BOARD OF GOVERNORS
OF THE
FEDERAL RESERVE SYSTEM

Office Correspondence

Date April 16, 1943

To Chairman Eccles

From Martin Krost and Kenneth Williams

Subject: Effects of "Hold the Line" Executive Order

Effects

The Order practically eliminates the authority of the War Labor Board to grant wage increases, (except to increase substandard wages), directs the OPA to keep all items affecting the cost of living at the September 15, 1942, level, and gives the War Manpower Commission authority to prevent workers' changing jobs to secure higher wages. The chances of keeping wages frozen as rigidly as the Order implies are extremely small; but the Order may serve the immediate purpose of preventing a break-through in the Little Steel formula in the Mine Workers' case.

Justification

The Order reflects the conviction that economic stabilization requires rigid stability in wage rates and that such stability cannot be enforced without equally rigid stabilization of all prices entering into the cost of living. The United Mine Workers' negotiations cannot be prevented from initiating a new wave of wage increases unless assurance is given that the cost of living will, in fact, be held stable. The urgency of this immediate problem is such that the risk cannot be taken of correcting inequities in particular prices or particular wages through the price mechanism for fear that the cumulative effect of such adjustments will unstabilize the whole wage structure.

The Order takes another step away from the peacetime situation of permitting wage rates to determine the allocation of manpower among different occupations and permitting prices to determine the volume of production of goods and their distribution among consumers. It will throw additional heavy burdens on our inadequately developed governmental machinery for allocating manpower, scheduling production, and determining consumption. In particular, subsidies will become an absolute necessity. We are abandoning control of economic activity by free markets and the situation is likely to be a difficult one until governmental controls have been worked out and administrators learn how to operate them.

The Order will relieve the inflationary situation by preventing the growth of money income attributable to wage increases. But, of course, it does nothing to prevent the growth which will be the result of further expansion of Government expenditure, unless coupled with increases in current rates of taxes and saving. It does help to assure, however, the Government in spending more money will get increased output, not the same output at higher prices.

Background

The latest Executive Order is the culmination of the movement toward governmental control of wages which started a year ago with the President's Seven-Point Anti-Inflation Program. As a result of that program the War Labor Board in the "Little Steel" case announced the policy of permitting further general wage rate increases only to those workers whose wage rates had risen less than the 15% which the cost of living had advanced between January 1941 and May 1942. Other factors continued to be considered in granting individual wage increases.

At that time the War Labor Board had authority only over cases under dispute between management and workers. As time passed and the manpower situation tightened, employers began to grant wage increases voluntarily in order to hold or attract manpower. By last Fall it became evident that control only over wages in disputed cases would be entirely inadequate to prevent inflationary wage increases. As a result, the Emergency Price Control Act of 1942 was amended and an Executive Order was issued on October 3, strengthening both wage and price control.

The Executive Order gave the War Labor Board authority over all wage increases including those voluntarily granted by the employer. In delegating this authority to the War Labor Board the Executive Order stated that the Board "shall not approve any increase in the wage rate prevailing on September 15, 1942, unless such increase is necessary to correct maladjustments or inequalities, to eliminate substandards of living, to correct gross inequities, or to aid in the effective prosecution of the war". The War Labor Board also was given authority to make such exemptions from this part of the Order in the case of small total wage increases as it considered necessary for the effective administration of the Order.

Neither the Act nor the Executive Order clearly defined inequalities, gross inequities, or the other factors which could be used to justify wage rates higher than those on September 15, 1942.

The War Labor Board issued several orders defining some of the exceptions and exemptions such as: (1) exemption of small firms (8 or less employees) from wage control; (2) workers who had received less than the 15% permitted under the Little Steel formula were to be covered by the gross inequity exception, and (3) permission for individual wage increases as a result of promotion or reclassification, merit, seniority, operation of piece-work, or incentive programs, and operation of apprentice or trainee programs. But in the main it followed the practice of deciding each individual case on its merits without stating specifically the conditions which must exist in order to justify wage increases under any of these clauses.

The "Little Steel" formula took account only of the increase in living costs up to May 1942. The War Labor Board assumed that the other points of the Seven-Point Program would be made effective and that living costs would be substantially stabilized. However, living costs continued to advance, especially food prices. By February 1943 total living costs were over 4% above May 1942. Food costs (according to official indexes which understate the actual rise) advanced 10%, led by a 17% rise in farm prices in the same period. Farm pressure groups were apparently intent on forcing still higher farm and food prices, even refusing to accept subsidies which could be used to prevent further increases in urban living costs.

Labor thus became restive and pressed for an upward revision of the Little Steel formula. Lewis openly stated that he was going to break the formula and get a $2 a day increase for his miners. Several important cases were pending at the time including the meat packers, West Coast Airframe, and others. Byrnes encouraged the War Labor Board to stand firm on these cases and the Board did so at the risk of losing its labor support and its existence.

Prices continued to go up; Congress passed the Bankhead Bill which would have raised living costs materially; Congress was at the point of passing the Pace Bill which would have raised living costs still further; OPA policy seemed to be turning in the direction of permitting price increases, relaxing enforcement, and abandoning safeguards against offering lower quality goods at prices fixed for higher qualities; farmers were still refusing to accept incentive payments to keep farm prices and living costs stable.

The situation was clearly critical. If farm prices and food prices were permitted to advance further it would be practically impossible to prevent Lewis from getting higher wages for the miners. If miners' wages were allowed to increase, the CIO and AF of L, both of whom had supported the President in his stabilization efforts, would have to ask similar increases for their members. It was clear that either the line had to be held or another round of inflation suffered. Strong action had to be taken. The Executive Order was the action taken and it appears to have been strong enough to give stabilization another chance.

The effect of the Executive Order on wages is to deny the War Labor Board power to authorize any further increases in wages above the Little Steel formula except those clearly necessary to correct substandard living conditions. Subject to the general policy of the Director of Economic Stabilization, reasonable adjustments in cases of promotion, reclassifications, merit, and incentive wages, etc. may still be made, provided such adjustments do not increase production costs appreciably or furnish the basis for price increases. Specifically, this means that the War Labor Board may no longer grant wage increases to correct maladjustments or inequalities, to correct gross inequities, or to aid in the prosecution of the war, except when, and if, authorized by the Economic Stabilization Director. The Order resulted in the immediate wiping out of 10,000 cases, affecting from 500,000 to 1,000,000 workers, already before the War Labor Board, and in eliminating the legal basis of Lewis' demands for higher mine wages.

In addition, the Order directed the War Manpower Commission to prevent employers from hiring new employees at rates above those received by employees in their previous jobs, unless the change in employment will aid in the prosecution of the war.

The Executive Order also stiffened OPA policy on price increases, added weight to the veto of the Bankhead Bill, discouraged reintroduction of the Pace Bill and gave clear assurance to labor and consumers that the cost of living was going to be held or even reduced toward the September 15th level. This assurance was necessary in order to make labor willing to go along at all on a wage freeze of such rigidity.

Thus the immediate effect of the Executive Order is to remove Lewis' threat to the Little Steel formula, to forestall thousands of wage increase requests, to reduce pressure for higher farm prices, and to increase substantially the possibility of obtaining Congressional approval for subsidy programs. The Order, if the proper policies continue to be followed, makes possible the development of a real stabilization program.

It is clear, of course, that living costs cannot be frozen unless effective efforts are made to reduce the amount of money in the hands of the public by raising taxes.

The elimination of "inequalities" as a justification for increases is defensible in time of war as a means of checking the growth of inflationary pressures. But if the policy of "no increases to correct inequalities" is rigidly enforced, a great deal of labor unrest may be expected to develop, which will be reflected in job-shifting with the subject of finding the highest-paying employer. It is quite common for wage rates, especially in plants and areas where employment has been expanding rapidly, to differ by 10-50% for exactly the same work. The best cure for this trouble is the kind of standardization illustrated by the recent War Labor Board decision covering the West Coast Airframe Industry in which job classifications and pay rates were made uniform for all firms in the area.

It is doubtful whether the War Manpower Commission has adequate administrative machinery to check labor turnover, even with the authority, given it by the Order, to prevent the hiring of new employees at increased wages. The existence of the authority, however, will probably prevent some pirating and job-shopping and will strengthen the War Labor Board in its handling of wage requests based on the necessity of stopping the movement of workers to higher-paying jobs.

If the wage freeze is really effective, it will eliminate opportunities to increase income by changing jobs or by using bargaining strength. Opportunities to increase income by doing more work ought to be left open. With this purpose, the War Labor Board ought to encourate the development of incentive wage systems. Such systems will increase output per man-hour, bring down labor costs, and reduce manpower requirements.