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6. THE WAGE-PRICE OUTLOOK FOR 1983

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Introduction

Although theorists long ago proclaimed the Phillips curve to be dead, the notion that severe recession can reduce inflation significantly was resurrected by recent events. Unemployment reached levels unprecedented in the post World War II period while price increases slowed substantially. As measured by the Consumer Price Index, price inflation during the year ending October 1982 was "only" 5.1 percent, just half the rate of the previous 12 months. The unemployment rate in October 1980 was 7.5 percent, but rose to 10.4 percent by October 1982. On the labor side, the employment cost index for total private compensation slowed from 10.0 percent in 1981 to 7.0 percent at an annual rate during the first 9 months of 1982.

Disaggregating the Price Side

As Table 27 shows, different breakdowns of the CPI tell different stories. Because of difficulty with the housing component, the Bureau of Labor Statistics will introduce a new version of the CPI, known as CPI-U-X1, in January 1983. The new index will use a rental equivalency methodology to estimate housing inflation. According to the X1 index, inflation during the year ending October 1982 was about 0.5 percent higher than the more generally reported increase. The decline in inflation according to the X1 version was less dramatic than reported by the conventional CPI.

Economists attempt to measure the underlying rate of inflation by filtering the noisy, volatile components out of price indexes. Table 27 provides such a calculation. The underlying inflation rate is the average of the inflation rates for commodities excluding food and energy and selected services. The inflation rate for nonfood, nonenergy commodities declined more quickly than for other components of the price index in the economic slump which began in 1979. Service inflation, especially in the medical area, has been less affected. The underlying inflation rate was a little more than 6 percent in the year ending October 1982.

The Wage Side

Table 28 shows that wage increases have been decelerating. On a total compensation basis, including fringe benefits and payroll taxes, wage inflation ran at an annual rate of 7 percent during the first nine months of 1982, down from 10 percent in 1981. Union wage settlements also declined. For example, the

Bureau of National Affairs' (BNA) index of first year union settlements showed a median increase of 9.6 percent in 1981 compared with 7.1 percent during the first three quarters of 1982. These figures omit wage adjustment due to escalators, but since the inflation rate was higher in 1981 than in 1982, the actual slowdown was even greater. Major agreements in the private sector declined even more dramatically from 9.8 percent in 1981 to 3.8 percent in 1982.

Union and nonunion wages rose at the same annual rate during the first 9 months of 1982 (6.7 percent), whereas in previous years union pay increases outpaced nonunion. On a total compensation basis, however, union increases still outpaced nonunion.

Recently, much publicity was given to wage concessions in such key industries as trucking, automobile manufacturing, and airlines. Some observers predict that an eventual wage explosion will occur when these industries get back on their feet. Others argue that the concessions will lead to a new pattern of labor relations in which the adversary relationship between unions and management will be replaced by a new spirit of cooperation. Both predictions are wrong.

Workers in the U.S. labor force fall into two main categories: union and nonunion. Most of the publicity about wage concessions has centered around union negotiations. These concessions have typically involved some combination of wage freezes, wage cuts, frozen or delayed cost-of-living escalator payments, and workrule relaxations. The prolonged recession threatened the job security of senior union members, and the concessions negotiated on their behalf were designed to avert mass layoffs, plant closings, and bankruptcies.

Table 29 shows the industry distribution of wage freezes and cuts in the union sector through mid-November 1982, based on a BNA survey. A broad range of industries was affected. However, the first five industries listed -- construction, metals, retail food, rubber, and motor vehicles -- accounted for 58 percent of the reported union wage freezes and cuts, and construction alone accounted for more than 25 percent. Yet, because construction settlements typically are local and often involve small numbers of workers, most of the publicity on union wage concessions has centered on manufacturing and transportation.

Undoubtedly, some of the union workers experiencing wage freezes or cuts will want their wage concessions undone when the crisis ends. American Chrysler workers, when faced with the possibility of having to strike to undo parts of a concession agreement, decided instead to resume negotiations after a cooling-off period. Their Canadian counterparts, however, exercised the strike option. But even if all union workers in the U.S. decided to follow the Canadian example and pushed for reversing the concessions, a relatively small proportion of the labor force would be affected. Out of a total employed labor force of almost 100 million perhaps two million workers were covered by union agreements including concessions. In any case, the current low level of strike activity in the U.S. does not suggest widespread militancy.

Wage concessions in the nonunion sector are more difficult to track. Indeed, since these are really unilateral decisions by management, it is misleading to term them "concessions." Management motives for wage freezes and cuts in the nonunion sector have varied. Sometimes they have been imposed on nonunion workers prior to negotiations with unionized employees at the same firm. Nonunion wage freezes are a signal to union bargaining teams that management expects a similar package from them. Sometimes nonunion pay has been frozen as a follow-up to a concession by union workers in the same company. And sometimes, nonunion pay has been cut or frozen simply because the employer's sales and profits were declining. Whatever the motivation, it is unlikely that nonunion management will wish to participate in a future wage explosion.

Few economic forecasters expect more than a moderate pace of recovery in 1983. Few believe that the recovery will be fast enough to reduce the unemployment rate substantially. Under these circumstances, a major re-ignition of inflation, particularly of wages, is most unlikely. Inflation expectations have been reduced because of the current low rate of price increases and general downward trend in the inflation rate over the last two years.

If a wage explosion is not in prospect, will the wage concessions have any lasting effects? Some observers note that the concession contracts have included experiments with worker participation in management, quality circles, and other cooperative arrangements. They suggest that these experiments signal a fundamental change in American labor relations. But history shows that many of these experiments will fade away once the economic crisis ends.

Although the current concessions and cooperative experiments have grabbed the headlines, they are not unique. The U.S. economy has gone through similar episodes before. In the early 1960s, for example, a period of low wage adjustments was also accompanied by innovations in labor-management cooperation. Then, such schemes and the Kaiser Long-Range Sharing plan, the Armour Automation Agreement, and others were heralded as new frontiers in labor relations. Yet after a few years of prosperity, most of these arrangements were dropped. Many of today's exciting innovations will suffer the same fate. Those innovations which will remain are programs which provide tangible, contractually defined benefits in the areas of income and job security.

In the auto negotiations, for example, part of the GM and Ford concessions packages included protections of senior workers against income losses. Some experiments in guaranteed job security also were undertaken. Clearly, workers threatened by layoffs see continuing value in these plans and will want to include them in future contracts.

Although management may regard these plans as potentially costly, they may provide greater management flexibility in the future. If workers are protected from layoff, they will be less resistant to the introduction of labor-saving technology, the relocation of factories, and similar changes. Both labor and management are likely to see advantages in these programs. One legacy of the current recession will be expansion of job-security programs in key industries.

Recently, the Conference Board's labor outlook panel forecast that wage settlements next year would average just below 7 percent.1/ The panel noted that the union sector in 1982 broke itself into two sectors: one experiencing wage cuts and freezes and one with "normal" bargaining. As Table 28 shows, if wage freezes and cuts are excluded from the 1982 union settlements, the BNA figures suggest a general range of settlements of around 8 percent while the BLS figures suggest about 7 percent. Thus, the Conference Board forecast essentially calls for a bottoming out of wage settlements in 1983. This is based partly on the premise that, except for the steel industry and related contracts, the scope for further mass concessions is limited. This assumption is further premised on at least some degree of recovery in 1983.

For nonunion workers, a recent survey by Hewitt Associates suggests pay increases of about 6 to 7 percent in 1983. Such projections may be changed, of course. Last year, as inflation abated, firms revised their wage projections.2/ However, a forecast of overall compensation adjustments in the 6 to 7 percent range seems reasonable and is in keeping with an underlying price inflation rate of about 6 percent.

The Social and Political Consequences

Unemployment has been the social cost of fighting inflation through restrictive monetary policy. The 1982 election results suggest that unemployment in the 10 percent range has political repercussions, which appear to have influenced monetary policy. Fiscal policy, however, may well be paralyzed by a stalemate between Congress and the Reagan Administration.

1/ Audrey Freedman et al., Labor Outlook, 1983 (New York: The Conference Board, 1982).

2/ Hewitt Associates, Survey Results: 1982 and 1983 Salary Increases (Lincolnshire, Ill.: Hewitt, 1982).

The UCLA Business Forecast calls for a limited recovery in 1983. But suppose the recovery fails to materialize. Suppose that economic conditions worsen significantly. Pressures for government action would surely mount. Accepted norms would be challenged. Calls for economic planning, perhaps under the rubric of Japanese-style government/business cooperation, would increase. Import restrictions would become more prevalent. One has only to look at the political and policy consequences of the Great Depression to find precedents.

Certainly, some in the Reagan Administration have considered this possibility. If so, someone in the Administration must question the continued pursuit of reduced inflation as the major goal of economic policy. In fact, inflationary expectations have been reduced dramatically, at least for the short-term. Although further decreases in inflation may be difficult to achieve, a major inflationary explosion in the next year or two seems unlikely even if the economy is given a significant stimulus. This fact probably has not escaped the attention of the President's economic and political advisors given that 1984 is an election year.

Table 27. Recent Trends in Consumer Prices (Annual Rates of Change)

	Oct. 1979 to Oct. 1980	Oct. 1980 to Oct. 1981	Oct. 1981 to Oct. 1982
All Items:			
CPI-U	12.6	10.2	5.1
CPI-U-X1	8.7	9.1	5.6
Commodities less food and energy	10.4	6.7	5.6
Medical Care Services	11.1	11.8	11.3
Other Services1/	10.2	9.3	8.3
Underlying Inflation2/	10.4	7.5	6.4

1/ Excluding transportation, household, rent.

2/ Average of commodities less food and energy, medical care services, and other services (excluding transportation, household, and rent) using Dec. 1981 weights.

Source: U.S. Bureau of Labor Statistics.

Table 28. Recent Wage Trends (Annual Rates of Change)

	1980	1981	1982 (first 9 months)
Compensation Increases1/	-	10.0	7.0
Wage Rate Increases1/	9.0	8.8	6.7
Union	10.9	9.6	6.7
Nonunion	8.0	8.5	6.7
BNA Median First-Year	9.5	9.6	7.1
Union Wage Settlements2/	-	(9.9)	(8.1)
BLS Mean First-Year Major	9.5	9.8	3.8
Union Wage Settlements2/	(9.5)	(11.2)	(7.1)3/

1/ Private, nonfarm industry. From Employment Cost Index.

2/ Excludes payments under cost-of-living escalator clauses.

3/ Figure refers to contracts featuring a guaranteed wage increase during the life of the contract.

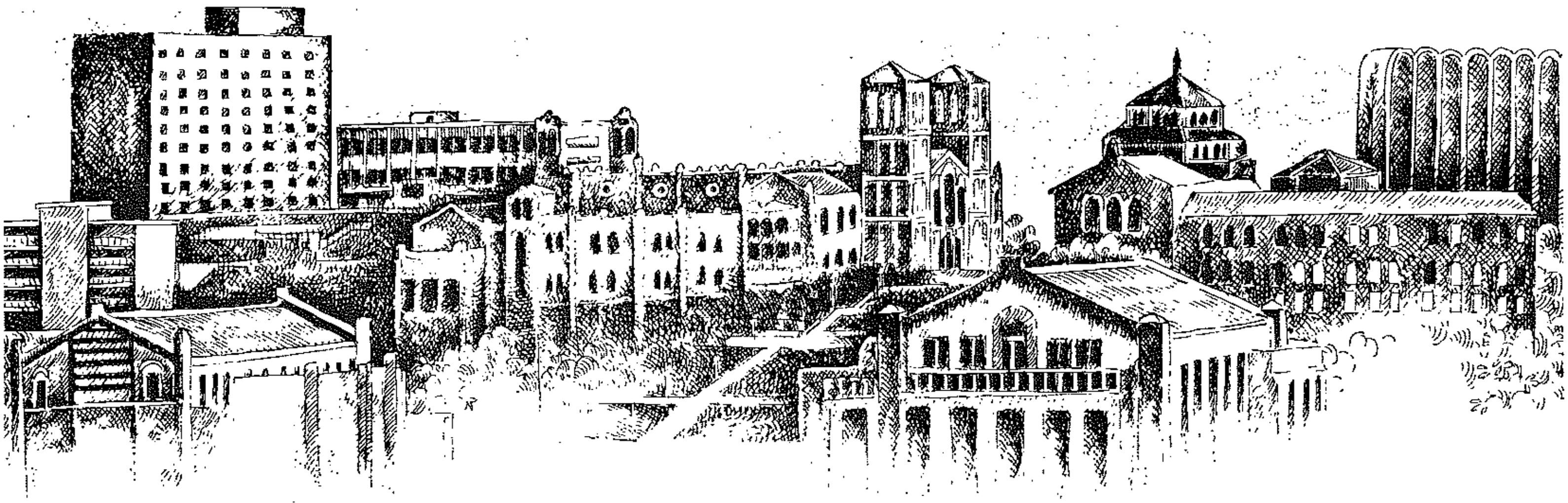
Note: Figures in parentheses exclude settlements with wage freezes and cuts.

Table 29. Frequency of Union First-Year Wage Freezes and Cuts through Mid-November 1982

Construction	37	Airlines	5
Metals and metal products	14	Canneries	4
Retail food stores	10	Printing	4
Rubber products	10	Aerospace	4
Motor vehicles and parts	10	Shipbuilding	2
Meatpacking	7	Furniture	2
Public transit	7	Instruments	2
Machinery	6	All others	11
Trucking	5	Total	140

Note: Mean Contract Duration = 2-1/2 years

Source: Daily Labor Report, various issues.



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