Nixon, Price Controls, and the Gold Standard

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Essay

[Following the Kennedy-Johnson administration in the United States, there was a massive effort to manage the marketplace, in part by controlling wages.] This initiative was not the handiwork of left-wing liberals but of the administration of Richard Nixon, a moderately conservative Republican who was a critic of government intervention in the economy. As a young man during World War II, prior to joining the navy, Nixon had worked as a junior attorney in the tire-rationing division of the Office of Price Administration, an experience that left him with a lasting distaste for price controls.

What, then, were the forces that led Nixon to try to impose government management on the most basic elements of the market? Certainly, economic matters were hardly his passion. That was reserved for foreign policy. Even foreign economic policy did not much interest him. There was a memorable time during some moment of international monetary perturbation when he rudely suggested exactly what should be done with the lira. As for domestic economics, he liked to give his radio talks on economics at noon on Saturdays, because he was convinced that the only listeners would be farmers riding their tractors, and they were likely, in any event, to be his supporters.

For one thing, whatever the effects of the Vietnam War on the national consensus in the 1960s, confidence had risen in the ability of government to manage the economy and to reach out to solve big social problems through such programs as the War on Poverty. Nixon shared in these beliefs, at least in part. "Now I am a Keynesian," he declared in January 1971 -- leaving his aides to draft replies to the angry letters that flowed into the White House from conservative supporters. He introduced a Keynesian "full employment" budget, which provided for deficit spending to reduce unemployment. A Republican congressman from Illinois told Nixon that he would reluctantly support the president's budget, "but I'm going to have to burn up a lot of old speeches denouncing deficit spending." To this Nixon replied, "I'm in the same boat."

While Nixon may have philosophically opposed intervention in the economy, philosophy took a rear seat to politics. He had lost very narrowly to John Kennedy in 1960 -- 49.7 to 49.5 percent of the popular vote. He sometimes blamed the state of Illinois, whose electoral votes had made all the difference and where the Chicago Democratic machine was known for its effectiveness in getting out all possible voters, dead as well as living Kennedy won Illinois by just 8,858 votes. But Nixon certainly believed that mismanagement of the economy had also cost him the election. "He attributed his defeat in the 1960 election largely to the recession of that year," wrote economist and Nixon advisor Herbert Stein, "and he attributed the recession, or at least its depth and duration, to economic officials, 'financial types,' who put curbing inflation ahead of cutting unemployment." Looking toward his 1972 reelection campaign, Nixon was not going to let that happen again. And he had to pay attention to economics. Despite the optimism about government's ability to manage the economy, economic conditions had begun to deteriorate. The inflation rate, which had been 1.5 percent at the beginning of the 1960s, had risen to 5 percent. Unemployment was also up from the 3.5 percent level of the late 1960s to 5 percent.

So the central economic issue became how to manage the inflation-unemployment trade-offs in a way that was not politically self-destructive; in other words, how to bring down inflation without slowing the economy and raising unemployment. One approach increasingly seemed to provide the answer -- an income policy whereby the government intervened to set and control wages, whether in hortatory words or legal requirements. Such policies had become common in Western European countries. In the 1970s, the Democratic Congress provided the tools by passing legislation that delegated authority to the president to impose a mandatory policy.

The administration remained overtly dedicated to markets. But there were those in it who believed that the "market" was more an idyll of the past than an accurate description of how the current economy functioned. To them, the economy was like the question that Lenin had expressed -- Kto kvo? -- Who could do what to whom? That is, they saw the economy "as organized by relations of power, status, rivalry and emulation." Government intervention was required to bring some greater balance to the struggles for power between strong corporations and strong unions that would drive the wage-price spiral upward.

A critical push toward an income policy came from Arthur Burns, whom Nixon had appointed to be chairman of the Federal Reserve. Burns was a well-known conservative economist; Nixon paid special attention to Burns because he had warned Nixon in 1960 that the Federal Reserve's tight monetary policy would accentuate the economic downturn and thus threaten Nixon's chances in the race against Kennedy -- which is exactly what had happened. Now, a decade later, in May 1970, Burns stood up and declared that he had changed his mind about economic policy. The economy was no longer operating as it used to, owing to the now much more powerful position of corporations and labor unions, which together were driving up both wages and prices. The now-traditional fiscal and monetary policies were seen as inadequate. His solution: a wage-price review board, composed of distinguished citizens, who would pass judgment on major wage and price increases. Their power, in Burns's new lexicon, would be limited to persuasion, friendly and otherwise.

Further reinforcement of the pressures toward control came with the recruitment of former Texas Democratic governor John Connally to fill the critical slot of Treasury secretary. The forceful Connally had no philosophical aversion to controls. Indeed he did not seem to have strong feelings one way or the other on economic policy. "I can play it round or I can play it flat," he would say. "Just tell me how to play it." What Connally did like was the dramatic gesture, the big play; and grabbing inflation by the neck and shaking it out of the system would be such a move.

A second issue was also now at the fore -- the dollar. The price of gold had been fixed at $35 an ounce since the Roosevelt administration. But the growing U.S. balance-of-payments deficit meant that foreign governments were accumulating large amounts of dollars -- in aggregate volume far exceeding the U.S. government's stock of gold. These governments, or their central banks, could show up at any time at the "gold window" of the U.S. Treasury and insist on trading in their dollars for gold, which would precipitate a run. The issue was not theoretical. In the second week of August 1971, the British ambassador turned up at the Treasury Department to request that $3 billion be converted into gold.

With inflation rising, the clamor to do something was mounting in both political circles and the press. At the end of June 1971, Nixon had told his economic advisors, "We will not have a wage-price board. We will have jawboning." But resistance to an income policy weakened with each passing month. The climax came on August 13-15, 1971, when Nixon and 15 advisors repaired to the presidential mountain retreat at Camp David. Out of this conclave came the New Economic Policy, which would temporarily -- for a 90-day period -- freeze wages and prices to check inflation. That would, it was thought, solve the inflation-employment dilemma, for such controls would allow the administration to pursue a more expansive fiscal policy -- stimulating employment in time for the 1972 presidential election without stoking inflation. The gold window was to be closed. Arthur Burns argued vociferously against it, warning, "Pravda would write that this was a sign of the collapse of capitalism." Burns was overruled. The gold window would be closed. But this would accentuate the need to fight inflation; for shutting the gold window would weaken the dollar against other currencies, thus adding to inflation by driving up the price of imported goods. Going off the gold standard and giving up fixed exchange rates constituted a momentous step in the history of international economics.

Most of the participants at the Camp David meeting were exhilarated by all the great decisions they had made. During their discussions, much attention was given to the presentation of the new policy, particularly to television. President Nixon expressed grave concern that if he gave his speech during prime time on Sunday, he would preempt the tremendously popular television series Bonanza, thus potentially alienating those addicted to the adventures of the Cartwright family on the Ponderosa ranch. But his advisors convinced him that the speech had to be given before the markets opened on Monday morning, and that meant prime time. A few of the advisors would recollect that more time was spent discussing the timing of the speech than how the economic program would work. Indeed, there was virtually no discussion of what would happen after the initial 90-day freeze or how the new system would be terminated.

Nixon's chief of staff, H.R. Haldeman, went in to see the president privately at Camp David the evening before his speech. "The P. was down in his study with the lights off and the fire going in the fireplace, even though it was a hot night out," Haldeman wrote in his diary. "He was in one of his sort of mystic moods." Nixon told Haldeman "that this is where he made all his big cogitations.... He said what really matters here is the same thing as did with [Franklin] Roosevelt, we need to raise the spirit of the country; that will be the thrust of the rhetoric of the speech.... We've got to change the spirit, and then the economy could take off like hell." As he worked on the speech, Nixon tormented himself, worrying whether the headlines would read NIXON ACTS BOLDLY or NIXON CHANGES MIND. "Having talked until recently about the evils of wage and price controls," Nixon later wrote, "I knew I had opened myself to the charge that I had either betrayed my own principles or concealed my real intentions." But Nixon was nothing if not a practical politician, as he made clear in his masterful explanation of his shift. "Philosophically, however, I was still against wage-price controls, even though I was convinced that the objective reality of the economic situation forced me to impose them."

Nixon's speech -- despite the preemption of Bonanza -- was a great hit. The public felt that the government was coming to its defense against the price gougers. The international speculators had been dealt a deadly blow. During the next evening's newscasts, 90 percent of the coverage was devoted to Nixon's new policy. The coverage was favorable. And the Dow Jones Industrial Average registered a 32.9-point gain -- the largest one-day increase up to then.

The Cost of Living Council took up the job of running the controls. After the initial ninety days, the controls were gradually relaxed and the system seemed to be working. But unemployment was not declining, and the administration launched a more expansionary policy. Nixon won reelection in 1972. In the months that followed, inflation began to pick up again in response to a variety of forces -- domestic wage-and-price pressures, a synchronized international economic boom, crop failures in the Soviet Union, and increases in the price of oil, even prior to the Arab oil embargo. Nixon, under increasing political pressure from the investigations of the Watergate break-in, reluctantly reimposed a freeze in June 1973. Government officials were now in the business of setting prices and wages. This time, however, it was apparent that the control system was not working. Ranchers stopped shipping their cattle to the market, farmers drowned their chickens, and consumers emptied the shelves of supermarkets. Nixon took some comfort from a side benefit that George Shultz, at the time head of the Office of Management and Budget, identified. "At least," Shultz told the president, "we have now convinced everyone else of the rightness of our original position that wage-price controls are not the answer." Most of the system was finally abolished in April 1974, 17 months after Nixon's triumphant reelection victory over George McGovern -- and four months before Nixon resigned as president.

In retrospect, some would call the Nixon presidency the "last liberal administration." This was not only because of the imposition of economic controls. It also carried out a great expansion of regulation into new areas, launching affirmative action and establishing the Environmental Protection Agency, the Occupational Safety and Health Administration, and the Equal Employment Opportunity Commission. "Probably more new regulation was imposed on the economy during the Nixon administration than in any other presidency since the New Deal," Herbert Stein ruefully observed.

Only one segment of the wage-and-price control system was not abolished -- price controls over oil and natural gas. Owing in part to the deep and dark suspicions about conspiracy and monopoly in the energy sector, they were maintained for another several years. But Washington's effort to run the energy market was a lasting lesson in the perversities that can ensue when government takes over the marketplace. There were at least 32 different prices of natural gas, a rather standard commodity, each of whose molecules is based on one atom of carbon and four atoms of hydrogen. The oil-price-control system established several tiers of oil prices. The prices for domestic production were also held down, in effect forcing domestic producers to subsidize imported oil and providing additional incentives to import oil into the United States. The whole enterprise was an elaborate and confusing system of price controls, entitlements, and allocations. It was estimated that just the standard reporting requirements for what became the Federal Energy Administration involved some 200,000 respondents from industry, committing an estimated five million man-hours annually.