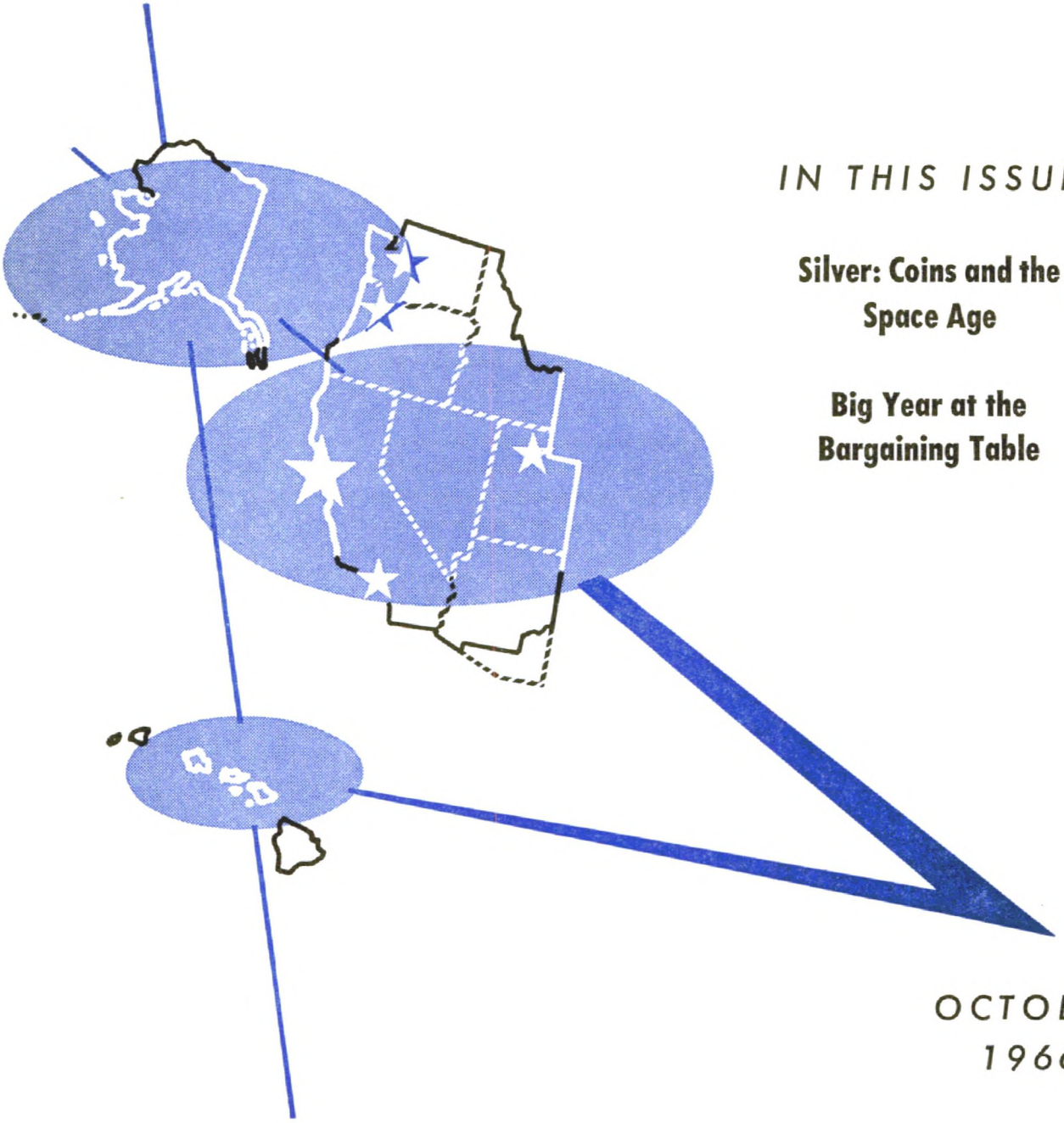
FEDERAL RESERVE BANK OF SAN FRANCISCO

MONTHLY REVIEW



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OCTOBER 1966

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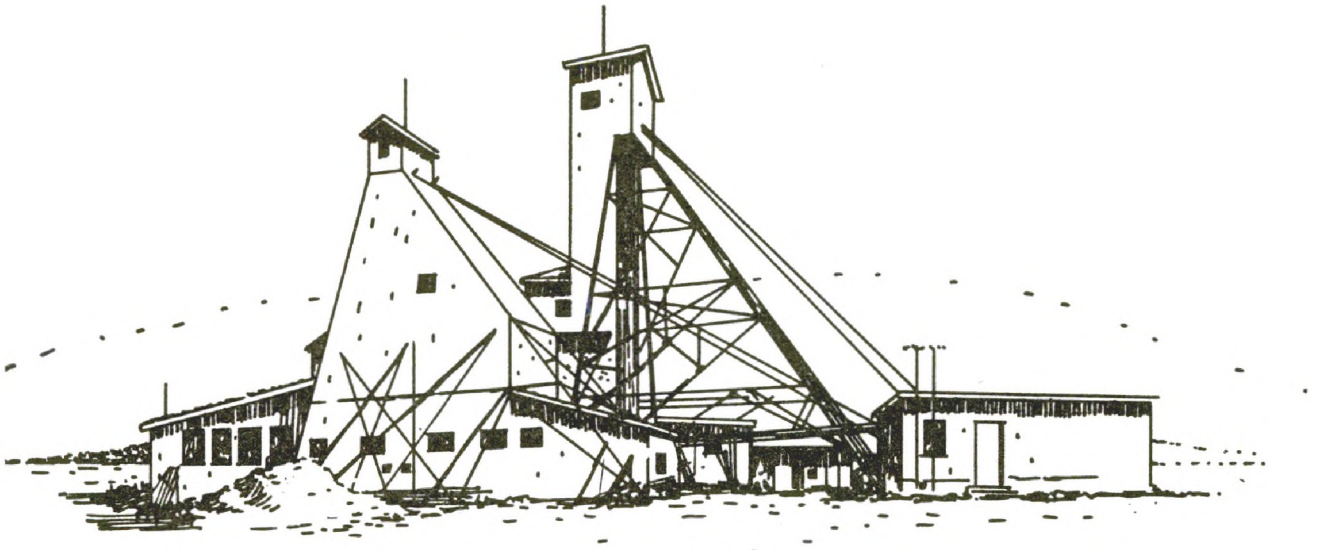
Big Year at the Bargaining Table

. . . The entire economy—not just the 2½ million affected workers—will feel the impact of upcoming labor-contract negotiations.

Editor: William Burke



Silver: Coins and the Space Age

SILVER'S remaining ties with our monetary system were almost completely severed on July 23rd of last year, when President Johnson signed into law the Coinage Act of 1965. A generation or two ago, when the mere mention of silver could arouse the emotions of men, the move would have caused a furor. Instead, the new Coinage Act — which made the first fundamental change in the nation's silver coinage since 1792 — sailed through Congress with a minimum of controversy, while the clad coins it created were accepted by the public with a minimum of complaint. Since the silver shortage threatened to exhaust U.S. Treasury stocks of the metal within three years, the need for remedial action of this type had become apparent to almost everyone. What follows is, first, a summary of the historical background to the Coinage Act and, second, a report on the status of this precious metal after a year's experience with the new legislation.

Confronted by the problem of rapidly dwindling supplies, arising from the growing imbalance between production and consumption of the metal, the Administration had moved early in this decade to assure the nation enough silver to meet its coinage requirements. On November 29, 1961, President Kennedy directed the Treasury to suspend its sale of free silver and to inaugurate a program for the gradual retirement of $5 and $10 silver certificates. The measure was designed to release for coinage some 400 million ounces, out of the total reserve of 1,700 million ounces of silver, which had been held as backing for these and other certificates.

Later, under the Act of June 4, 1963, the Treasury began to redeem silver certificates at $1.2929 an ounce to meet industrial demands, but at the same time the Federal Reserve began to issue $1 Federal Reserve notes in order to eliminate silver as backing for these certificates.

In April, 1963, Treasury Secretary Dillon had told the Senate Banking and Currency Committee that, with the passage of the proposed legislation, the Government's silver reserves would "assure an adequate supply of silver to meet our coinage requirements for the next ten to twenty years." But as 1964 progressed, consumption of silver came to exceed all earlier expectations, and it became readily apparent that even the Act of 1963 had failed to provide a lasting solution to the Treasury's problems.

Growing deficit

Production of silver in the United States had fallen short of consumption consistently throughout the postwar period, but the gap began to widen appreciably after 1958. While domestic production actually declined slightly from 1958 to 1963, consumption for coinage and industrial use rose sharply, from 124 to 222 million ounces. As a result, the annual deficits increased from a sizeable 100 million ounces or so in the 1950-58 period to a very substantial 187 million ounces in 1963. But then, in 1964, the deficit jumped to 289 million ounces, as consumption soared from 222 to 326 million ounces and production rose only moderately to 37 million ounces. Moreover, since foreign production began to lag behind consumption by a sizeable margin, total world consumption (outside the Soviet Bloc) amounted to more than two-and-one-half times total new production in 1964. With metal usage at 556 million ounces, the supply deficit in that year was 338 million ounces.

Foreign sources thus filled less and less of the U.S. deficit, because of the expanding needs for the metal abroad. At the same time, returns of lend-lease silver dropped steadily from a peak of 103 million ounces in 1958 to zero in 1963. In making up the growing deficiency, Treasury stocks receded by 523 million ounces in the five-year period, to 1,583 million ounces in 1963.

Then, in 1964, foreign demands actually comprised a drain on Treasury stocks, and this country became a net exporter of silver for the first time since the lend-lease shipments of World War II. Total exports during the year amounted to 110 million ounces, more than triple the 1963 figure, while imports declined from 64 to 55 million ounces. In meeting this demand plus the soaring domestic demand, Treasury stocks of the metal dropped 23 percent in 1964 alone, to 1,214 million ounces.

Industrial consumption

An increase in industrial consumption of silver, mainly for use in photographic film, electrical and electronic components, and storage batteries, helped to intensify the growing shortage. Industrial consumption in this country dropped from an annual average of 100 million ounces in the early 1950's to 86 million ounces in 1958, but in the next five years it rose by more than 5 percent annually, and in 1964 it jumped by 11 percent, to 123 million ounces.

Overseas, the expansion in industrial consumption had been even more impressive, particularly in West Germany and Japan. Between 1950 and 1958, foreign industrial consumption doubled, and by 1964 it increased again by half, to 163 million ounces. Just by itself, world industrial consumption exceeded production by 71 million ounces in 1964.

Excess industrial demands were met by the public through the redemption of silver certificates. With each dollar exchangeable for .7734 ounces of silver, the availability of Treasury supplies held the market price at $1.2929, the level first reached in September 1963. Yet in addition to this drain, the public withdrew 70 million ounces for speculative holdings and inventory accumulations, for a total of 141 million ounces in redemptions.

Nevertheless, by far the largest drain on Treasury stocks resulted from the tremendous expansion in silver usage for coinage. The actual silver crisis might have been delayed for years had not a terrific coin shortage developed.

Soaring coinage

Consumption of silver for U.S. coinage began to rise sharply in 1961. In the next two years, consumption for this purpose doubled, reaching 112 million ounces in 1963. Even with this, the demand could not be met, and the shortage of coins turned critical around mid-1964.

At one time limited to relatively few geographical areas, to particular coins, and to particular seasons of the year, the shortage eventually became a general problem affecting the entire economy. Merchants found it difficult, and in some instances impossible, to make change. Banks, unable to satisfy their customers' requests for coin, found it necessary to ration their supplies. In fact, coin rationing was instituted down the line—from the mints, to the Federal Reserve, to the commercial banks, to the public.

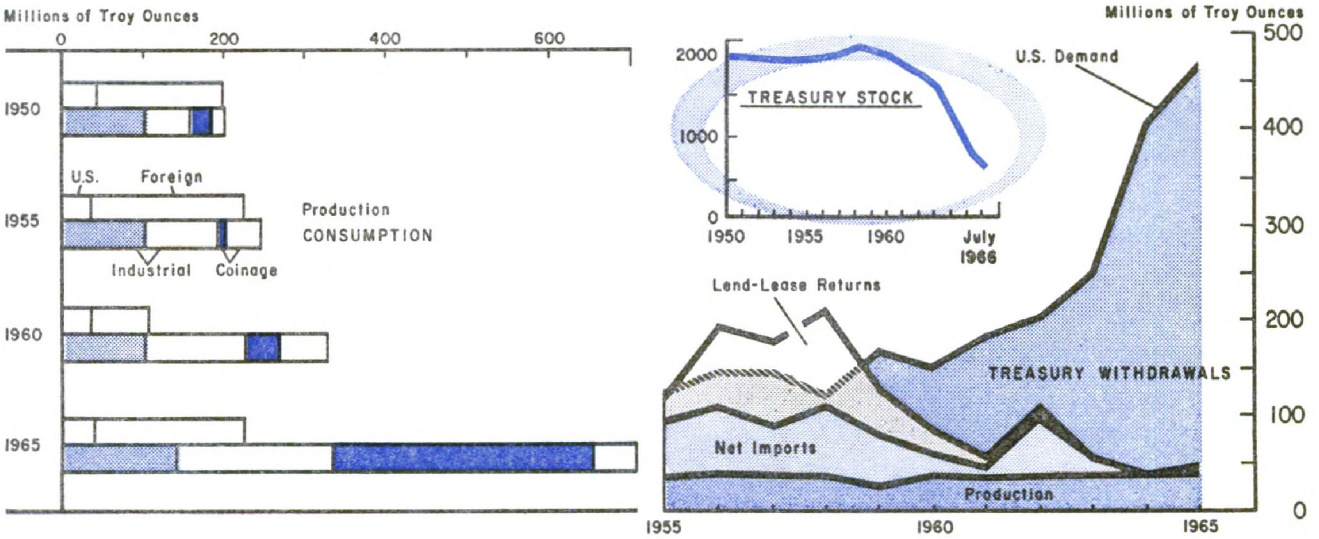
A new type of entrepreneur, "the money merchant," appeared on the scene, acquiring coins by the bagful and trying to sell them to the highest bidder. The American Bankers Association staged a "Calling All Coins" campaign which was designed to bring to market the large supply of coins stored in the nation's piggy banks. One chain of food stores conceived of the idea of issuing scrip, in denominations of 1, 5, and 10 cents, redeemable at the company's stores, but dropped the plan when it found that it might be violating Federal law.

A number of explanations were offered for the shortage. The most widely-accepted explanation emphasized the growing use of some 12 million automatic coin-operated vending and service machines—ranging from parking meters and telephone pay stations to machines that dispense hot and cold drinks, sandwiches, candy, cigarettes, music, and laundry and dry-cleaning services—and the growing coin requirements of toll roads, sales taxes, and school lunches. Another popular explanation blamed the shortage on the burgeoning demands of a rapidly growing population and a rapidly expanding economy.

According to Mint Director Eva Adams, the expansion in coin production should have been more than adequate to compensate for all these developments. From fiscal 1959 through fiscal 1964, the Mint had nearly tripled the production of coins, from 1.6 to 4.3 billion pieces, while population had increased 8 percent, gross national product 28 percent, and vending machine sales by 47 percent, over that period. Furthermore, the 48 billion coins available for circulation provided an average of 240 coins for every man, woman, and child in the United States.

The Committee on Government Operations, investigating the coin shortage, drew attention to the problem of *availability* as opposed to the actual *supply* of coins. Large

Silver consumption soars under impact of coinage and industrial demand
. . . deficit covered only through rapid depletion of Treasury stockpile



amounts had been placed in circulation, but large amounts had been withdrawn, by businessmen anxious to assure themselves of an adequate supply for the needs of trade, by the nation's 8 to 10 million coin collectors—and by speculators, who bought up new coin by the roll, by the bag, and even by the ton in the hope of profiting from a possible increase in the price of silver or coin. (Incidentally, vending industry spokesmen pointed out that, although some $3,500 million in coins went into the nation's millions of vending machines annually, only about $22 million remained in the machines at any one time.)

This explanation also received support from the records of the Federal Reserve System. As commercial banks found themselves with less and less coin, the "flowback" of coin returned to the Federal Reserve Banks had dropped sharply, from 11.4 billion coins in fiscal 1962 to only 6.7 billion pieces in fiscal 1964. Deliveries of new coin from the Mint had risen, but the added supply had been more than offset by the drying up of return flows from circulation. By mid-1964, the return flow had shrunk to the point where it was less than the amount of new coin received from the Mint, whereas in more normal times the return flow was nine times as great as Mint deliveries. Consequently, the Reserve Banks were unable to deliver coin on request and had to ration the limited supply.

The tendency to hoard apparently had snowballed. The rise in the price of silver to $1.2929 an ounce and the fact that the silver dollar was worth a dollar of silver undoubtedly had encouraged the run on silver dollars at the Treasury early in 1964. Then, when the Treasury had exhausted all but 3 million "cartwheels" and, amidst great publicity, was forced to restrict redemption of silver certificates to bullion, broad new public interest in coins was stimulated.

The withdrawal of coins gathered further momentum when the Treasury, on March 24,

issued the Kennedy half-dollar. The coin was not a commemorative piece and was intended to circulate freely as just another coin. Instead, people all over the world sought to keep it for sentimental and esthetic reasons. The demand was so great that the coin sold at premiums wherever available. In Italy it brought $15, in Hong Kong $5. In this country, many people were unable to obtain even a single coin, although they sold for as much as double face value when first issued. (Coin fanciers with short memories should be reminded that the same type of shortage occurred when the Lincoln-head pennies first made their appearance in 1909.)

Crash cure

Whatever the reasons for the coin shortage, Treasury officials decided that it could be overcome only by a rapid and substantial increase in production. By flooding the economy with coins, they hoped to convince those who held them for speculative reasons that the market would soon be saturated.

At first, the Treasury had planned to boost production as efficiently and economically as possible at the existing mints, while meeting long-range needs through the construction of a new Philadelphia mint authorized by Congress late in 1963. The new mint, after its completion, should be capable of producing as many coins as the Denver and old Philadelphia mints combined.

Events, however, forced the adoption of

another approach. In mid-1964, the mints were put on a round-the-clock seven-day-a-week intensified "crash program" designed to double the annual production of coins from 4 to 8 billion in a year's time. The program included expanded purchases of equipment and utilization of mint properties—including the production of annealed blanks for nickels and pennies at the U. S. Assay Office in San Francisco—and the purchase of metal strip for coinage from private industry. Legislation also was sought and passed (on September 3, 1964) to continue the 1964 date on new coins indefinitely. Its purpose was to provide so many coins bearing that date that the incentive of dealers and hoarders to divert such coins from normal commercial uses would be destroyed.

As 1964 drew to a close, the Treasury was well along in its program. During calendar year 1964 the Mint produced 5.5 billion coins, compared with 3.4 billion pieces the year before. Production in the last six months was nearly 60 percent higher than production in the second half of 1963—and it was also equal to the entire production of coins in 1962. But about 203 million ounces of silver were consumed during 1964's rapid upsurge of Mint production. In fact, about 73 million ounces went into the production of some 200 million Kennedy half-dollars which disappeared almost immediately as souvenirs and collectors' items.

Western lawmakers meanwhile succeeded (July) in persuading Congress to appropriate $600,000 for the minting of 45 million silver dollars, so dear to the heart, mines, pockets, and slot machines of the West. All of the new silver dollars were to be shipped directly from the Denver mint to Western Federal Reserve Banks for distribution to commercial banks serving the areas where silver dollars were used as a medium of exchange. Even so, many observers predicted that the new silver dollars would disappear into the hands of collectors and speculators—just as 460 million others had already vanished. Thus, in view of the likelihood of hoarding and in view of the consequences of diverting silver and production facilities that could be more profitably used in alleviating the shortage in smaller denominations, the silver dollars were never struck.

In February 1965, the Director of the Mint was able to report a definite improvement in the coin situation. Businessmen were able to get through 1964, including a busy Christmas, without an actual crisis, even though retail sales in 1964 were $29 billion higher than in 1963. The shortage of pennies, which at one point had been critical, was completely relieved, while the shortage of nickels was almost over. Nonetheless, shortages continued in the silver coins, and the half-dollar was not circulating at all.

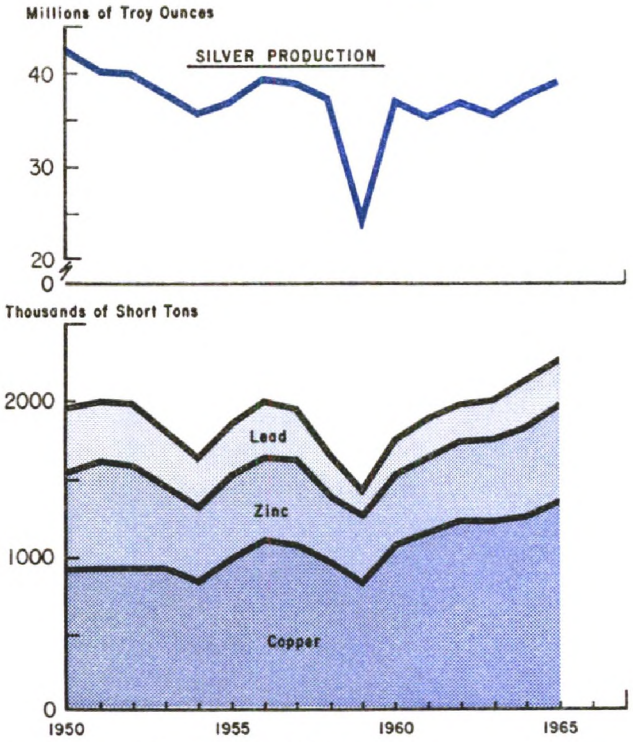
At the same time, the problem of silver supplies had grown more acute. Production of coins in the fiscal year ending June 30, 1965 reached 7.3 billion pieces, but, during that June, the use of silver in coinage ran at an annual rate of 300 million ounces, while the Treasury's supply was down to 1,000 million ounces.

Obviously, unless production increased or consumption declined, Treasury stocks of the metal would be depleted in about three years. In that event, the mints would have to stop coining dimes, quarters, and halves of the kind then in use. The Treasury would no longer be able to offer silver to all comers at $1.2929 an ounce. The price of the metal might rise beyond $1.3824—the point at which the silver content of these coins would be equal to their face value—and coins would begin to disappear from circulation.

Inelastic supply

Prospects were slim for an expansion in world production large enough to reduce the deficit appreciably. Despite a 40-percent in-

Silver obtained mostly as byproduct of copper-lead-zinc mining



crease in the price of silver, from an average of $.925 an ounce in 1961 to an average of $1.2929 an ounce in 1964, domestic mine output had moved up only slightly, from 35 to 37 million ounces, and still remained below the average level maintained during the early 1950's. In addition, there were reasons for believing that any future expansion would also be small.

Expansion of silver production always had been made difficult by a simple fact of technology. Two-thirds of the nation's silver is traditionally recovered as a co-product or a by-product in the treatment of base metal ores—copper, lead, and zinc. As such, the demand and price for these metals influence production of silver to a larger extent than the demand and price for silver itself. Since production of two of these metals (lead and zinc) actually had declined over the past fifteen years, silver's sluggish output was all but inevitable. In addition, 90 percent of the nation's measured silver reserves were located in base metal deposits of this type.

Furthermore, silver production from these mines would depend on the quality as well as the quantity of the ores being worked. For example, porphyry copper deposits, a major source of primary copper in this country, contain a very low percentage of silver (0.02 to 0.11 ounce recovered per ton of ore), but they had remained a major source of silver because of the vast tonnages mined and processed each year. Yet in view of the mining of ores of lower silver content, production of silver declined slightly between 1950 and 1964, even in the face of a 50-percent rise in copper production.

The postwar trend in foreign production had been somewhat more favorable. Output abroad rose fairly steadily until 1958, but annual production then held at around 170 million ounces until 1962, before rising further to 180 million ounces in 1964. Two-thirds of the silver recovered abroad each year is processed as a by-product. Nevertheless, a rise in base-metal prices after 1961 had intensified mining of such deposits throughout the world, and thereby had helped expand silver output.

Higher silver prices had helped to stimulate exploration for new deposits and the development of previously by-passed marginal veins at primary silver mines—those in which the value of silver constituted over half the total value of the ore. Extensive exploration was being carried out, for example, in the Coeur d'Alene region of Idaho, the location of all four of this nation's primary silver mines. One venture, the "Rainbow" project, included the sinking of a 3,500 foot shaft, to reach deeper veins of silver.

The real hope for a substantial production increase, however, rested on the discovery of silver bonanzas similar to the Comstock Lode. One such discovery was made at Timmins, Ontario, in late 1963. Ore reserves at that Canadian site were estimated at 55 million tons, and averaged 7.08 percent zinc, 1.33

percent copper, and 4.85 ounces of silver per ton.

Recognizing the pressing need for new silver discoveries, Interior Secretary Udall in late 1964 directed several agencies to expand exploration activities. Thus, in September of that year, the Office of Minerals Exploration increased the percentage of Federal financial assistance from 50 percent to as much at 70 percent of the total cost of new exploration ventures.

In addition, the Geological Survey initiated a reconnaisance program designed to indicate likely areas of near-surface silver deposits in various Western states. The program included geologic mapping and geophysical and geochemical studies of target areas, utilizing the latest instruments and techniques—including an instrument capable of detecting mercury, which is generally located with silver deposits. Old districts such as the Comstock and the Tonopah were scheduled for study with the new techniques in the hope of discovering additional reserves.

Meanwhile, some unexpected target areas showed definite promise. Some bedded sandstone, for example, was found to contain appreciable amounts of silver, particularly in the Silver Reef deposits of Utah, and the same was true of black calcite deposits located in some Western mining districts. Also, on the basis of a Geological Survey report, a deposit near Battle Mountain, Nevada, was being tested by a mining company as a potential copper-gold-silver producer.

Despite this progress, however, it was evident that, even if new discoveries were made, substantial increases in silver output would be slow in reaching the market, because of the time required to bring new properties into production.

Projecting supply

On the basis of projects definitely underway or with definite financing, the American Mining Congress projected in 1964 an 18-percent expansion in total world production (outside the Soviet Bloc) over the 1964-68 period. A later Bureau of Mines study projected a much smaller expansion of total supply, but both studies envisioned a substantial increase in U. S. production.

This country, as the world's second ranking producer, was expected (according to the AMC study), to increase output by 8.3 million ounces over the 1964-68 period. Most of the increase was to come from the following: in Utah, the opening of a high-grade lead-silver deposit in the East Tintic district and expansion of copper production at Bingham Canyon (3.3 million ounces); in Montana, expanded output at Twin Buttes and Flat Head (2.5 million ounces); and in Idaho, increased output at Silver Summit (1 million ounces). Copper projects at Battle Mountain, Nevada, and Mineral Park, Arizona, and a newly discovered lead field in south-central Missouri, were to account for the remainder.

Mexico, for many years the world's largest producer, was expected to supply only 2 million additional ounces—a smaller increase than that of any other major silver-producing country. The AMC study based its pessimistic forecast on the Mexican industry's heavy tax burden as well as the restrictions on foreign investment in that industry.

On the other hand, Canada's output increase was projected at more than 13 million ounces, with most of the expansion coming from the newly found deposit at Timmins, Ontario. The remainder was to originate from a new lead-zinc mine in New Brunswick, a copper-zinc mine at Lake Dufault, Quebec, and the Granduc and Western copper mines in British Columbia.

Australia was to contribute an additional 6.3 million ounces, mainly from a project which was scheduled to double lead production at Mount Isa. In Peru, expansion planned at Cerro de Pasco and four smaller mines was

expected to contribute about 2.8 million ounces. The Philippines, Ireland, and France meanwhile were slated to increase production by anywhere from 1.5 to 3.0 million ounces each over the four-year period covered in the AMC study.

Neither the import trade nor the recovery of secondary silver appeared capable of closing the gap in domestic supplies. Imports of silver, emanating mainly from Canada, Mexico, and Peru, declined sharply after 1962, while exports, destined mainly for the United Kingdom, France, West Germany, and Japan, accelerated until a net export balance developed in 1964. Moreover, the recovery of silver from secondary sources—such as scrap silverware, photographic wastes, and worn coins—increased appreciably in the 1955-61 period but then receded to only 12 million ounces by 1964.

Inelastic demand

A decline in industrial demand might, of course, have eased the situation, but this appeared extremely unlikely. In many of its most important industrial uses, the demand for silver had proven to be inelastic—unresponsive to an increase in price—because no known alternative equaled its high electrical and heat conductivity, resistance to corrosion, and sensitivity to light. In fact, industrial consumption in this country rose 11 percent in 1964, despite the 40-percent increase in the price of the metal in the previous two years.

Consumption of silver for photographic film, plates, and sensitized paper, which together comprise the largest market for the metal, increased at an annual rate of about 2 percent between 1959 to 1963, and then jumped 20 percent, to 40.3 million ounces, in 1964 alone.

The photographic industry's consumptions would have increased even more rapidly had it not learned to economize on its supplies. By extracting silver from photographic solutions used in developing film, for example, it was able to reclaim as much as 10 million ounces in 1964.

Under the stimulus of the sharp run-up in silver prices, the industry also accelerated its research aimed at the development of substitutes. In many of silver's most important applications, however, no other material could be found with silver's unique ability to record an image when exposed to light. (The only major alternative was the use of electrostatic copying methods in office equipment.) Because silver was all but indispensable to the photographic process, its use in this field was expected to increase along with the continued growth of the industry.

The electrical-equipment and electronics industry was one of silver's most rapidly growing outlets. Consumption of silver in these fields rose almost 50 percent between 1959 and 1964, from 20.5 to 30.3 million ounces, and, as a result, the industry surpassed silverware and jewelry to become silver's second largest market.

Unequalled as an electrical conductor, silver's use as an electrical contact had expanded until it could be found in practically every on-off switch and electrical appliance. Silver-wire contact relays also were at the heart of most computers and almost every piece of telephone and aviation equipment. According to industry sources, approximately three-quarters of the silver used in this field went into voltage connections for such important uses as space-vehicle guidance systems and military electronic systems, and for these uses there is no known substitute for silver.

Consumption in brazing alloys and solders, another rapidly growing field, expanded from 10.5 million ounces in 1959 to 15.8 million ounces in 1964. During World War II the use of silver alloys as industrial joining media gained impetus in the manufacture of shells, gun parts, and ordnance. After the war, silver

brazing alloys became important in air-conditioning and refrigeration equipment, electrical appliances, and automobile parts—in fact, in virtually every end-product where joining or bonding was involved. And entirely new applications also arose: silver-infiltrated tungsten for rocket fuels, as well as silver brazing alloys capable of withstanding heat and pressures generated at supersonic speeds. For these applications, which require high-temperature soldering, substitution of other materials was completely impractical.

Consumption of silver in storage batteries, a relatively new use, almost tripled between 1959 and 1964, reaching 9.0 million ounces. In fact, the development of high-energy batteries had been largely dependent on the increasing use of the metal. Batteries utilizing silver, when coupled with zinc or cadmium, can be recharged, and they are very useful for applications requiring high output in relation to weight, such as for spacecraft and portable tools and appliances. Because these batteries rely on the chemical reactance of silver, the substitution of other materials again would not have been feasible.

For all these reasons, the industrial demand for silver had expanded inexorably, even in the face of stable or declining demand for the metal in its more traditional uses. Silver consumption in dentistry, medicine, and mirrors had increased very little in recent years. Meanwhile, consumption for silverware and jewelry had actually declined, from 28.0 to 22.5 million ounces in the 1959-64 period, as a result of the rising price of sterling silver and the increasing acceptance of stainless-steel flatware of modern design. But in all other uses, the industrial demand for silver had mushroomed in the early 1960's.

Treasury's position

In view of the soaring industrial and coinage demand and in view of the rapid depletion of its silver stock, the Treasury was forced

to take a long, hard look at the silver content of the nation's coins. Then, after a two-year study, the Treasury in its *Staff Study of Silver and Coinage* (May 1965) concluded that, "the world and the U. S. silver supply and production situation and outlook do not warrant continuation of the large-scale use of silver in the U. S. coinage." Moreover, since subsidiary silver coinage of reduced content undoubtedly could suffer from difficult transitional problems and from the fear of future changes in silver content, the Treasury argued for a once-and-for-all change: "If any silver is to be retained in the subsidiary coinage system, it should be limited to a clad silver piece of 400 fineness."

On the basis of technical studies, the Treasury recommended cupronickel clad on a copper core as the best metal for a new and permanent subsidiary coinage. This material was acceptable on the basis of its ability to provide uninterrupted service as a medium of exchange; its acceptability to the public

in terms of weight, color, wearing qualities, and operation in vending machines; its ease and certainty of production; its cost and availability; and its compatibility with present coinage.

Cupronickel, already used in the U. S. 5-cent piece, was the most widely used coinage material in the world. It had circulated side by side with silver coinage in high-denomination coins in the United Kingdom. Coins of cupronickel clad on a copper core could operate in vending machines rapidly without the difficulty, expense, and inconvenience of modifying existing rejectors. Furthermore, the Mint had made sizeable production runs using the cupronickel clad material without encountering serious difficulties.

According to the Treasury, the cost of the alloy—45 cents a pound, based on 33-cent copper and 79-cent nickel—would be much less than silver at $18.81 a pound. Coinage at the projected fiscal-1965 rate would require approximately 5,355 short tons of copper and 1,785 short tons of nickel annually. In both cases, the tonnages would represent a fractional part of total domestic consumption and could be drawn from surpluses in the strategic stockpile.

The Coinage Act

Many of these Treasury recommendations were contained in the legislation which President Johnson submitted to Congress in June 1965. In the President's words, the legislation would "insure a stable and dignified coinage, fully adequate in quantity and in its specially designed technical characteristics to the needs of our 20th-century life. It can be maintained indefinitely however much the demand for coin may grow".

Immediate action was urgent because, "There is no dependable or likely prospect that new, economically workable sources of silver may be found that could appreciably narrow the gap between silver supply and demand. . . . The one part of the demand for silver that can be reduced is governmental demand for use in coinage". That reduction in governmental demand would amount to an annual saving of some 90 percent of the silver formerly used for coinage.

Public Law 89-81, the Coinage Act of 1965, passed virtually in the form presented by the Administration. The new half-dollar was to be a composite coin—an outside layer (80 percent silver and 20 percent copper) clad on an alloy core (21 percent silver and 79 percent copper). To the naked eye the coin would be almost indistinguishable from the old half-dollar, but it would contain 40- instead of 90-percent silver. The new dimes and quarters, although identical in size and design to the former 90-percent silver coins, were to be silverless. Each of these also would be a composite coin—an outer layer (75 percent copper and 25 percent nickel) clad on a core of pure copper. The Act did not call for any change in the silver dollar, but it specified that none be minted for five years.

The Government's readiness to sell silver bullion from its stocks at $1.2929 an ounce had already provided protection against the melting of silver coins by effectively preventing the price of silver from rising above the face value of the coins. Now, since the Treasury intended the silver coins to circulate alongside the new coins, the Act provided further protection for the silver coinage by authorizing the Secretary of the Treasury to prohibit the melting, treating, or export of any U. S. coin. Again, to discourage hoarding, it stipulated that any 900-fine coins minted after the law's enactment would be inscribed with the date 1964.

Finally, the legislation authorized the President to establish a Joint Commission on the Coinage, composed of the Secretary of the Treasury, the Secretary of Commerce, the Director of the Bureau of the Budget, and eight representatives each of the Senate, the House,

and the general public. The Commission was to study the progress made in the implementation of the new coinage program and to make recommendations on such matters as the economy's need for coins, technological developments in metallurgy and coin-selector devices, the supply of the various metals, the future of the silver dollar, and the time and circumstances in which the Government should cease to maintain the price of silver.

Consumers vs. producers

Despite the diversity of interests with a stake in silver's future, public opinion, as expressed in Congressional hearings on the Coinage Act, was virtually unanimous that the silver content of the nation's subsidiary coinage would have to be cut. Emotions ran high, however, on the question of "how much".

Silver users, anxious to have ample supplies of the metal available at stable or declining prices, wanted silver to be completely eliminated from the coinage. They pointed out that total world production in 1965 would be some 100 million ounces less than industrial consumption alone, and that the use of 15 to 30 million ounces per year in the Kennedy half-dollar would only divert supplies that could more beneficially be used in industry and the arts.

Silver users reasoned that, under the new legislation, Treasury silver requirements for coinage would drop about 90 percent, to around 30 million ounces annually; in fact, this figure would drop to only 15 million ounces when the production of half-dollars was reduced to more normal levels. With the exception of Canada and Switzerland, most other countries had already eliminated or drastically reduced the use of silver in their coinage. Foreign use of silver for this purpose had declined one-fourth between 1961 and 1964, to 62 million ounces, and, according to expert testimony, could be expected to drop to 30 million ounces by 1970.

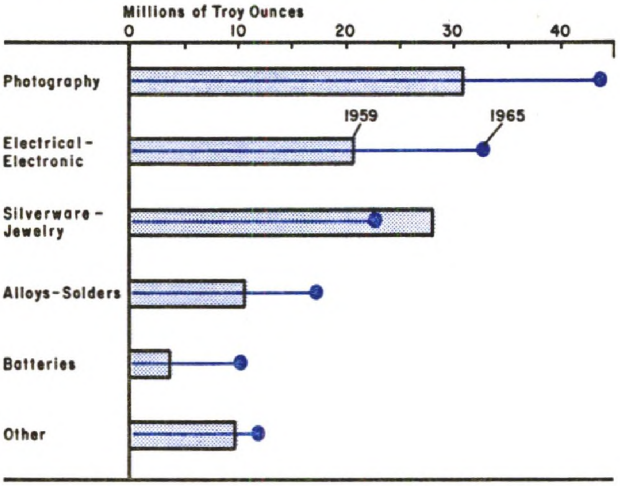
If worldwide industrial consumption were to increase by 25 percent by 1970—less than the increase over the prior five years—it would reach 360 million ounces. In that case, world industrial and coinage demand could total 420 million ounces in that year.

Yet, according to the most optimistic estimate of the American Mining Congress, total world production at best would increase in the interim by only 35 percent, to 290 million ounces, leaving a worldwide deficit of some 130 million ounces. Secondary sources could (optimistically) be expected to supply no more than 50 million ounces of this calculated deficiency. The remainder of the deficit would have to be met from Treasury stocks—but that source would be completely depleted by 1970 under present and projected consumption patterns.

Silver producers took a somewhat different view of the future. Fearing that a sharp swing away from silver might trigger a price break, they argued for the retention of silver in the coinage to the maximum extent feasible. They claimed that the gap between supply and demand had been abnormally inflated in 1964 by the hoarding of both Kennedy half-dollars and some 70 million ounces in other forms. Furthermore, they argued that annual world production could increase by as much as 55 million ounces by 1968 on the basis of current exploration, and that this increase and the gradual recovery of the 1,800 million ounces of silver outstanding in coins would permit the retention of some silver in both the 50-cent piece and the smaller denominations as well.

Western governors argued that the only real way to prevent the eventual depletion of Treasury stocks would be for the Government to allow the price of silver to rise in a free market. In their opinion the Treasury's proposals would do nothing to further any increase in the production of silver and would

Most industries boost silver buying sharply as new applications develop



only aggravate the coin shortage. At their conference at Portland, Oregon, the Western governors therefore resolved "that Congress provide for retention of silver in reduced amounts in all coins now silver, that an affirmative program be adopted to increase exploration for and development of domestic silver supplies, and that silver be permitted to seek its own price in the market place."

The vending industry, with its $3.5 billion annual take in coins, wanted coins that would be "compatible" with the nation's 12 million coin-operated merchandising and service devices. About half of these devices would reject coins not having the correct electrical properties, and to change them would require three years' time and an expenditure of perhaps $100 million. Furthermore, the industry wanted coins that would pose no inconvenience to the consuming public, which plunked 30 billion pieces into these machines annually for over 12 billion cups of coffee, milk and soft drinks, about 4.5 billion candy bars, and numerous other goods and services.

Finally, almost every company with a material in any way suitable for coinage—from aluminum to zirconium—pressed its claim for inclusion in the new coinage.

A bit for everyone

Actually, the Coinage Act was a composite package containing something for nearly everyone. For Western silver producers, silver kept at least a stake in the coinage, with the new half-dollars requiring at least 15 million ounces per year. Producers also received the assurance of a minimum of $1.25 per ounce for their silver.

Silver users did not get an entirely silverless coinage, but they did get silverless dimes and quarters. In addition, the continued redemption of silver certificates by the Treasury provided an effective ceiling on the price—at least for awhile. The vending industry supported the new coinage, because the cupronickel and copper coins had the same electrical properties as the silver coins and worked satisfactorily in existing machines.

The keenest disappointment was felt by speculators who had been gambling on higher silver prices. The price of silver on the exchanges dropped by as much as 3 cents an ounce upon enactment of the new legislation.

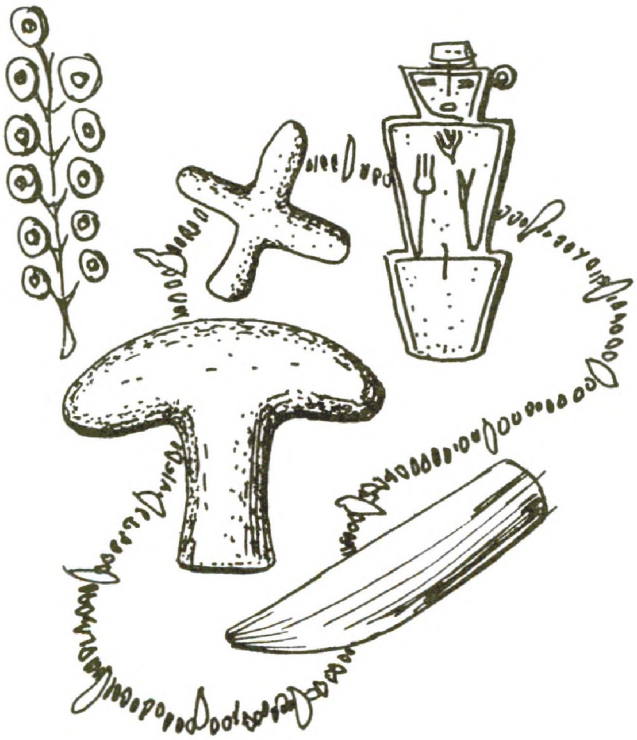
Stamping out the shortage

Considering the persistence of the coin shortage, the release of the new coins apparently did not come a moment too soon. Despite the continued expansion in production of silver coins under the "crash program," Federal Reserve inventories of quarters had shrunk to only 15 million pieces for the entire nation by November 1, 1965, when the tremendous demands of the Christmas season were just beginning.

The far-reaching provisions of the Coinage Act, which authorized the reactivation of coin production at the San Francisco Assay Office, expenditures for the construction of new facilities, and the acquisition of necessary metallic strip, equipment, and supplies, enabled the Mint to achieve an unprecedented rate of production earlier than anticipated. Early in November the Mint was able to release over

230 million of the new clad quarters, backed up by a very large production stream amounting to a quarter-billion pieces a month—four times the highest production rate ever previously attained. These new coins carried the economy safely through the Christmas season without a crisis.

Early last February, when almost 700 million new quarters already were in circulation and the first new dimes and half-dollars were about to be released, Assistant Treasury Secretary Wallace told the Senate Subcommittee on Government Operations that "the supply of our most vital coins—the quarter, dime, nickel, and penny—is in better shape now than in any comparable period during the last ten years. . . . There is no shortage of those coins most vital to the transaction of business." Flowback and inventories at the Federal Reserve Banks had increased in all denominations except the half-dollar. Relatively few of the latter were in circulation, although more than 480 million Franklin half-dollars had been minted between 1948 and 1963 and almost as many Kennedy half-dollars had been issued in the last several years.



All in all, the Mint estimated fiscal 1966 production at about 9.3 billion coins, one-third of them being clad coins. For fiscal 1967, it estimated production at about 13 billion coins—about 10 billion in clad coins and the balance in the "minor" coins (nickels and cents).

The Treasury's objective was to manufacture enough of the new clad coins within a two-and-one-half-year period to replace, if necessary, the 13 billion old dimes and quarters now in circulation—and to build up an emergency inventory. Total production for fiscal years 1965-67 was scheduled at 34 billion coins—enough to provide every person in the country with 180 additional pieces.

From the point of view of its silver supply, enactment of the Coinage Act apparently did not come a moment too soon for the Treasury. Stocks dropped 35 percent in 1965, to 804 million ounces, mostly because of withdrawals for the minting of silver subsidiary coins.

Meanwhile, although U. S. mine production rose by over 5 percent, from 37 to 39 million ounces, industrial consumption rose by 14 percent to 140 million ounces, its highest level since 1945.

The Coinage Act touched off a wave of liquidation of speculative holdings, however, and redemptions of silver certificates in 1965 amounted to just over 77 million ounces. After passage of the Act, withdrawal rates declined from an average of almost 14 million ounces per month to an average of 4 million ounces per month. In addition, total exports of silver dropped 7 million ounces below imports, to 48.5 million ounces, or less than one-half the quantity exported in 1964.

The lid on $1.2929

How has the new coinage affected the supply, demand, and price outlook for silver? The changeover to the new coinage has slowed down, but by no means eliminated,

the drain on Treasury supplies. This year the Treasury will require 50 to 60 million ounces for coinage. Production of the 90-percent silver coins ended in April, earlier than expected, and coinage requirements since that time have been running at an annual rate of about 32 million ounces—only one-tenth of the 1965 rate.

Withdrawals by the public for industrial use and speculative and inventory holdings, by means of the redemption of silver certificates, averaged 12.5 million ounces per month during the first eight months of 1966. If that rate continues, redemptions this year will drain off about 150 million ounces, and stocks could drop as much as 210 million ounces by year-end, to just under 600 million ounces. Of that total, 165 million ounces must be set aside as a stockpile for critical defense needs.

Treasury officials are convinced that even this dwindling supply will be adequate to keep the lid on prices for some time to come. The Treasury, moreover, according to its agreement with the Office of Emergency Planning, will be able to dip into the defense reserve if its use becomes necessary to meet "critical national needs." The Secretary of the Treasury also has at his disposal a more drastic alternative: the regulation or prohibition of exports, as authorized by the Coinage Act. But export controls in effect would separate the U.S. and foreign markets, and might result in an increase in world prices above the U.S. price. As a consequence, silver ordinarily imported into this country could be diverted to foreign consumers, thus frustrating the Treasury's objective.

The question of the price ceiling will not even be considered until the President has convened the Joint Commission on the Coinage. The Commission's work must wait until the transition is far enough along to provide a sound basis for assessment, not only of the silver situation, but also of any other problems arising in connection with the new coinage. One such problem, for example, may be a scarcity of copper. As a result of releases to industry to meet a tight supply situation, the Government stockpile now amounts to only 409,000 tons, against a national objective of 775,000 tons.

Opinions vary widely regarding what would happen when (or if) the $1.2929-per-ounce ceiling is removed. Most silver dealers do not expect the price to skyrocket. They point out that if the price reaches $1.38 an ounce, it would become profitable to melt 900-fine subsidiary coins for their silver content, thus opening up a potential lode of perhaps 1,800 million ounces. But speculators disagree, and have backed up their opinion by bidding up silver futures and mining stocks, and in some cases hoarding bullion.

Perhaps the difference of opinion is based on timing. Treasury stocks should be sufficient to hold the price at $1.2929 an ounce during the transition period to mid-1968. Beyond that date, the silver outstanding in the old-style coins will provide a restraint on the price. But at some time in the distant future, perhaps ten years from now, even that supply may be exhausted. Between now and then, we may ponder the Treasury's conclusion, as stated in its *Staff Study of Silver and Coinage*: "Analysis of supply and demand factors does not yield any precise estimate of the level that silver prices might reach in a free market."

—*Yvonne Levy*

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Big Year at the Bargaining Table

OVER the next twelve months, labor and management teams will be hammering out major contracts for almost 2½ million workers in some of the nation's largest and most important industries. The outcome of these negotiations — in electrical products, trucking, autos, meatpacking, and other industries — will help to determine the level of employers' costs and thereby influence the course of the continuing struggle against inflation.

The numbers involved, although three times as great as the total for the preceding four quarters, are not substantially larger than during the last major period of negotiations. Rather, the recent public interest in the negotiations stems from the economic environment surrounding the contract talks, and this environment is almost certain to influence the substance of the agreements as well as the incidence of labor strife over coming months.

A lack of slack

Vital factors in the economic environment include: a tight labor market, evidenced by the lowest sustained rate of unemployment since 1953 and marked shortages in skilled occupations; Federal legislation boosting the minimum wage and broadening its coverage; and a recent spurt in wages and average employee compensation accompanied by a slowdown in the growth of manufacturing productivity. As a result, unit labor costs in manufacturing, for the first time since 1960, are running ahead of year-ago levels. Such a trend puts pressure on profits or prices — or both.

Labor's determination to achieve the best possible settlement has been growing as union analysts note the hefty growth in profits during the present decade and the accelerated rise in living costs during the last year or so. Union leaders are interested in protecting workers' purchasing power and are distressed to find considerable gains in wages and fringe benefits being erased by a combination of higher social-security taxes and rising consumer prices. Ahead of them, too, they see the possibility of an increase in personal-income taxes. The revival of popularity of the recently ignored escalation clause, which ties wages to living costs, is one symptom of the attempt to minimize the impact of rising prices on workers' purchasing power.

The final factor causing concern over upcoming negotiations is the record of the recent past. The anticipated breathing spell in labor relations failed to materialize this year. Greater-than-guidelines wage settlements became relatively common, and work stoppages — statistically insignificant but editorially newsworthy — caused public discomfort and aroused considerable sentiment for more effective mediation procedures.

Bargaining playbill

First in line for renewal are contracts covering almost 175,000 workers in the electrical-products industry, terminating this quarter. The largest union — the International Union of Electrical Workers (IUE) — presented demands fairly representative of the sentiment expressed in numerous labor conventions this year, but somewhat different from the demands presented at the last round of contract talks three years ago. At that time, national prosperity was still plagued by a relatively high level of unemployment. Organized labor responded by concentrating on job security, the distribution of available work, and the reduction of technology's impact on employment — often at the expense of money in the pay envelope.

Although these earlier goals are far from forgotten, more emphasis is now being placed

on larger paychecks. Moreover, as a union with new leadership, the IUE might be expected to take a firmer bargaining position and be more responsive to local union problems than otherwise.

The electrical workers' bargaining goals include annual wages (so as to put production workers on the same footing with salaried white-collar employees), reduced geographic wage differentials, and increased job security, as well as increases in fringe benefits and pay. The pay demands include a "catch-up" wage increase to compensate for the years without escalator clauses, reinstatement of escalator provisions, and larger boosts for skilled workers. The companies' original offer amounted to four percent a year in increased costs, so the new contract may well set the stage for substantial increases, above the 3.2-percent guideline, in other bargaining situations. Most business observers have been carefully watching the negotiations unfold — and several Cabinet members took an active part in negotiations in early October, in an attempt to bring about a settlement for national security as well as national economic reasons.

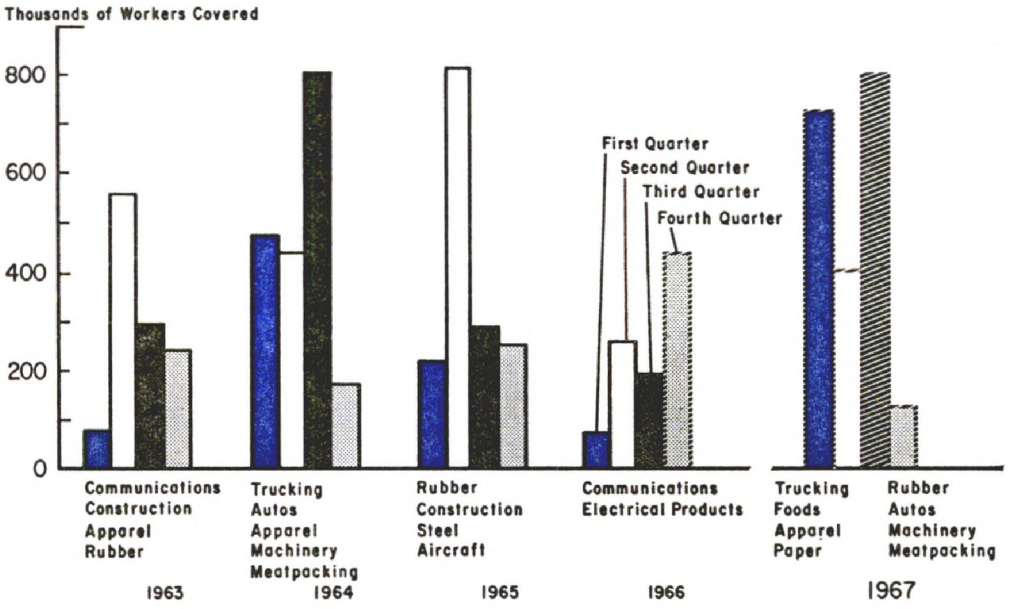
The eventual settlement included many 1966-model features. An extension of the deadline brought about a national agreement involving a 5-percent boost in costs, but local issues precipitated strikes at plants across the nation. One of these strikes, at a key defense plant, was halted by an injunction under the Taft-Hartley Act.

Throughout the autumn months contracts are also expiring with telephone companies across the nation. The largest union involved, the Communications Workers of America, gained a 4.6-percent wage boost and a wage-reopener clause in negotiations concluded in September, but the union membership rejected that agreement in early October. In any event, the September contract remains the "pattern agreement" for bargaining in the communications industry, which will continue into the spring of 1967.

The new year will usher in the contract deadline at major oil refineries. In 1964 these workers asked for a 5-percent annual wage boost, and received 4.5 percent. Now, the union has made the 5-percent boost "mandatory" for a settlement which will establish the pattern for 45,000 workers outside the refineries themselves. Another large contract due to expire in January will bring the ILGWU together with dress manufacturers. And in February, the Teamsters' contract with California food processors and growers comes up for renewal.

By the end of this year, negotiations will

Bargaining activity on many labor fronts scheduled to rise sharply in coming months



probably begin for renewal of the "National Master Freight Agreement" which runs out March 21. The contract, between the Teamsters, the nation's largest union, and Trucking Employers, Inc., an employer group organized in response to demands for a national agreement, covers about 450,000 employees of 15,000 companies. The union's goal of a single standard agreement for drivers from Maine to California bore some fruit in the 1964 agreement, which put a floor under wages and benefits and covered non-monetary items, but left some regional questions unsettled. Twenty regional supplementary agreements which cover local conditions and wages will expire at various times throughout 1967. Local differences proved difficult to iron out in the earlier negotiations, and the union will try to come closer to its single-contract goal in 1967. In March, also, a bargaining deadline faces Pacific Coast pulp and paper manufacturers.

Later negotiations

During the second quarter, contracts will expire at a somewhat less hectic pace. Major contracts will be renewed in the rubber industry in April, and in cement in May and June. The leading rubber companies will face, in the new leadership of the United Rubber Workers, a negotiating team that is committed to a stiffer bargaining position than heretofore.

At mid-year bargaining deadlines will occur for the crucial copper industry. Since that industry is plagued by short supply, labor difficulties in overseas producing centers, and a domestic price level below that of the world market, a repetition of the work stoppage which occurred in 1964 could prove serious for defense and civilian production. The summer quarter, moreover, will also be contract time for the major meatpacking firms.

Next September, the UAW's 600,000 production workers will reach the end of their old contract with the Big Three automakers. The present set of agreements, signed in 1964 after a series of workstoppages, added about 4.5 to 5 percent to the companies' labor costs. But whatever the size of next year's wage package, its implications will be substantial for American industry, since the giant union's membership includes agricultural-equipment and construction-machinery workers as well as autoworkers — and since the size and shape of the UAW package will influence negotiations throughout the manufacturing sector.

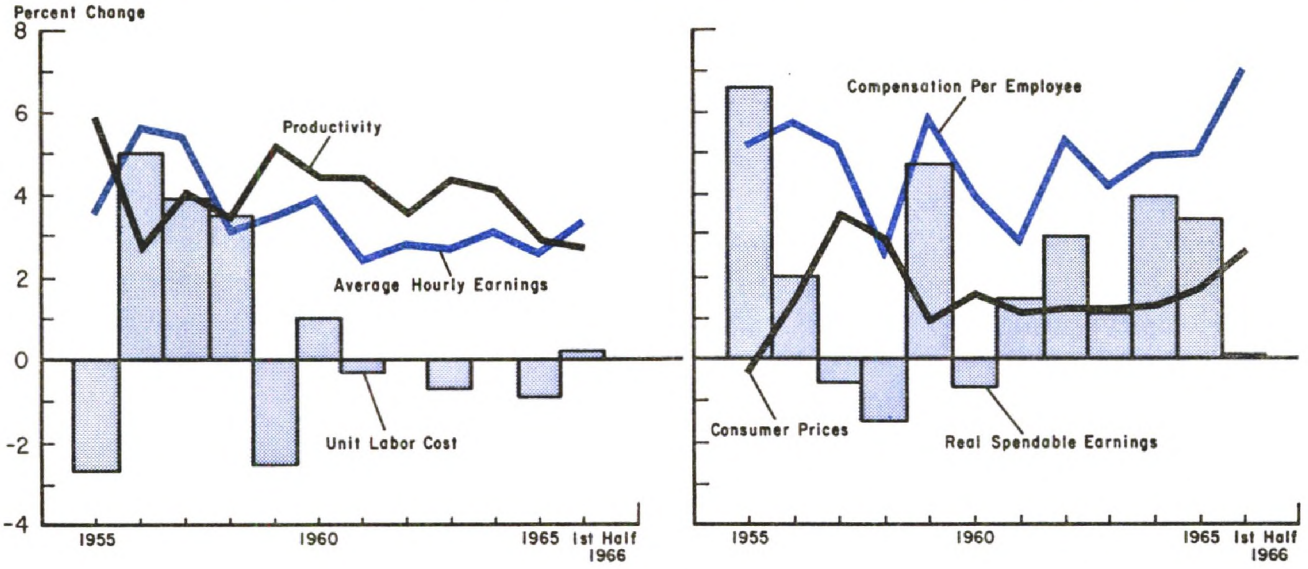
A contract calendar is, at best, an imperfect guide to the timing of new contracts, although the expiration of each old contract generally serves as a starting point for some newly-won benefits. Union members may stay on the job long after a contract has expired, especially if some progress is recorded in bargaining sessions. The deadline may be postponed voluntarily, as it was in the steel industry in 1965, or it may be extended by legal constraint, as in the airlines in 1966.

On the other hand, disputes may arise when a contract is still in force. Wages may be reopened for discussion during the life of a contract, or a wildcat strike may develop our grievances. Disputes may also arise in industries which have open-ended contracts, such as in the railroad industry. (The automobile industry for example has been plagued by wildcat walkouts this fall, although the contracts do not expire for another year.) And yet, despite all these qualifications, the contract calendar outlined above provides a reasonably good indication of the economic pressures that may arise on the labor-management front over the next year.

In the West

The major bargaining situations in this coming period will vary widely in their regional impact. Their direct impact on West-

Employers now see rise in labor costs as wage gains outstrip productivity, while employees enjoy smaller gain in real earnings because of rising prices



ern workers and Western businessmen will obviously depend upon the regional distribution of employment in the industries now gathering at the bargaining table.

Roughly one out of every eight of the nation's workers is employed in Western industries. In oil refineries the ratio is closer to one in six, and a similar ratio holds for the electrical-products industry. Bargaining in these industries, and in other Western-oriented industries such as telecommunications and trucking, will have a significant impact on the Western economy.

Negotiations in other industries will have a relatively small direct influence on this region. Only one apparel worker in twenty works in the West, the proportion is only slightly greater in the rubber industry, and Western labor will have virtually no involvement in next summer's talks with major meat-packing firms.

At the same time, some negotiations which do not involve many people nationally are very important to the region. This was true in 1966 for negotiations with long-distance bus lines, which involved a lengthy walkout, as well as those at Pacific Coast ports, which were settled without interruption of work. The same will be true in 1967 for California processors and growers (February deadline) and for Western pulp and paper companies (March deadline). And renewal of pacts in copper mining in July will be of special importance to the West because of the industry's concentration in this region.

Moreover, even those industries with a relatively low concentration in the West may play a very significant economic role in the various communities where their facilities are located. The best example is the auto industry, which is important regionally even though only one of every 25 autoworkers is employed in the West.

Interaction

Of course, the effect of a new labor agreement goes far beyond the workers and firms directly involved in its creation. The Western worker and his family are also consumers, and Western producers act as suppliers, competitors and buyers to firms in other industries in other parts of the country. Thus, an interruption of production, or an agreement leading to readjustments of prices in industries three thousand miles away, will involve the worker or businessman in Los Angeles, Boise,

or Honolulu. And the settlements which he himself makes will spread their effects across the country as well.

Agreements increasing wages, wherever they occur, may affect other workers and employers throughout the entire labor market. Thus, much of the concern at present centers on the impact of hefty settlements on labor costs throughout the economy. One large, well-publicized settlement, it is argued, with or without interruption of production, will affect wage settlements of: other workers involved in the industry's bargaining round; other workers with similar jobs, or belonging to the same union, in entirely different industries; employees in unrelated jobs in the same company or industry; the next contract to expire, whatever its coverage; and non-union hiring, especially in a tight labor market where employers must bid for qualified workers in order to fill their mounting orders. The shortage of certain skills is most important in boosting wages at the upper end of the pay scale. At the other end, and of equal concern, is the newly-enacted Federal minimum-wage legislation.

Pay raise for millions

In terms of its ability to fatten pay envelopes, the minimum-wage legislation dwarfs even the largest union contracts. The new act will raise the wage floor from $1.25 to $1.40 next February 1, and to $1.60 a year later, for almost 30 million workers now covered. Nearly 6 million of these employees earn less than $1.60 at present. In addition, coverage will be extended for the first time to some 8 million workers in retailing, restaurants, hotels, laundries, taxi fleets, logging, agriculture, education and Federal Government, at an initial rate of $1 an hour.

For farm workers — completely excluded in the past — the minimum will advance by two annual 15-cent-an-hour steps, to $1.30 on February 1, 1969. The law affects only those farms using more than a certain minimum number of man-days, and it excludes family members and commuters working during peak seasons. The minimum for other workers covered for the first time will advance in four annual steps, to $1.60 by 1971. Part of the increase in coverage is due to a reduction in the annual-sales figure which is used as a yardstick to determine whether or not a business must pay its employees a minimum wage.

Legislation setting wage floors are common among states as well as on the national level. All nine states in the Twelfth District have minimum-wage laws setting statutory or wage-board rates, although minimum wages in Arizona, California, Oregon and Utah apply only to women and minors.

Wage floors are part of national policy to aid workers at the bottom of the wage scale, to raise their standard of living. Opponents of increased minimum wages (and their extension to millions of additional workers) argue that they tend to eliminate low-skill jobs and thus destroy opportunities for the workers the legislation is designed to help. Moreover, they claim that boosts in wage floors are inflationary, causing upward pressures on wages throughout the economy as other workers seek to retain current differentials. The latter argument is eliciting the greatest interest nowadays, in light of the contracts coming to term in the near future.

New areas involved

Two categories which have been closely involved in the accelerated rise in prices over the last year are agriculture and services. These sectors have also been involved in a new trend in organizational activity and labor disputes, along with an upward movement in wage floors.

Unionization in agriculture has been a slow process, hampered by problems inherent in organizing a scattered and sometimes migra-

tory work-force. Farmowners have resisted unionization, arguing that their perishable crops are vulnerable to harvest-time strikes and that output cannot be recouped in such cases. Nonetheless, the organizing drive gained speed this year. At the beginning of 1966, fewer than 2,000 workers — out of a total employment of 300,000 workers on California farms — were covered by union contracts. Thus, contracts signed this year with California grape growers represent a significant breakthrough, despite their limited coverage.

Public and professional services have been considered so vital to society that many states have passed anti-strike laws, and professional groups have adopted voluntary rules barring walkouts. Yet this year has witnessed strike action by public-health doctors, social workers, and a variety of municipal employees across the country. California experienced, in one community or another, walkouts or threatened walkouts by teachers, nurses, and other professionals.

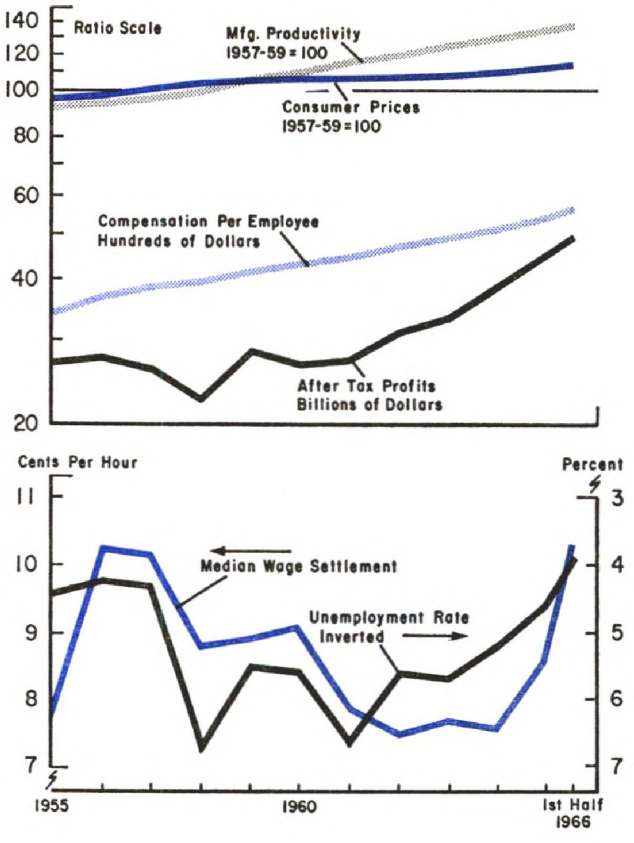
The walkouts may not be labeled strikes, and they often are in violation of statute. But the tight labor market, and the shortage of certain essential skills, render stiff legal penalties difficult to enforce against de facto strike action. The problem is one of discovering effective alternative methods of allowing these employees to press their demands. Although their services are essential, and their productivity difficult to assess, professional public-service workers feel that they too should be allowed to better their economic position.

Labor: cost or paycheck?

Gains in wages and fringes, or reduction of hours, are translated into rising labor costs to industry. Boosts in manufacturing hourly earnings moved within a fairly narrow range earlier in this decade, below the average increase for the last half of the 1950's. Equally important, productivity gains were substantial enough to produce a slow decline in labor costs per unit of output. This year, however, productivity gains have been smaller than before and labor costs have increased at a faster pace than productivity, with the result that unit labor costs have turned upward.

Labor costs are likely to continue rising in coming months, but the extent of the increases will depend, at least in part, upon the size of the new contract settlements. Productivity gains may be aided by the new plant and equipment now coming on stream, but if these gains fail to counteract rising wage scales, unit labor costs will accelerate. The result will be a growing pressure on profit margins and on prices — especially in light of the suspension of the investment-tax credit and accelerated-depreciation procedures. Any difficulty in boosting prices, due either to the

Wage pressures reflect rising prices, profits, productivity—and more jobs



force of competition or to public pressures, would be certain to stiffen management's bargaining stance.

Organized labor's bargaining stance meanwhile may be stiffened by concern over labor's falling income share and its rising cost of living. The basic position, expressed recently by the AFL-CIO Executive Committee, is that "Wage and salary earners have not received a fair and adequate share of the benefits of the economy's forward advance." Labor spokesmen base their argument on a comparison of the recent path of profits and worker's compensation: from 1960 to 1965, after-tax corporate profits soared by 67 percent, or twice the percentage increase in compensation of employees.

In response, management argues that labor, by looking at the last five years, is seeing only part of the picture. During the last half of the 1950's, when wages and salaries rose 30 percent (and wage supplements jumped 77 percent), profits after taxes showed a slight overall decline. Profits are necessary for continued expansion, and the "feast" years thus are seen as making up for a period of "famine."

Meanwhile, just as industry watches unit labor costs and profit margins, the worker is interested in the purchasing power of the money he takes home. Labor negotiators accordingly attempt to win pay raises large enough to counteract anything that threatens to reduce the size or the value of the pay envelope. In recent years average employee compensation registered substantial advances, while taxes declined and consumer prices rose only slowly. This year, however, retail prices are rising at a faster pace, and increased social-security taxes are cutting into take-home pay. As a result, real spendable earnings of the average factory worker are no higher now than they were a year ago. And for 1967, the use of a tax increase to combat inflation — a move which would reduce spendable earnings — seems a real possibility.

Up the down escalator?

One method of protecting wages against rising prices is through the negotiation of an escalator clause — a contract provision tying workers' wages (usually) to changes in the consumer price index. During 1966 about 2 million union workers were covered by major contracts containing escalation clauses, and another 500,000 unorganized employees received cost-of-living adjustments.

Seven out of ten (1.4 million) of the union workers are in manufacturing. The largest group (about 600,000) is in the automotive industry, where the first escalator clause was negotiated by the United Auto Workers in 1948. Next in size is the Teamsters' agreement with the trucking industry. Escalator agreements are common in farm and construction equipment, aerospace, and meatpacking; there are some in chemicals, retail trade, and public transit; but they are virtually unknown in other industries. In construction, the only escalator contract of any consequence is one which will provide cost-of-living adjustments for 10,000 Los Angeles painters starting next year.

Changes in the consumer price index are the most common basis for calculating wage escalation, but other measures may be used instead. One contract (with an Indiana bakery) in good classical fashion ties wage increases to the price of a 20-ounce loaf of bread. (The workers have received three escalation boosts within the last twelve months.) Another calls for a pay boost to cover a possible increase in New York City's subway fare.

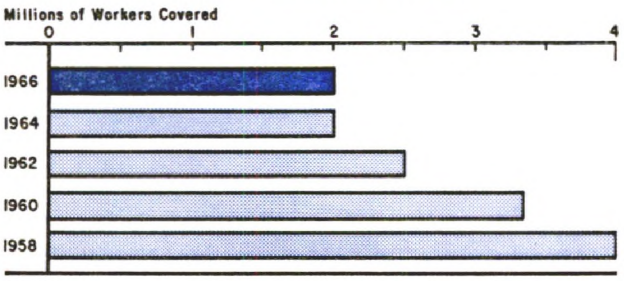
Over the last three years, the number of workers covered by escalation clauses has remained at the 2-million mark. Nonetheless, cost-of-living clauses have varied widely in popularity over time, depending upon the course of consumer prices. Coverage reached

about 3.5 million in 1952, fell as prices remained level after the Korean War inflation, and increased in 1956 as prices moved upward again. That year marked the first such clause in the steel, aluminum, and meatpacking industries, and the reinstatement of escalation clauses by railroad unions. By 1957 the previous peak of 3.5 million was reached once again, and in the following year 4 million were covered — twice the present number. But then, as the price trend lost momentum, the clauses were dropped in favor of other bargaining goals.

In 1966, with the consumer price index accelerating again, escalator clauses are back in style. For example, a cost-of-living adjustment was involved in the contract ending the airline strike last summer; a limited escalator clause had to be included in the final pact after the union membership voted down the initial contract. Other unions have declared their intention to demand escalation clauses in current bargaining sessions. Two electrical unions are asking total coverage under cost-of-living adjustments, and the oil and railroad unions are anxious to win escalation clauses next year.

Despite their attractiveness to labor, cost-of-living adjustments will not be extended without considerable opposition from both industry and government sources. The opposition is based on the fear that escalators contribute to a wage-price spiral. Escalators, the argument goes, increase wages when prices rise — but wages are costs to industry, and as such are likely to touch off another round of higher price tags, followed by another round of higher wages, and thus greater inflationary pressures. In addition, industry objects to such agreements because they provide an added uncertainty in projecting future costs.

Cost-of-living escalator clauses less important than heretofore



Off season?

Although it had been heralded as a slack period for labor negotiations, 1966 opened with New York City's first mass-transit strike. Late in March the railroads experienced a short walkout; in mid-May service on Western bus lines was interrupted for over a month; and early in July the mechanics' union went on strike against five major airlines. With the exception of the railroad dispute, the number of strikers involved in these situations was relatively small, but a considerable portion of the public was involved through inconvenience, disrupted plans, or loss of income in tourist centers. (One of this summer's hit tunes concerned a young man stranded by the airline strike.) Still other disputes have precipitated intensive mediation efforts in response to possible interruption of defense production.

Strikes such as these have produced widespread sentiment for legislation to strengthen the government's hand in dealing with potential walkouts. The costly settlements, in turn, have given rise to demands for re-evaluation of the Administration's guideposts for noninflationary wage and price behavior.

These unexpectedly thorny bargaining situations led William E. Simkin, Director of the Federal Mediation and Conciliation Service, to characterize this year's mediation activity as busier, and the negotiations more difficult, than any he could remember. And the bulk of the bargaining schedule still lies ahead.

— Adelle Foley