The risk is that we will drift or be led into a new pattern, downgrading collective bargaining and the free market system. The proper role of Government under our political and economic system should be to create and maintain the market machinery in good working order—not undertake to substitute for it, or confuse the issues of its imperfections by admonitions that it do better.

This is precisely the risk that we face today. We do not believe that the guideposts can restrain inflation in a period of tight labor and commodity markets, nor do we believe that they should be relied upon for this purpose even if they were effective.

From past experience, we would expect that the failure of the guideposts will lead the control-minded policymakers in the administration to seek more direct and damaging restraints on private economic decisionmaking.

The debate which would certainly follow a forthright request for authority to impose direct controls would have a healthy effect. If the administration believes controls are needed, we would prefer controls imposed and limited by statute to the ambiguous and arbitrary exercise of economic power now assumed by the administration without sanction of law or provision for redress of grievances.

A full-scale study within the Congress, such as we have urged the Joint Economic Committee to undertake, might convince well-meaning proponents of the enforcement of the guideposts of the long-run perils to which systematic interference with the market mechanism exposes our free economy. If such a debate did nothing else, however, it would make abundantly clear the technical difficulties which stand in the way of devising a satisfactory formula governing the changes in wages and prices in our economy.

VARIETY OF EXCEPTIONS

The complexity of the guidepost concept is demonstrated by the fact that there are a variety of exceptions which are not as clearly dealt with as behavior under the general rule. Since the average rule is more easily administered than the numerous exceptions, inefficiencies in allocation of resources may result, as Professor Musgrave pointed out to the committee.

The Council's decision to scrap the 5-year moving average as an appropriate indication of the general productivity trend and to retain instead the 3.2-percent guidepost of last year illustrates another inherent weakness of the guidepost concept: the problem of developing a measure of the trend growth of productivity. What time period truly represents the trend value of productivity in the U.S. economy? Should this value reflect only output per man-hour or output per unit of total factor input? Should the national increase in productivity include the large gains in agricultural production along with the smaller increases in the nonagricultural sectors? Should wages go up 3.2 percent in industries which experience substantially larger productivity increases? These are a few of the difficult questions which should be debated. Depending on the answers, the value of the wage-price guidepost would be vastly different.

Another difficulty with the guidepost concept is that the approach lends itself more readily to markets in which a few firms are dominant and wage settlements involve large contracts. Inescapably, their enforcement becomes selective and discriminatory.

The guideposts also miss the mark in concentrating on industries rather than individual firms, where much of the wage determination and price setting actually occurs. The concept of an industry of homogeneous enterprise has been blurred in recent years. Even if an industry could be clearly identified, the position of individual firms within that industry differ markedly from one another.

The guideposts are intended to deal with cost-push inflation caused by market power, even in the absence of excess demand. The argument that specific industries or unions exercise a high degree of arbitrary market power is often overstated. Among other factors, it frequently overlooks the competition of domestic substitute products as well as imports. For the most part, price or wage increases in these highly visible situations are a response to rising demand and limited supply, just as is the case with other industries.

THE EUROPEAN EXPERIENCE

In any event, spreading wage and price increases are only possible if a rapidly increasing supply of money supports an excessive level of aggregate demand in the economy generally. If aggregate demand is held within nonin-