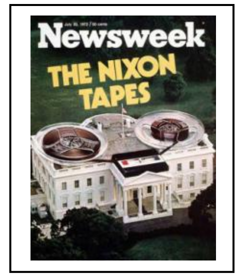

Mitchell's Musings 9-16-13: Before Nixon's Second Freeze

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In last week's musing, we utilized newly-released Nixon "White House" tapes to examine the decision to impose a second freeze on June 13, 1973 as part of the wage-price controls program then in effect.[1] Some general background on the program and that freeze was included in that musing. A key aspect of the freeze decision was the increasingly-dramatic Watergate affair which by then had already caused resignations of key administration officials. The newly-released tapes suggest that despite whatever outward appearances were being projected, White House attention was heavily focused on Watergate; every other policy – domestic or foreign – was being viewed from a Watergate perspective. Specifically, each policy was being evaluated for its capacity to divert public attention from Watergate and to project an image of a president still in charge and dealing capably with national problems.

The wage-price controls program was no exception to this Watergate focus. Indeed, wage-price policy was increasingly becoming an instrument of political persuasion. Of course, even under more normal circumstances, *any* presidential policy has a political dimension and the controls program – which began in August 1971, well before Watergate – had also been no exception to that generalization. However, there was a major difference between the controls decision of August 1971, which began with a wage-price freeze, and the second (price-only) freeze of June 1973.

Prior to the first freeze and to the more general decision to impose controls, there was a divergence of views among economic advisors inside and outside the administration about a wage-price regulatory system. Some economists consulted by President Nixon did not favor the decision, especially those with a "free-market" orientation. But others thought some kind of wage-price intervention would be helpful in combating inflation.

The Kennedy-Johnson administration had earlier experimented with a voluntary wage-price guideposts program. Although that effort ultimately fell apart, there was some empirical evidence suggesting it had a temporary inflation-retarding effect (but was later overwhelmed by Vietnam War-era excess demand). Various European countries were experimenting with forms of "incomes policy" under which union and management groups and national governments agreed to standards of anti-inflation behavior.

There was a tendency to view price and wage setting as "administered." Key union settlements set a general pattern of wage increases. Major firms then had the market power to pass through the resulting cost increases, adding a profit markup. If a wage standard was set, and if firms were held to fixed markups, the inflation process would be controlled.

Because of these earlier and contemporary policies and lines of thinking, some prominent American economists believed that some version of wage-price policy – combined with more conventional macroeconomic measures – might be helpful in reducing inflation. Or, at least, they thought it was a

[1] http://www.employmentpolicy.org/topic/12/blog/mitchell%E2%80%99s-musings-9-9-13-nixon%E2%80%99s-wage-price-controls-and-their-watergate-entanglement.

policy experiment worth undertaking. While it is impossible to know the degree to which President Nixon weighed politics versus economic advice at the time, there was a diversity of economic perspectives around in 1971. So a presidential decision to go the controls route was not going against a virtual unanimous opinion in the economics profession. The opinions were in fact mixed.

In contrast, the second freeze had little economic support, either from official advisors of the President or from outside economists. Last week's musing noted reference on White House tapes recorded just after the June 13, 1973 TV speech by the President to opposition from Nixon's economic advisors. Treasury Secretary George Shultz and Herbert Stein, chair of the President's Council of Economic Advisors, were opposed and their advice was being overridden. However, various non-economic aides were telling the President that his speech had been magnificent and would demonstrate to the country that the White House was taking care of national business.

Of course, with the benefit of hindsight, we know that Watergate did not melt away following the freeze speech. We know that the freeze, and the Phase IV wage-price controls that followed, did not have a lasting anti-inflation effect. Indeed, the complex energy (oil) price controls that evolved in Phase IV and were retained after the larger controls program was abandoned led ultimately to shortages and gasoline lines under President Carter. Those aides who were talking to the President immediately after the speech could not have known of these later developments. Nonetheless, there was too much of the "yes-man" in those post-speech conversations from the aides. In my view, there was way too much. The President was being told what he wanted to hear and not what he needed to hear.

Next week's musing will deal specifically with the televised speech itself. By way of preview, however, the speech was certainly serviceable in terms of style of delivery. But it was not the spellbinder that the post-speech evaluations by presidential aides might lead one to believe. It was not the kind of speech destined to reset the national agenda, particularly since its content went against the advice of both internal and external economic opinion.

That observation leads to an interesting question. What was the President hearing from his advisors *before* the TV speech? What was the evolution of the advice leading up to the speech? Among the newly-released tapes, we have some indication of that evolution. I have posted some telephone conversation excerpts from before the speech at https://www.youtube.com/watch?v=RdKK6lKmXYE.

The first brief conversation is a phone call of April 30, 1973 from Treasury Secretary George Shultz immediately after the announcement by Nixon of the Watergate-related resignations of John Ehrlichman and H.R. ("Bob") Haldeman. Shultz calls to express his sympathies to the President. The President is clearly grateful for the call and for Shultz's remarks. As best we can tell from the call and Nixon's voice, the President is emotionally upset and perhaps not fully in control. But he insists that he will come to a labor-management committee meeting Shultz will be running that was part of the Phase III controls program. Nixon wants to show he is still in charge and remains an active participant in the program.

A second call – this one with Office of Management and Budget (OMB) Director Roy Ash – took place on May 12, 1973. By this time, it appears that some discussion about imposing a second freeze is beginning to occur. But Ash is opposed to the idea as are Shultz and Stein. The freeze talk seems to be coming from John Connally. Connally, a Democrat, was Shultz's predecessor as Nixon's Secretary of the Treasury. (He was no longer a Nixon administration official but – after returning to Texas politics for a time – had switched to being a Republican at around the time of this call.)

The main additional support for a Connally-type step is Alfred Sindlinger, a pollster used by the President who thinks a freeze would have a good "psychological" effect on the country. Exactly what a psychological effect (as opposed to an economic effect) was supposed to mean is not clear from the call. But it seemed to involve the idea of the President showing he was still running the country and taking care of the public's business. Ash notes, however, that it is easier to get into a freeze than to chart a graceful exit. And Nixon notes that a freeze was tried back in 1971 and now he seems uncertain that it had been a good idea.

The third conversation of May 20, 1973 takes place between President Nixon and his Chief of Staff Al Haig. Most of the conversation is related to the Watergate affair but economic matters come up in the excerpt provided. Haig says Phase III wage-price controls now have to be evaluated in the light of Watergate. Connally wants a freeze, but Haig can't get Shultz and Stein to move away from opposition to any such move. Haig is not necessarily in favor of a freeze but he wants the economic advisors to think politically.

Nixon says that sometimes you have to do things for political reasons - even if there are no good economic justifications - and his economic advisors, including Ash, should recognize that fact. Haig says the administration might eventually need to follow the Connally position and impose a freeze. Nixon indicates that a freeze might be necessary to buoy up the country for political purposes even if the economic effects are bad.

A second Nixon-Haig call that same day reiterates these views. Nixon says in that call that the move to relax controls in Phase III had been disastrous. It appears from this conversation that Shultz's Deputy Secretary William E. Simon favored stricter controls in contrast to his boss and his letting his disagreement with Shultz be known. Nixon wants to put Connally in charge of energy policy – essentially oil and gasoline prices. He does not want Vice President Agnew to be involved in energy policy since he (Agnew) knows nothing about the subject unlike Connally. Giving the job to Agnew (who was later to resign because of a scandal unrelated to Watergate) would be a "loser."

The final call takes place just before Nixon's second freeze TV speech. The President talks to Shultz – whose views he has now overridden. Shultz is being a Good Soldier, nonetheless, and will publicly support the freeze. But in the call he doesn't endorse the idea; he just is going along with presidential policy. The only concession Nixon has made to Shultz was to exempt rents from the freeze.

Nixon wants to say that the reason for the exemption is that rent controls cause slums. Shultz knows that while that impact might occur in the long run if rent controls were retained indefinitely, it is unlikely to be the result of a 60-day freeze. The housing stock will not fall apart in two months. He suggests that a better rationale for the exemption would be that rents were not rising rapidly and were thus not inflationary. That suggestion seems to be typical of Shultz's mode of advising Nixon which has been noted in earlier musings. Shultz does not contradict the President. Instead, he suggests an alternative view.

In short, the new tapes reinforce the idea that as Watergate began to engulf the White House, decision making in the economic sphere, specifically on the wage-price controls program, became distorted by a desire to divert public attention from the scandal. In the end, the second freeze appeared to be a thrashing around of policy rather than a carefully considered decision. Nixon's political advisors might have thought the second freeze and the speech were great accomplishments that would shift the public off Watergate. That has not been the verdict of history.