war time as long as the people's hearts are in the war they will put up with a lot of things Notice the difference in war time, moreover, when you are fixing prices you are holding them down. In peace time the effort has been to hold them up

Now in soft coal, down to the winter of 1917 they made pretty ghastly mistakes They cut the margins much too fine, and they cut the price too low. You had thousands of scattered mines and they are hard to control They hadn't allowed any differentials in coal There was one fixed price for bituminous coal There was one case where a company having a mine with a high ash content and one with a high number of thermal units just closed down the good mine and used the mine with high ash content because there was no differential allowed The trade was used to making differentials in coal on the basis of BTU's Follow trade practices just as far as you can, study trade practices, get intelligent men of the trade in with you Learn about their system of private wires, their ways of getting communication, their ways of collecting information. Find out where the sore spots are going to be, consult the trades. They will cooperate with you magnificently Close cooperation with men, yes, but use their brains as well. There's one of your best resources, the brains of the able men in the mercantile field. Even bankers have brains.

I am going to refer to a document I have here, a photostatic copy of which I will give you. It is a paper I read before the American Economic Association at the meeting of December 1917 It goes into a great deal of detail. I imagine you have the American Economic Review which contains the proceedings, published in March, 1918, for the December meeting, but I will give you this additional copy Mr Harry Garfield, who took charge of that coal situation when it was pretty bad, is a very urbane gentleman, and one of the things that was needed was a first rate gentleman to smooth down ruffled tempers. He did that nicely and he made concessions. I haven't followed thoroughly that soft coal control after December of 1917, but I think it got very much better under his policies which were in the direction of making more allowance for human nature, conciliating, and widening the margins

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Now one thing that you want to be perfectly clear about is that your objective is winning a war. Your objective is not to keep people from making some money The Government is altogether too much concerned with just price rather than functional price. You are concerned with functional price, the price that will let the processes go on That's one of the appalling things about government when it comes into economic life It is animated by medieval conceptions. Government control of economic life grew out of war and war was a state of nature in the middle ages and early modern times. In the 19th century the market became the great coordinator and broke away from these medieval restraints. Now this last great war made Government very powerful and this depression brought Government actively into economic control again on the basis of medieval and early modern economic fallacies

My friend Senator Gore, the blind Senator from Oklahoma, one of the great minds of the country, in his speech which he had to extemporize at the time of the Thomas Amendment, combating the debasement of the dollar and other things, said: "Henry the VIII approached total depravity as nearly as the imperfections of human nature would allow But the vilest thing that Henry ever did was to debase the coin of the realm!" If you read Henry's argument and explanation of that you will find that he was concerned with promoting foreign trade and improving the economic situation of England by making easier money All these things have been tried before, and, above all, price-fixing on the theory of just price. Nobody has any right to try fixing prices who hasn't mastered the theory of economic equilibrium in terms of price, and before tackling price fixing you want to master what the great masters of economics already have done with the analysis of free prices. In particular I am going to name two or three things the price-fixer ought to read before he does anything Read John Bates Clark's "Distribution of Wealth", a great book published in 1899, a picture of the economic equilibrium Read the chapters on cost of production in Bohm-Bawerk's "Positive Theory of Capital" and read the chapter on cost of production in Wieser's "Natural Value " You might read, too, a book by Schaeffle called the "Quintessence of Socialism " There is some discussion of functional price in that. First, learn what prices do, and why free prices are needed

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DISCUSSION

Colonel Jordan: Gentlemen, if there are any questions you would like to ask Dr. Anderson will be very glad to answer them. We give this privilege to our guests as well.

Q. In addition to our problem of price control we have studied somewhat the study of control of profit. Would you care to speak briefly on the matter as to whether or not the control of profit in war is feasible in its relationship to the price control?

A. I differentiate between a long war and a short war. If you have got a short war what you want is quick results at the beginning. You want men to make great shifts, some to put up new plants, some turn to doing another thing, and there will be risks in that. You had better let them see the real incentive. As a war goes on further and further you have got your big adjustments made, then you can increase the pressure. You see somebody making too much profit, and you can take cognizance of that, but I think the best way to do it is with the tax machinery rather than with direct regulation of profit. You have got to have profit taxes, and you will have war profit taxes, excess over what they had been accustomed to making, and things of that sort. Now that links up with the question, too, of whether you want to finance a war by borrowing or by taxation. I expressed an opinion here three years ago. When you want prices to go up you want activity to go on and you don't want the industries that are losing ground to be under further pressure of unreasonable taxation. But as the war goes on longer and longer, more taxes, less borrowing. I think that where they undertook the limitation of profit in 1917-1918, especially on that cost-plus basis, what they got was much bigger costs than they otherwise might have had. Haven't you reached the conclusion cost plus contract wasn't a good one? Here is a man who is efficient and good, very capable; here are other men not so good, and you are using both. Why shouldn't this man make a bigger profit than the others? You are paying him the same price and he is doing it cheaper, and he is using less of the resources of the country in doing it. But extraordinary profits we would go after with taxation. This would be my guess.

Q. Dr. Anderson, in the fixing of prices which scheme do you think would be the most feasible at the outbreak of emergency, to get hold of certain raw materials, commodities, wages you might say, as the Government saw fit, or to place a ceiling over everything at a certain date? In other words, piece-meal or fixing the entire price structure at one time? Which would you think would be the most feasible?

A. Fixing the entire price structure at one time would, in my opinion, be taking away the whole flexibility of the price system. I should do it piece-meal where necessary. I should not do it unnecessarily. I should do it primarily in the case of scarce commodities needed for war. You see, you have got to accompany each move in prices with compensatory moves to supply some substitute for what prices do. In particular, you have got to ration things. You have got to see that they go to the right places. You just can't do that for the whole system. There is no brain big enough to do it and a collection of brains working at cross purposes, as they often do, will be worse than one.

Q. May I make a remark? My expression was faulty. I gave you to understand wrongly. What I meant was to put a ceiling over prices and they can fluctuate up and down beneath. That is quite different.

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A. You have got to do it by some very arbitrary way and what you find is the real reason for some prices going much higher perhaps than you anticipated, others not nearly so high. You can't make a big enough plan. You want to leave the general functioning going on. The human organism is not a perfect analogy. There are times though when we will devise substitutes for certain organic functioning. There are extreme cases of diphtheria where the old doctors used to fix another way of breathing. I don't know whether they do that any more, they probably don't have to with the serum. But you have got such a complicated thing. A man may take a bluéprint of the liver, make it from the outside not knowing what the liver is, and it does seem to have all those veins. Why not put a big vein or put a tube through? But you can't do it that way. In my opinion you must rely in war primarily upon your price system, the general going on of economic life uncer the price system and the things that you want to strike at are the things where there is military reason for it. One other thing, there are many indirect ways of doing it. You don't want your labof and other resources diverted to a lot of peace-time construction in war, but we handled that in various ways. For another thing, we controlled the capital market. We got the bankers and investment bankers busy in holding down non-essential financing. A man wanted to borrow money to go into construction, and that had to be very carefully passed upon. The production was very great. There are very many ways of control, and the most dangerous way of control of all is price fixing. I would use some price fixing here and there but you have got your adjustment of comparative taxes and borrowing, direct control of the capital market, holding down nonessential borrowing, your rationing of supplies acting through industrial organization where it exists and where it is highly concentrated. There are many devices, and universal price fixing would be the worst, I think.

Q. We are very much worried in time of war about the moral system of the men in the front line if they get an idea from home that their families aren't getting enough to eat and that prices have gone beyond their reach. It is a very difficult thing to divert their attention to the front entirely and not keep them worried about their own people. How can we have any assurance that that situation won't arise again unless we have price fixing to some extent?

A. In the case of great essentials like wheat and so on you can do something along the lines I have indicated. You could do as we did in this last war. You can do a good deal by generous provision for the helpless ones that the soldier left behind. Incidentally, we took a lot of care not to send men where we could avoid it who had dependents who really were helplessly dependent upon them. Then, as I say, by this general matter of a tax program, progressive increases in taxes, reduction in borrowing as your war goes on, you hold prices down by that. But even if this consideration led you it wouldn't do to go further in price fixing than you would otherwise go. You can still limit it to the essentials of life, not to all prices. I don't see any objection to letting luxuries go way up high if at the same time you are holding down other industries producing luxuries and limit the raw materials that can come to them. One question came up, by the way: Should they make pianos in 1917? Some of those studying it decided yes, for export to the Argentine in exchange for wheat to go to England, all right for pianos for that purpose but not otherwise. We commandeered a lot of the men who were making pianos because they could also make airplane wings and things of that kind. Some pianos to go to

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the Argentine to get wheat to go to England — it would be along that line. I want the Army itself to study what is essential for the Army and to make your program a program concerned with winning a war and not with regulating people.

Q. Dr. Anderson, in the case where price is determined by world market are you in favor during the war of the Government entering into the affair and asserting economic pressure to control those prices? In the commodities where the price is normally determined by a world market are you in favor of the Government entering into the affairs during war and exerting economic pressure to control those prices?

A. It depends upon our circumstances. Suppose it is a commodity, let's say rubber which we don't produce here, and what about it? The Government wants to put the American price below the world price, and we don't get rubber. Now the Government can, on the other hand, if the need is great enough and the war severe enough, say to the men making materials: "You can only have so much." We will control the supply of rubber, we will ration it and that would tend to hold the price down. To the extent that you get into a field where the main price control is outside the country unless you happen to be allied with the powers that produce that thing, you can't do very much, can you?

Q. That's quite true. However, take the case of tin during the World War when the British controlled the tin market. They were holding the price up. Our Foreign Legion went over there, we had been talking to them, and they refused to lower prices. We controlled certain things and we had been giving the allies the same price we gave our own people. If they didn't come down on tine we said that we would charge them a higher

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price. The result was that the price of tin was lower. There are certain things that can be done. I am asking whether you are in favor of doing that.

A. It will differ from case to case. It will be a question of whether you were going to improve a situation or make an international discord that might make it worse. You would have to judge each case on its merits. It is a problem for the State Department primarily and the Army secondarily. Is that a satisfactory answer?

Q. I get it that you are in favor of applying it when it is feasible.

A. With the very great qualification always that if you put that price, say in case of rubber, down to a point where the natives of the British and Dutch East Indies are not interested and the supply is going to fall off, no. Watch that because you want rubber.

Colonel Jordan: Admiral Conard, would you care to say something?

Admiral Conard: No, I haven't any particular comments because I feel more or less familiar with Dr. Anderson's views, having read his circular lectures, and all that you have said today you have said before, and I thoroughly agree with your point of view.

Dr. Anderson: May I for your record refer to these two publications which I have here: this paper of 1917 called "Value and Price Theory in Relation to Price-Fixing and War Finance," and this paper of 1936, The Chase Economic Bulletin No. 1, "Governmental Economic Planning and Prices", concerned especially with governmental price-fixing in time of peace. The two together will give my rounded view of the thing.

Colonel Jordan: Dr. Anderson, I want to express the appreciation of the College for your coming here and talking to us. It has been a great pleasure to have had you, sir.