

comment from each of you on whether or not you feel that escalator clauses are or are not inflationary?

Mr. WALLICH. I think Mr. Reuther must have been arguing on the assumption that there are wide profit margins that permit absorption of above productivity wage increases. Moreover, with respect to his own industry, productivity increases may well be above average, so that it would be possible even without reduction in profit margins to absorb normal wage increases, plus an escalator.

But for the economy as a whole, it seems perfectly clear that escalator clauses will be inflationary, unless we are to assume that profits can be continually squeezed. The guideposts made very clear that labor as a whole, if income shares are to be maintained, cannot get wage increases in excess of productivity gains. If those are 3 percent and we give labor 7 percent, then the only way to get back to the 3 percent that labor can get is to have inflation of 4 percent. That would be the result of escalating.

If then, we further escalate the 7 percent to 11 percent because of the 4-percent inflation, what we do is to escalate the inflation as well as wages. I see no alternative.

Mr. LEKACHMAN. I think, in general, I agree with Mr. Wallich once more on the effect of escalator clauses, but I would stop short of saying that because they have an inflationary tendency they are necessarily to be resisted at all cost. They do embody a measure of protection. If you like, you can even think of a series of labor contracts containing escalator clauses as putting some pressure upon the Government to use the kind of fiscal policies which would make them inoperative.

I don't think that that is necessarily what Mr. Reuther had in mind, but it might be indeed an effect of such a widespread writing of contracts.

Mr. COLM. I don't know what Mr. Reuther had in mind, but there is one fact. The way the escalator clauses are written and operated, they do put a timelag between the price rise and the wage increase. To that extent, whether they are inflationary or not may be a question of semantics. They are more inflationary than if there were no wage increase. But they are a factor slowing down the transmission of the price rise through the economy.

For instance, the British during the war managed the price index to make the most use of this price lag, so that actually apparent escalation was actually a mechanism designed to slow down inflation. Some of the unions oppose the automatic escalation because they think by reopening negotiations they can get more, trying to anticipate future price increases. This would certainly be more inflationary.

We also should consider why we have price increases. If we have a price increase because of lack of fiscal measures, then the price increase acts in a way as a crude substitute for a tax. And the more groups are protected, the smaller those are, who find that they have to carry the burden. In that respect, I would say full cost of living adjustments add to inflationary pressure. But much depends on the mechanism of how they operate, the time lag between the actual price rise, the reporting of the index, and the application to the next payment.