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Baffling Inflation: Cost-push Inflation
Theories in the Late 1950s United States

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Baffling Inflation: Cost-push Inflation Theories in the Late 1950s United States

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Abstract
The aim of this essay is to examine how cost-push inflation theories, which highlight autonomous increases of wages and other production costs as a cause of inflation, played their decisive role in the policy debate to interpret the price movements in the second half of the 1950s. In late 1956, economic experts including politicians and journalists as well as economists started to observe a peculiarity accompanying the ongoing inflation, namely, the apparent lack of excess aggregate demand, and they placed great emphasis on cost-push inflation theories to interpret this peculiar phenomenon. When the recession of 1958 entailed a steady increase of general prices, some experts considered this as another supporting evidence of cost push inflation. Against the background of this atypical inflation, the United States Congress, then ruled by the opposition Democratic party, engaged in large-scale inquiries of inflation. These investigations produced one report among others that emphasized cost-push theories, which was called the Eckstein Report after the technical director and Harvard economist Otto Eckstein. This essay concludes that the controversy on the inflation of the late 1950s created various processes that shaped and propagated cost-push inflation theories.

1. Introduction
The aim of this essay is to examine how cost-push inflation theories, which highlight autonomous increases of wages and other production costs as a cause of inflation, played their decisive role in the policy debate to interpret the price movements in the second half of the 1950s. After the large price increases in the period between World War II and the Korean War, the United States successfully avoided inflation in the mid-1950s. However, the prices started noticeably rising in 1956.

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and continued this upward trend through 1960 with a short interruption in 1958. This persistent
inflation attracted broad attention as it happened in peacetime and was not subject to traditional
understandings of general price movements. The government and the Congress actively engaged in
this debate, and many economists offered divergent interpretations to what was understood by
some to be an unprecedented phenomenon. This essay will attempt to give a historical narrative to
this controversy and discuss the connections between the peacetime inflation of the late 1950s and
cost-push inflation theories.

Inflation theories focusing on the increase of production costs instead of excess aggregate demand
was nothing new in the late 1950s. In the bullionist controversy of the turn of the 19th century in
England, opponents of David Ricardo and Henry Thornton ascribed the inflation during the
Napoleonic Wars to bad harvests. The same arguments had since been made in various episodes in
the history of economic thought. However, cost-push theories revived with acute interest in the late
1950s. One of the major reasons behind this revival was the massive increase of labor union
membership after the end of World War II. Union membership in the United States rose from 25
percent of non-agricultural labor force to 40 percent in 1950, and more specifically, more than half
of the workers in heavy industries were organized in labor unions (Slichter 1954, 329-330; Dubofsky
and Dulles 2004, 333).²

This essay, however, focuses on another reason for the rise of cost-push inflation theories: namely,
the apparent lack of excess aggregate demand.³ Indeed, the recent rapid increase of union
membership was readily spotted as an alternative explanation for the ongoing inflation, but it is also
important to see why traditional, demand-pull inflation theories were so promptly abandoned.

There is evidence for such quick abandonment of aggregate demand as the working factor in the late

² However, according to Dubofsky and Dulles (2004, 355ff), the labor movement was losing its momentum in
the late 1950s as the proportion of unionized workers to the entire working force stopped increasing in 1955
and did not seem to be increasing in the following years.

³ Several studies mention this aspect of the late 1950s inflation, such as Goodwin (1975a, 1), Meltzer (2009,
118) and Forder (2010, 5). Meltzer incidentally noted a contradiction in cost-push inflation views which alleged
a link between the growth of corporations and unions and inflation. He pointed out that the recession that
immediately preceded the inflation of the second half of the 1950s accompanied a decline of general prices.
1950s inflation. Contemporary commentators often highlighted a budget surplus in 1956 and apparent failure of the tight money policy to stop the inflation; and after 1958, general prices increased alongside a sharp rise of unemployment (See the graph below\(^4\)). All these peculiarities that suggested the lack of excess aggregate demand despite the concurrent inflation came to be seen as a sign of an obvious deviation from the orthodoxy of demand-pull theories.

On the discussion of price movements in the mid-twentieth century in the United State, Robert Leeson (1997a, 1997b) has offered a controversial interpretation. Leeson argued that the Phillips curve was brought to bear on political party division against the background of the 1960 presidential election. He highlighted the expulsion of communist academics from American universities and almost explicit political loyalty of leading economists, thus stressing that the intellectual environment was tinged with partisan intentions. In his interpretation, therefore, it was for the purpose of claiming the superiority of policies of the Democratic party that Paul Samuelson and Robert Solow introduced the Phillips curve to the American context, in the American Economic Association conference in December 1959.

\(^4\) CPI and unemployment rate are based on the figures of the US Bureau of Labor Statistics, and discount rate on those of the Federal Reserve Bank of St. Louis (http://research.stlouisfed.org/fred2/)
Regardless of whether we take this interpretation to be tenable or not, however, a different political connection can be found with Samuelson and Solow’s work on the Phillips curve. After mentioning the “puzzling phenomenon of the 1955-58 upward creep of prices” (Samuelson and Solow 1960, 177) in one of the introductory paragraphs, Samuelson and Solow frequently referred to an investigation by one congressional committee. It was the study on *Employment, Growth, and Price Level*, whose reports published in separate volumes in 1959 and 1960, by the U.S. Congress Joint Economic Committee. Especially, Charles Schultze’s paper included in one of the related publications was heavily relied upon to the extent that Samuelson and Solow mentioned it in four separate places in the article (Samuelson and Solow 1960, 177, 181, 184, and 187). This congressional investigation was conducted under the initiative of the Congress ruled by the opposition Democratic party, and to that extent, Samuelson and Solow’s article can be said to have reflected the intention of the Democratic party, but this can only suggest that those two economists played a more passive role of responding to a report made in the political context than Leeson ascribed them in his above essays.

The controversies concerning inflation and unemployment in the 1950s set up another set of debates subsequently fought in a more academic field, the ones between Keynesians and Monetarists in the 1960s and 1970s. The connection between the 1950s policy discussions and the Keynesian-Monetarist controversies can also be found in another respect, apart from the introduction of the Phillips curve in the United States, which was just mentioned. Brian Snowdon and Howard Vane (2005, Ch. 4) give a summary of several issues in the Keynesian-Monetarist controversies, and among them was an issue concerning lags in monetary policy. Discussions about this issue was, as Snowdon and Vane narrate, triggered by Milton Friedman’s essay “Supply of Money and Changes in Prices and Output,” published in 1958; and many economists responded to it, including J.M. Culbertson (1960), John Kareken and Solow (1963), and James Tobin (1970). Friedman’s essay was written well in the context of the 1950s policy debate rather than purely out of his independent interest because it was commissioned and published by the above-mentioned
congressional committee, the Joint Economic Committee, for the specific purpose of shedding light on the ongoing inflation in the late 1950s.

The reports made by the Joint Economic Committee in the late 1950s were, in fact, important historical junctions where various economic theories about general price movements were aggregated in a single place and through which a certain set of ideas were propagated with the authority of a congressional committee attached. As we will see below, these investigations by the Joint Economic Committee involved a number of professional economists and were subsequently cited by many scholars. The present essay will thus examine the controversy on the ‘baffling inflation’ of the late 1950s, which left economic experts puzzled and eventually led to the full-fledged investigations of the Joint Economic Committee. With this aim, what follows will chronicle the remarks of politicians and journalists and economists’ views offered in the general media.

2. Inflation, 1956-57

Since the short recession of 1953-54 ended and the economy took an upturn, the Federal Reserve consistently and steadily raised the interest rates. The discount rates were increased from 1.5 percent in April 1955 to 3.5 percent in September 1957. According to Meltzer (2009, 133ff), however, the attitude of the Federal Reserve was not as clear cut as the consistent rise of the discount rates suggests. The pace of this economic expansion was variable in 1956 unlike in the previous year: the growth slowed down in the first and third quarters whereas the expansion was more vigorous in the second and fourth. Therefore, the Federal Reserve held its tight monetary policy while also fearing a possible decline of economic activities. Furthermore, the year 1956 was a presidential election year, and the Federal Reserve was under constant pressure from the administration not to apply too deflationary impact on the economy.

5 The phrase ‘baffling inflation’ was the title of an article by an economic reporter of the New York Times, which will be discussed in Section 2.
The Federal Reserve took cost-push inflation theories seriously. Again, according to Meltzer (2009, 138, 141-2, et al), some of the members of the Federal Open Market Committee supposed that it required an extremely tight policy if it was to stop inflation with monetary policy alone. Allan Sproul (1896-1978), the President of the New York Fed and influential Board member, stated in the FOMC of March 1956, “the Committee would be fooling itself if it thought it could prevent this wage-cost spiral short of adopting a very severe monetary policy” (FOMC Minutes, March 27, 1956, 33). Indeed, the concern about cost-push inflation contained a fear of turning itself against the administration. Sproul went on to say, “Whether the System would have the assent of the Government and of the public to such a course seemed . . . to be a real question” (FOMC Minutes, March 27, 1956, 33). In another occasion when a strike in the steel industry settled with a wage increase in August, Alfred Hayes (1910-1989), who had just succeeded Sproul, expressed concern over its effects on general prices. Chairman William McChesney Martin also felt alarmed and left a strong remark; “[t]he steel strike had been a disaster” (FOMC Minutes, August 7, 1956, 15)

The Eisenhower administration first publicly recognized the inflation in November 1956, and here, too, cost-push inflation was emphasized. Faced with a clear sign of steady inflation, President Eisenhower expressed his determination to fight inflation in his press conference. Answering the question about the trend of general prices, Eisenhower told reporters that there were two types of inflation; one is monetary inflation that is caused by the cheapening of money via deficit spending and printing money; the other is the inflation arising from cost increases, or in his terms the one “brought about by the efforts of all people to gain a bigger portion.” Following up this presidential remark, Edwin Dale, economic reporter of The New York Times, wrote an article to analyze the state of the U.S. economy. Dale noted government budget surpluses and a low growth rate of money supply, and suggested that the current inflation was not entirely the first type of inflation distinguished by the President.

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In January 1957, the Eisenhower administration issued its views on inflation in two important occasions. First, in the State of the Union address on January 10, Eisenhower adopted a more direct approach to the cost increase than in November: namely, he relied on exhortation and urged businesses and labor to take cooperative actions to the administration’s efforts to stem inflation.

The other outlet of the position of the administration was the President’s Economic Report, written in more academic terms by the Council of Economic Advisers. Here, too, it was clearly stated that the best economic outcome would not be achieved only by controlling the aggregate demand, and this claim was underpinned by the seemingly inadequate success of anti-inflation policies in the previous two years: the “experience [in recent years] suggests that fiscal and monetary policies must be supported by appropriate private policies. . . To depend exclusively on monetary and fiscal restraints as a means of containing the upward movement of prices would raise serious obstacles to the maintenance of economic growth and stability” (Council of Economic Advisers 1957, 44). In the press conference next month, Eisenhower took an even stronger position toward business and labor by threatening with wage-price controls although he also made it clear that it was not within his immediate course of action.

An influential economist and liberal political activist Leon Keyserling (1908-1987) responded to the President’s suggestion of the necessity of wage-price controls. Having served as chairman of the Council of Economic Advisers in the previous Truman administration, Keyserling had been critical of economic policies of the current administration. Especially, his antipathy was directed at the tight money policy of the Federal Reserve and Eisenhower’s conforming to it. In his letter to the Editor of the Washington Post in February, Keyserling ridiculed the change of attitude toward price controls of the Eisenhower administration, which once boasted the successful termination of price controls that

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7 According to Gordon (1975, 113-118), the report attracted criticisms from Milton Friedman and Neil Jacoby in correspondence.
Truman had put in place. In the same letter, he noted a cost-push factor as a cause of the inflation, or in his terms, the “crass exploitation of markets by some who rigidly administer and lift their own prices without justification.” Keyserling also criticized Eisenhower that thorough investigations by Congress should have been encouraged before suggesting wage-price controls.

John Kenneth Galbraith (1908-2006) wrote an essay in a general periodical in February, in which he ascribed the ongoing inflation to the increase of production costs owing to large corporations and organized labor. Galbraith had become a popular author after great success of *American Capitalism* (1952) and *The Great Crash, 1929* (1954) (Parker 2005). In his essay in the *Atlantic Monthly*, he observed that prices had increased more distinctly in industries where unions were strong and linked this diagnosis with his discussion of remedies. The policy of tight money, put into place for more than one year, appeared to him to be ineffective: such a policy “has been applied with increasing severity for many months. . . Prices are still rising” (Galbraith 1957, 40); and this seemed to him perfectly reasonable since the profits of large corporations were higher than they had been before and even a substantial increase in interest rates would be unlikely to stop large corporations and unions from raising their prices and wages. In the end, his suggestions of several minor remedies are cautiously guarded by his remark on political influences of the special interest, an undertone common with his signature work published a year later, *The Affluent Society*.

In the early summer of 1957, two Senate committees conducted a study on inflation. One was by the subcommittee on Antitrust and Monopoly of the Judiciary Committee, headed by a prominent Democratic Senator Estes Kefauver (1903-1963). Kefauver, announced the launch of the investigation on the current inflation in July 1957, and it invited witnesses of corporate executives and labor representatives as well as four professional economists. This study was entitled

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11 His views on inflation also reflected his peculiar understandings of functions of monetary policy. Keyserling would shortly come to insist that tightening policies would increase costs of capital and therefore product prices in some sectors, and that more direct measures, such as credit controls, would be effective (Brazelton 1997).
“administered prices,” the phrase that came into use with the research of Gardiner Means on big businesses during the New Deal era in the 1930s. Edwin Nourse, former chairman of the Council of Economic Advisers under President Truman prior to Keyserling, claimed that wages were administered as well as product prices; Richard Ruggles, economics professor at Yale, directed attention to labor productivity and argued for policies to improve such productivity and reducing cost increases (wages included) to the level proportional to the growth of labor productivity; and Galbraith noted that administered prices were inevitable in the modern economy but was skeptical of the effectiveness of radical control measures.\(^\text{12}\) Means, also among the invited panelists, wrote a letter in connection with his witness and advocated the President organizing a national conference of business and labor leaders, at which he would achieve their agreement to restrain from wage increases beyond those that reflected labor productivity growth.\(^\text{13}\)

On the other hand, the other Senate committee that investigated the inflation, the Finance Committee, indirectly enlisted the guidance of economists. It was Senators in the committee who spoke at the hearings but they cited words of economists, such as Galbraith and Warren Smith (1914-1972) of the University of Michigan,\(^\text{14}\) both of whom had suggested in their papers that monetary policy was not a solely reliable measure to stop inflation. Thus, in this committee, as in the Kefauver committee above, there were reverberations of uneven effects of tight money policy and ‘administered’ prices and wages.

Having written articles on inflation since November of the preceding year, Dale ran an article in August that mentioned the division of opinions among economists.\(^\text{15}\) He again noted the oddities accompanying this inflation: the government running a surplus, the policy of tight money in place, and substantial excess capacity in the economy, all of which are potential causes of deflation rather

\(^{14}\) Warren L. Smith would serve in several executive posts, such as an economic consultant to the Joint Economic Committee of the U.S. Congress (1959-1960), the Commission on Money and Credit (1960-1961), the Anti-Trust Division of the U.S. Justice Department (1961-1963), and most notably, member of the CEA (1968-1969).
than inflation. ‘New inflationists’, as he termed in contrast with ‘classicists’ who believed in the
efficacy of monetary and fiscal policies on inflation, focused on the powers of big businesses and
organized labor to raise prices and wages without regard to the strength or weakness of demand;
and they supposed that this autonomous rises were largely supported by the increase of money
velocity. This understanding of the ongoing price movement implied pessimism towards
conventional measures like monetary policy. Dale mentioned one feasible measure as a likely course
of action by the government in the near future: namely, price-wage controls involving only the
President’s appeal for self-restraint of business and labor, which, to a certain degree, had been
applied since January.

‘New inflationists’ would have included many popular economists besides those already mentioned:
Keyserling, Galbraith, Nourse, and Means. Sumner Slichter (1892-1959) of Harvard, labor expert and
author of popular books and frequent contributor to general periodicals, was one of the two
economists cited in Dale’s August article (the other was Keyserling). As is also highlighted by Leeson
(1997b), Slichter’s stature among the American public was indeed substantial in his times to the
extent that his colleague described him in an obituary as “undoubtedly the best-known economist of
his day to the American community generally” (Dunlop 1961, xxi). Slichter would usually write essays
for general periodicals on the state of the American economy in plain English that contained sober
reading of economic statistics. However, he was not only the most well-known figure in the
economic academia in general, but also the most vocal among the cost-push inflation theorists of
the time.  

Slichter’s views on inflation were directly linked with his understandings of the recent development
of industrial relations in the United States. Slichter had presented a paper on the relationship
between inflation and wage determination, at the annual meeting of the American Economic
Association of 1953 (Slichter 1954). The paper was also intended as a critique of Milton Friedman’s

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16 A New York Times article (on September 14, 1957) introduces Slichter as “the most vocal exponent among
our better known economists of ‘creeping,’ or ‘chronic,’ inflation.”
(1951) thesis that labor unions did not have influence on the increase of money wages, or even that they prevented money wages from rising as fast as such wages would in the absence of unions. Slichter supposed that non-union employees had less strong but largely comparable bargaining power to organized workers because high union density in the United States after WWII made it very difficult to replace even unorganized workers and also because employers were reluctant to have a dissatisfied labor force by not allowing them to have wages that they regarded fair. Therefore, Slichter’s understanding of the current wage structure was such that the pattern set by the industries with strong labor unions was followed by the rest of the economy with a certain lag without much regard for the demand conditions in different industries; and, he thus claimed that the American wage-fixing arrangements were producing an inflationary bias. Slichter therefore recommended that the public and the government be alert to wage settlements in order to achieve stable general prices under this constant pressure of wage increase.

In the early stage of the inflation of the second half of the 1950s, Slichter observed the upward tendency of price movements due to wage-cost increases. In the articles that appeared in the New York Times Magazine (Nov, 1956) and in Nation’s Business (Feb, 1957), Slichter predicted that slow inflation would continue in the long run, mainly on the ground of the bargaining power of labor unions, but he also stressed that modest inflation was a benign feature of the contemporary economy and did not contain a serious danger.

After the summer of 1957, the administration’s attack on the inflation continued. In September, the President formed a panel of top economic officials including the chairman of the Federal Reserve Board so as to facilitate communication between the government and the central bank. However, the Consumer Price Index remained constant for four months from July through October, and the inflationary pressure was interpreted to have somewhat weakened. The threat of creeping inflation became out of fashion in the public media, albeit only temporarily. Constant inflation returned shortly, this time accompanying recession.
3. Recession, 1957-58

Recession set in at the end of 1957. In November, the unemployment rate suddenly increased by half a percentage point from 4.5 percent in October. The increase of unemployment continued until the unemployment rate reached 7.4 percent, the highest since 1940, in April 1958. In February 1958, President Eisenhower took an unusual step by making a televised speech to assuage people’s concern over the recently published unemployment figure. Eisenhower had kept shunning the term ‘recession,’ but later in the same month he finally used it and expressed determination to end it as quickly as possible. The Gallup poll in March 1958 indicated a rapid increase in the proportion of the people who chose unemployment as the most important national problem, from 7 in the previous month to 40; and the approval rate of the Eisenhower administration dropped by 6 percentage points in March and reached the lowest point since he was sworn in five years ago. Many politicians, including economist-turned-Senator Paul Douglas, were openly concerned about the state of American economy, and they called for concrete action, such as tax cuts and monetary easing.

The Federal Reserve Board recognized a decline of the economy in November 1957 and reduced its discount rates by 0.5 percentage point. The economy continued to show signs of slowing down in December. In a FOMC meeting, Chairman Martin, who would usually stay silent and make summarizing statements of other Board members, spoke first and called for further easing. Other members concurred, and it was agreed that the Federal Reserve should emphasize that it was recognizing the current dire economic situation (Meltzer 2009, 164). As the recession was worsening, the Federal Reserve prioritized stopping the recession and ceased being alert to inflation. It quickly reduced the discount rates from 3.5 percent to 1.75 percent only in seven months (Note that it took

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more than two years for the Federal Reserve to raise the discount rates from 1.5 percent to 3.5 percent in 1955-57).

To many economists, this recession was unexpected. In March, Slichter was asked for an opinion on the recession by The New Republic magazine. In preceding November, he had written in the same magazine that the economy would be expanding in the spring.\(^{21}\) After he stressed the recession was less serious than it appeared, he blamed the recession on the deflationary policy of the Federal Reserve. He reckoned that the Federal Reserve prevented the price level from “adjust[ing] itself to rising costs”. In April, Slichter offered his views to the Senate Finance Committee in the hearing in which Chairman Martin of the Federal Reserve Board was also present. Here, too, Slichter blamed the Federal Reserve for being too late to stop its tight money policy although he also noted, and Martin concurred, that economists in general were still wanting in the understanding of business cycles and that this prevented them from predicting this strong recession.\(^ {22}\)

Even when recession was developing in the whole country, the problem of inflation did not completely disappear. Indeed, during this recession, general prices were rising rather than declining, and this appeared to have been recognized by various actors. A Washington Post financial columnist Harold Dorsey (1900-1970) ran an article in May to criticize cost-push inflation theories; and there he described the over-excitement of his opponents by stating, “The recent announcement of another increase in the Consumer Price Index for the month of March . . . brought forth a chorus of ‘I told you so’s’ from those who have been believers in the inevitability of persistent creeping inflation.”\(^ {23}\) This description suggests there was a large following of Slichter’s analysis of inflation, and they felt it was verified by the fact that recession accompanied general price increases. In the same month, an economist of Duquesne University sent a letter to the Editor of the New York Times, observing the peculiarity of the ongoing recession: “One characteristic of the current recession is a

\(^{22}\) The Washington Post and Times Herald, April 19 and 24.
persistently high level of prices. . . . how can a recession, obviously a result of deficient total demand, coexist with inflation?" The author of the letter then used this observation to express support of cost-push inflation theories.

In the same month, a New York Times economic reporter Dale also wrote an article on inflation. This article featured the “great debate” within the economics academia. In his summary of the debate, the current inflationary recession had not given any clear proof for either side of the debate, and economists on both sides generally agreed that it had not. This was, Dale noted, because there was wide agreement that in the early stage of recession prices tend to remain stable because some goods and services lag behind in their price response. Therefore, seeing that agricultural products and services accounted for the most of the price increase since November 1957, Dale pointed out the demand pull economists (or the ‘classicists’ in his term) could defend their position. He then added that the price movement in the next several months would give reliable judgment on the current debate. Here we can notice that a subtle shift occurred in the debate. The issue now turned more on whether the demand pull theories are tenable than whether cost push theories are worth consideration as it was before the recession.

In August, Dale partially answered the above self-posed question by expecting inflation to resume in the following year. The wholesale prices had declined since January 1958 but only to a limited extent. This led him to conclude that “a general slack in demand . . . apparently cannot pull down most prices in the American economy.” Various indices of money wages, he also observed, pointed to an increase in the wages of manufacturing during the recession. In these wage figures, he saw an additional evidence for the immunity of money wages from general economic conditions and

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24 The New York Times, May 5, 1958, p. 28. The author of the letter was Cyril A. Zebot (1915-1989), immigrant from Slovenia and professor of economics at Duquesne University (1958) and then at Georgetown University (1958-1978).
remarked, “There is more and more backing among economists for the general concept of ‘wage inflation.’”

Mid-term elections of U.S. Senate and House of Representatives were going to be held in November, and the campaign for these elections gradually became intense in the months leading up to them. Inflation remained one of the major issues during this campaign for both Republicans and Democrats. Democrats were eager to spotlight economic mismanagement of the Eisenhower administration, and the creeping inflation that had been underway since 1956 was the most conspicuous examples after the recession of 1958. Inflation was also highlighted in the Republican campaign, but for a different reason. In the press conference in August, President Eisenhower emphasized two policy issues, inflation and government deficits, for the midterm election campaign. He stressed large deficits were being authorized by the Democratic-ruled Congress, and that this would before long revive the danger of inflation. Despite the efforts of the Republicans to convince voters that their opponents were reckless spenders and sowing the seeds of inflation, they suffered large losses in the elections, in which 48 seats in the House of Representative and 13 seats in the Senate were lost. The New York Times summarized the Democrats’ victory by stating: “The biggest issues working for the Democrats . . . were the ‘pocketbook issues,’ including unemployment, the recession, the steady increase in the cost of living, and in some sections of the farm belt, still depress farm prices.”

4. Two Studies by the Joint Economic Committee

Although many economists’ views on inflation and recession were expressed in the occasions hitherto mentioned, they were provided with more serious outlets by one congressional committee. The Joint Economic Committee of the U.S. Congress (which changed its name from The Joint Committee on the Economic Report after 1955, JEC hereafter in this essay) is one of the twin organizations instituted by the Employment Act of 1946 (the other twin was the Council of Economic

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Advisors, or CEA hereafter, which serves the President). The Committee’s regular task was to review the CEA’s annual economic report at the Congress, but it also has engaged in independent studies on various pressing economic issues. The peculiar phenomenon of inflation that started in 1955 was readily under the radar of the committee. It authorized the two studies to investigate this inflation, entitled respectively “The Relationship of Prices to Economic Stability and Growth” (1958) and “Employment, Growth, and Price Level” (1959).

The JEC was staffed by politicians from both parties, but Democrats held a firm majority of the committee after the 1956 election (4-3 among representatives and 4-3 among senators, and after the 1958 mid-term election, 5-3 and 5-3). Consequently, chairman was occupied by Democrats. The first study mentioned above was conducted under the chairmanship of Rep. Wright Patman (1893-1976), veteran congressman with strong interest in economic issues and frequent correspondent with professional economists. Patman was widely recognized as a relentless critic of the tight money policy of the Federal Reserve (Young 2000, 157 and Ch. 7) and had asked the Congress for an investigation on the Federal Reserve System in 1955 and in 1957, only unsuccessfully.30

Despite the overt intention of the chairman, however, this investigation was designed to be impartial. It invited economists from labor and industrial organization as well as university economists from many institutions. The compendium of the papers, mostly written by university economists, was first published in March 1958, when the recession had been building up for several months already. Friedman’s paper on the lags of output and prices changes to money supply changes, mentioned in the Introduction, was included in this compendium. The Wall Street Journal reporter commented on the compendium and noted the variety of opinions offered, in the article titled “Lawmakers poll 47 economists on behavior of prices, get roughly 47 different views.”31 Indeed, some contributors stressed price increases were a benign accompaniment of economic growth, and others highlighted the serious danger of inflation. Again, Martin Bailey and Albert Rees, both of the

30 The New York Times, Jan 8, 1957; June 3, 1958,
University of Chicago, in their different papers denied the importance of unions and corporations as a factor of inflation while Gardner Ackley, Abba Lerner and many others insisted on their importance. Taking the side of the former position, Friedman in the above paper hypothesized that the recent inflation was caused with a certain lag by the change of money supply. Based on these varied papers, the JEC conducted hearings in May, which was followed by another set of hearings for economists from unions and industrial organizations in November (in which union economists blamed corporations, and economists from industrial organizations berated unions), and a final set of hearings in December.

This study was well accepted by economists. When Willard Thorp (1899-1992) of Amherst College, distinguished economist who held advisory positions in three administrations, organized a conference and published a non-technical book entitled *The New Inflation* (1959) with Richard Quandt (b. 1930) of Princeton, the book acknowledged the usefulness of the various data and theories offered in the report of this JEC study. The book *The New Inflation* was one of the many publications in 1959 and 1960 to highlight cost-push inflation theories.

The extent of thoroughness and impartiality that the JEC was striving for in the study of the inflation can be estimated by a report published between the first set of hearings and the second for the above investigation. In October 1958, the JEC compiled a report “Economic Policy Questionnaire”, in which it essentially took a ballot on inflation and economic growth from university economists (Joint Economic Committee 1958b). The questionnaire was estimated to be distributed to 1,500 individuals (It was circulated through the heads of economics department in 150 institutions), and the Committee received 615 completed responses. Among questions asked were “how much unemployment you would accept as a condition for price stability?” and “what constitutes a

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32 Thorp and Quandt write in the preface: “We must also make our obeisance to the Joint Economic Committee of the Congress for its activity in this field in 1958. It produced a Compendium of Papers, Commentaries, and two sets of Hearings, a record 1,842 pages long, dealing with the ‘Relationship of Prices to economic Stability and Growth.’ It is a monumental source of theory and fact” (Thorp and Quandt 1959, vii).

33 For instance, JSTOR search with the words ‘wage’ and ‘inflation’ shows a peak in 1960. The numbers of search results narrowed by the discipline of economics are: 124 in 1955, 134 in 1956, 171 in 1957, 180 in 1958, 190 in 1959, 246 in 1960, 193 in 1961, and smaller numbers follow for immediate subsequent years.
satisfactory level of price stability?” For the first question, the answer ‘5 percent’ received the most responses, and for the second did ‘1 percent and under 2.’ The questionnaire also asked which policy option should be given the most preference to control inflation, and monetary policy received more than half of the responses while direct control was preferred by only 6.2 percent. On the other hand, however, to the question on whether wage increases affected the recent inflation in a significant degree, the response was broadly divided with 50.4 percent answering ‘Yes’ and 40.7 percent ‘No.’

The above-mentioned second study, Employment, Growth, and Price Level, was started after the 1958 mid-term election, in the eighty-sixth congress. In January 1959, Patman was succeeded by Paul Douglas, academic-economist-turned Senator. The Democratic party leader Senator Lyndon Johnson had called for a thorough investigation on the ongoing inflation in December 1958 (even though such an investigation had been just finished by a congressional committee!), and Johnson turned on the JEC for such an investigation. Johnson phoned Douglas on February 10, and the JEC announced the launch of an investigation in the same week. An article on the Washington Post praised this announcement as a wise move from the Democratic party. The Eisenhower administration had established a cabinet committee to study the recent inflation and placed Vice President Richard Nixon as its chairman. The Washington Post article thus viewed the newly announced JEC study as Democrats’ attempt to counteract the “Nixon committee” and “the administration . . . already committed to one set of answers.” As Scott Gordon (1975, 123-125) narrates, this Nixon committee hired Allen Wallis, Chicago-trained economist and then dean of the School of Business at Chicago, and published a report in June that criticized the overspending authorized by the Democratic-ruled Congress.

34 The exact wording of this question was: “Do you believe that in recent years rising prices have resulted in significant part from a tendency of real wage increases to exceed the rise of productivity?”
35 Letter from Douglas to Democratic members. Paul Douglas papers, Box 255, folders labeled 1959.
The Senate resolution that authorized this investigation afforded hiring of a technical director. The JEC announced on April 12 that it appointed for such a position Otto Eckstein, a Harvard professor only at the age of 32. A plausible reason for his appointment would be that the leading members of the JEC were pleased by his paper submitted to the previous JEC study discussed above. In that paper (Eckstein 1958), entitled “Inflation, the Wage-Price Spiral and Economic Growth,” he provided a reasoning to reconcile intricate statistics with a conclusion that the sectors with large corporations and unions were a source of the general price increase of 1955-57.

The JEC started to hold hearings, however, even before it appointed Eckstein as technical director. In March, Slichter, Keyserling and others were invited; and many other hearings followed through the end of 1959. The JEC published in connection with this study the Committee Report (written by the JEC members with a minority report attached, 156 pages), the Staff Report (written by Eckstein and staff economists, 488 pages), and the twenty-three study papers in several separate volumes.

The first volume of study papers was published in September 1959, with Douglas’s press release comment accusing a parallel inquiry of the cabinet committee headed by Vice President Nixon of politically motivated. The first volume was solely devoted to the paper by Charles Schultze (b. 1924), which I mentioned in the Introduction. Schultze had served in the Council of Economic Advisers as a staff economist and was then an instructor at Indiana University. His paper “Recent Inflation in the United States” put forward a theory called ‘demand shift inflation.’ Schultze first admitted that it was difficult to statistically discern the effects of demand-pull factors and cost-push causes; but he argued that it could be reduced to the “sensitivity of prices and wages to changes in the demand for goods and services” (Schultze 1959, 1); and he assumed upward flexibility and

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38 The Washington Post, April 13, 1959, p. A21. Eckstein would be appointed as member of the CEA under the Johnson administration. He is also notable for the foundation and management of an economic forecasting company, Data Resources Inc., which was later sold to McGraw-Hill.
40 Like Eckstein, Charles Schultze would take important posts under Democratic governments. He was Assistant Director of the Office of Management and Budget in 1962, Director of the same office in 1965-67, and chairman of the CEA in 1977-81.
downward rigidity of money wages and described how this assumption leads to general inflation under specific circumstances. When demand shifted from one sector to another, he suggested that money wages in the second sector increase while those in the first sector do not decline because of downward rigidity. Furthermore, in the case when the sector in which demand declined is supplied by the other sector, prices of products in the former must increase to absorb the increase of costs. Thus, when demand shifted between different sectors in the economy, inflation must result even though the aggregate demand remained unchanged.

The second volume of study papers was published in November. In one of the two papers included there, Eckstein and Gary Fromm of Brookings Institution stressed the significance of cost factors in the recent inflation. The paper quantitatively estimated the effect of steel price increases on general prices with the input-output analysis. Forty percent of the increase of the wholesale price index and 23 percent of the increase of final product prices were estimated to result from the steel price increases.

At the annual meeting of the American Economic Association, held in December, a session was organized to discuss “Problem of Achieving and Maintaining a Stable Price Level.” One of the papers presented there was now famous Samuelson and Solow’s essay, often credited with introducing the Phillips curve in modern macroeconomics. As I noted in the introduction, their paper relied on the study papers by Eckstein and Fromm as well as Schultze. However, it was not just Samuelson and Solow who were concerned with the ongoing JEC inquiry, but the other participants of the session also extensively discussed Schultze’s demand shift theory (Reynolds 1960; Chandler, Lerner, and Pechman 1960). In fact, the urgency is more clearly seen from the discussions of these participants, who prepared long lists of concrete policy proposals that could address the Schultze-type creeping inflation, such as holding national labor-management conferences and lowering tariffs and regulations to promote competition. Two discussants, Lester Chandler (1906-1988) of Princeton and Joseph Pechman (1918-1989) of the Committee for Economic Development, so readily accepted
Schultze’s inflation theory as an explanation of the inflation of the second half of the 1950s that they questioned Samuelson and Solow not distinguishing between the price movements before and after 1955 to derive a quantitative estimate of the relationship between inflation and unemployment. 41

In December 1959, the JEC published the Staff Report, and the Committee Report, divided into the majority (Democratic) and the minority (Republican) reports, a month later. The Staff Report was divided into eleven chapters, each treating different economic policy fields including remedies to structural unemployment and low prices in agriculture sectors. However, its main theme was evidently more specific, which was to analyze a contradiction that prevailed in the previous several years between general price stability and economic growth and to propose ways to avoid it. The chapter on growth in recent years (Ch. 3) contained a controversial statistical conclusion that economic growth of the United States was less rapid in the years after 1953, the year Eisenhower replaced Truman as U.S. President, than it was before; and the report argued for a different policy approach from that being taken by the Eisenhower administration. The chapter on postwar inflation (Ch. 5) endorsed Schultze’s demand shift inflation theory as an explanation of the inflation of 1955-1957. This analysis of the recent inflation underlay the policy proposals in Chapter 10, which included strengthening of anti-trust laws and lowering of import duties so as to encourage competition, and creation of labor-business conference at the national level. It also mentioned government intervention in wage negotiations as a last resort. More specifically, a method was considered that would open hearings in the Congress to examine proposed price increases.

41 Chandler stated, “[I]n the 1951-53 period when unemployment averaged below 3 per cent there was less upward price pressure than we experienced in the 1956-57 period when unemployment averaged closer to 4 per cent. As Charles Schultze has noted, the latter period was characterized by large shifts in the composition of demand” (Chandler, Lerner, and Pechman 1960, 214, emphasis mine). Pechman wrote, “I am prepared to accept Professor Charles Schultze’s sector inflation hypothesis to explain 1956 and 1957. But the remaining years do not fit the Samuelson-Solow version of the Phillips curve for the United States or any other pattern, for that matter” (ibid, 220). Incidentally, it is interesting to note that Chandler was probably the first (or second to Samuelson and Solow themselves) to point out the long-run shift of the Phillips curve. He stated, “To the extent that they felt more assured that unemployment would remain low and that prices would continue to rise, trade-unions would probably demand larger wage increases and employers would be less disposed to resist them” (ibid, 213).
The Staff Report received several full-length reviews from academic journals (Hoover 1960; Wonnacott 1960; Minsky 1960; Robinson 1960). These reviews suspected a political bias in some parts of the Staff Report; they especially singled out as such an example the above-mentioned estimate of economic growth. However, they left generally favorable comments on the report. Hyman Minsky’s review on the Review of Economics and Statistics viewed Schultze’s demand shift theory as a “serious and ingenious contribution to the analysis of inflation” and “good foundation upon which further work can be built” and the whole JEC study as a “success” (Minsky 1960, 6 and 12). In his review on the American Economic Review, Romney Robinson devoted more than four pages out of a fifteen-page article to critically discuss Schultze’s inflation theory after stating, “Schultze’s name has already been associated with a particular explanation of [the price rise of 1955-57]” (Robinson 1960, 1004).42

Schultze’s paper did not end its life in the Staff Report of Employment, Growth, and Price Level. There is evidence that Schultze’s study paper was considered in the following Kennedy administration. After sworn in as the President of the United States, John F. Kennedy set up a committee to discuss ways to stop cost increases and resultant inflation, called Labor-Management Advisory Council, and the CEA chairman Walter Heller led the discussion to achieve a consensus that it was necessary to put concrete measures into place (Barber 1975, 141-2 et al; Burke 1979). The CEA prepared working papers for Labor-Management Advisory Council, among which was Schultze’s paper “Recent inflation in the United States.”43 Schultze himself was invited by Heller for the discussion in October 1961.44 His paper no doubt significantly affected the discussion within the Kennedy administration. The administration would later adopt a ‘guidepost’ policy, which recommended wage increase not to exceed the overall average of productivity increase in the previous five years.

42 Another reviewer observed subtle effects of quantitative studies being published as part of a congressional inquiry. Paul Wannacott suggested that Eckstein and Fromm’s study paper on the effect of steel price increases would not have been taken as seriously had it been published in a professional periodical.
43 Walter Heller Papers, Box 25, Folder ‘wage-price guideposts’ 5/5.
5. Conclusion

This essay discussed the rise of cost-push inflation theories in the late 1950s. First, in the period of economic expansion in 1956-57, it was realized that tight money policy could not fully restrain the upward price movement; and second, during the recession of 1958, a rapid increase of unemployment alongside a steady rise of general prices was considered to be a sign of the validity of cost-push inflation. Indeed, there were scholars who rejected the idea and maintained traditional inflation theories focusing on the aggregate demand, especially the Chicago economists, Martin Bailey and Albert Rees. However, politicians and economic reporters in the general media kept mentioning cost elements of the causes of inflation, and publicly influential economists, such as Leon Keyserling and Sumner Slichter, readily backed up their recurring hints of alternative views about inflation.

Economists of today might see this idea of cost-push inflation with skepticism. They might even try to explain the inflation of the late 1950s with a notion that has gained a fairly broad consensus since the late twentieth century with the research of Ben Bernanke and others, namely lags in the effect of monetary policy. Friedman was indeed ahead of his time in this respect. He argued in 1958 that changes of output and prices lag behind changes of money supply. However, this notion does not seem to have gained support from the majority of contemporary economic experts although a few economists left favorable comments on it (Robinson 1959, 1960). The idea which gathered much greater interest among contemporary economists was Charles Schultze’s demand shift theory with its close attention to industry-by-industry demand conditions and intuitive assumptions about the wage determination practice.

This essay has also shown the process of propagation of cost-push inflation views. Executive officials and a few popular economists began this propagation process by cautiously observing the puzzling nature of the ongoing inflation. The inflation was then followed by a recession which some believed showed convincing evidence for cost-push inflation theories. At this high point of the interest in the
general price movements, the Joint Economic Committee provided high-profile venues for in-depth studies to be collectively published with the authority of the congress. Along all the way, economic reporters well versed in economics, among whom the most notable was Edwin Dale of the New York Times, realized the close connection between abstract ideas and actual economic phenomena. Political party rivalry was certainly instrumental to a great deal of publicity surrounding inflation, too. It created debating points, and it divided actors into two camps which responded to them with two distinct conclusions. All these elements in the propagation process seem to have been crucial for a theoretical notion to gain wide circulation in the public sphere so quickly.

Inflation was no doubt one of the most widely discussed political issues in the United States in the late 1950s. In fact, it could influence the outcome of national elections. In this situation, therefore, it is suspected that even an ad-hoc policy guidance was highly appreciated. Confusion concerning the cause of inflation—cost push or demand pull—was certainly one motivation for Samuelson and Solow in presenting their paper in 1959 as we can see simply from the content of the paper, but the political urgency of the issue would also have been a decisive element at a different level, the level that orients one's research interest and determines types of final products that one regards important.

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