While the 4-percent target has been consistently maintained by the recently retired Council (save possibly for the brief wavering in 1966 just noted), it is not yet clear whether it will be continued by the new one, or indeed whether *any* specific target will be named. For the purpose of this discussion, however, we are going to assume that is still the official target.

The dilemma

Given this assumption, we submit that the United States is impaled on the horns of a dilemma: its employment and price-level objectives are incompatible. Like a modern Tantalus, it strains for the alluring fruit of full employment without inflation, but the prize continues to elude its grasp.

The dilemma arises from the tendency for increases in labor costs to outrun productivity gains, hence for the price level to advance, when the unemployment rate is at or below the target figure. The rate compatible with price-level stability is substantially *above* that figure. As things now stand, the country can enjoy either full employment or a stable price level, but not both.

Since unemployment and inflation are alike evils to be minimized, and since they are in substantial degree alternative (the more of the one, the less of the other), we confront the problem of a "trade-off" between them. This problem presents two questions, one of fact, one of policy. The factual question concerns the *terms* of the trade-off: what is the relation between unemployment and inflation? The second concerns *policy:* given these terms, at what point is more unemployment better than more inflation, or vice versa?

We deal in this chapter with the factual question only. Obviously, the policy decision depends in large measure on the terms of the trade-off. How much acceleration of the inflation rate is associated with a given reduction in the unemployment rate? How is this inflation response related to the *level* of unemployment from which this reduction is effected? Unless we have a fix on the answers to these questions, the determination of policy proceeds in the dark.

I. Relation Between Unemployment and Increases in Labor Compensation

We can explore the trade-off problem by analyzing first the historical relation between the unemployment rate and the rate of rise in hourly labor compensation.

For this purpose, history means the postwar period, since comprehensive figures on hourly compensation were not available earlier. But not all of the period is properly includable. Some portions were clearly abnormal. There were wage explosions in 1946–47 following the release of World War II controls, and in 1950 following the outbreak of the Korean war. There were wage controls during that war, affecting the years 1951–53. There were recessions in 1949 and 1954. In fact so little of the postwar prior to 1955 can be considered indicative of the normal relation between unemployment and increases in compensation that we begin our analysis with that year.