

which says that the profit margin on total costs should maintain a stable relation thereto. Certainly this is implied in the statement that—

“Every management with some market power must ask itself:

Is a price increase justified by increases in costs? Or is it an attempt to take advantage of prosperity to widen profit margins?”³⁷

If this interpretation is correct, it means that the price guideposts are not violated by an increase in the absolute amount of profit proportional to the rise in costs; what is proscribed is an increase in its relative amount. So long as the percentage margin on costs remains constant, any price effect from a rise in the absolute amount of profit is simply a byproduct and reflection of a rise in the underlying costs themselves. It is a problem for cost control, not for price control.

III. DIFFERENCE BETWEEN WAGE RESTRAINT AND PRICE RESTRAINT

It is a political axiom in most Western countries, and certainly in the United States, that any attempt to restrain wage increases, whether by direct action or by exhortation, must be accompanied by parallel measures to restrain prices. For the hortatory approach, this means that all admonitions to well-doing must be strictly bilateral, and must convey the impression that industry and labor are equally responsible for inflation and equally able to control it.

The propagation of this myth by politicians, and by economists in political office, has given rise to a delicate semantic balancing act, of which we have seen examples in the preguidepost exhortations quoted above. Pleas for wage and price restraint are invariably conjoined, usually in the same paragraph, often in the same sentence. You can read dozens of them without findings so much as a hint that one factor is more important than the other.

Notwithstanding this ritual neutralism, there is a profound difference in the potentialities of wage and price restraint. This arises from the fact that wage restraint affects the major cost of production, whereas, as already noted, price restraint affects the profit margin on this cost (and others). The price impact of changes in labor costs can be, and historically has been, far greater than the impact of variations in profit margins.

Relative profit margins are subject to fluctuation, depending on economic conditions, but they show no tendency to increase secularly. While the fluctuations contribute at times to raising prices and at others to lowering them, over the long run they are neutral. They are not, therefore, a cause of sustained inflation. Contrast this with wages. Labor costs per unit of output can rise year after year over long periods, with growing cumulative effect.

Margin variance

We can illustrate this statement about the behavior of relative profit margins by reference to the corporate system, the only sector of the economy for which separate profit figures are available. The following chart shows the picture for the past decade (p. 32).

³⁷ *Ibid.*, p. 93. It is true, of course, that in recent years the Council has exhorted industry to reduce profit margins. Thus in 1967 it observed that “The public interest requires that producers absorb cost increases to the maximum extent feasible” (Economic Report, 1967, p. 133). In 1969 it suggested that business should absorb “a share of unavoidable increases in costs through acceptance of lower profit margins” (*Ibid.*, 1969, p. 59). We construe this as evidence of the Council’s desperation over the collapse of wage restraint (of which more later) and the accompanying inflation, not as a revision of the basic philosophy of the guideposts.