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METHODS and PROBLEMS of PRICE Control

Eugene L. LASH
Maj CAC

Date submitted: 24 May 1949

Methods and problems of price control, by
Maj E. L. Lash. CGSC. 1948-49.

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COMMAND AND GENERAL STAFF COLLEGE
FORT LEAVENWORTH, KANSAS

Logistics Specialized Course
Regular Class, 1948-49

METHODS AND PROBLEMS OF PRICE CONTROL, AND THEIR
APPLICATION TO MOBILIZATION PLANNING

EUGENE L. LASH
Major CAC

Date submitted: 24 May 1949

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Command and General Staff College
Department of Logistics
Fort Leavenworth, Kansas

File No. 8-18

20 May 1949

SUBJECT : Methods and Problems of Price Control, and
their Application to Mobilization Planning.

1. PROBLEM-To present the methods and problems of price control as related to war conditions and mobilization planning, and to evaluate their application in current mobilization planning.

2. ASSUMPTIONS-That, in the event of mobilization, price control will be necessary.

3. FACTS BEARING ON THE PROBLEM-There is no statutory authority for the existence of a price control agency, with the exception of limited authority for the administration of rent control legislation.

4. DISCUSSION-(See ANNEX 3.)

a. Direct price controls on all commodities, applied immediately the need becomes evident, will stabilize prices and prevent speculative buying; however, indirect or selective controls applied to basic or critical materials will decelerate price increases in some commodity areas.

b. The need for advance planning demands existence, at top governmental level, of an adequate agency for continuous planning and rapid expansion to meet war price emergencies. There is no such agency.

5. CONCLUSIONS-That an agency should be established capable of continuous planning and expansion to meet war price emergencies; and that such an agency should be within the structure of the National Security Resources Board.

6. ACTION RECOMMENDED-

a. That the Director of Logistics, GSUSA, submit to the Legislative and Liaison Division, Department of the Army, for presentation to the Congress, legislation substantially as outlined in ANNEX 4.

b. That this study be approved and forwarded to the Director of Logistics, GSUSA, for consideration (ANNEXES 1 and 2).

Eugene L. Lash
EUGENE L. LASH
Major CAC
Student

ANNEXES: 1. Draft memo to the Commandant, C & G S C.
2. Draft letter of transmittal to the Director of Logistics, GSUSA.
3. Discussion of price control methods and problems.
4. Outline of recommended legislation.
5. Bibliography.

Concurrences : (Omitted)

Nonconcurrences : (Omitted)

Consideration of nonconcurrences : (Omitted)

May 1949

APPROVED

F. A. HENNING
Colonel, FA
Director

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ANNEX 1

COMMAND AND GENERAL STAFF COLLEGE
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SUBJECT: Methods and Problems of Price Control

(IDENTIFY THIS MEMORANDUM SLIP WITH PAPERS TO WHICH ATTACHED.)

TO	SUBJECT MATTER	FROM DATE AND INITIAL
Commandant, C & G S C	<p>1. I concur in the recommendations of the attached research study.</p> <p>2. Request that this study be transmitted to the Director of Logistics, GSUSA, by means of a letter which has been prepared for your signature.</p>	F.A.HENNING, Colonel, FA Director, Dept. of Log.

COMMAND AND GENERAL STAFF COLLEGE
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ANNEX 2

SUBJECT : Methods and Problems of Price Control, and
Their Application to Mobilization Planning.

TO : The Director,
Logistics Division, GSUSA,
The Pentagon,
Washington 25 D.C.

1. The Attached staff study, "Methods and Problems of Price Control, and their Application to Mobilization Planning," is transmitted to you for consideration and appropriate action.

2. The research study was prepared by a student at this College, and concurred in by the Director, Department of Logistics. The recommendations made for price control planning seem to have considerable merit.

M.S. EDDY
Lt. General, USA
Commandant

ANNEX 3 : DISCUSSION OF PRICE CONTROL OBJECTIVES,
METHODS, AND PROBLEMS, AND MOBILIZATION PLANNING

OBJECTIVES

1. General a. Discussion of the objectives of price control should be prefaced by a brief examination of the influences which the attainment of those objectives will counteract. These influences are of two categories: 1/ Monetary and non-monetary.

(1) Monetary influences result fundamentally from the manner of war financing. Expansion of money and credits, due to increased governmental and commercial loans and bank credits, 2/ creates increased demand for all consumer goods.

(2) Non-monetary influences may be operative regardless of how war is financed. These influences result from vitiation of normal peacetime effects of the competitive price system. They may be generally classified 3/ as : Excess of demand over supply, speculative buying, competitive bidding by armed services and industry, denial of normal sources of supply, and seeking of advantages by organized groups.

b. The effect of combined monetary and non-monetary inflationary influences, resulting from conversion of our economy to maximum war production, is analogous to the effect of dividing a great river, causing part of the water to flow through a new channel, to a new outlet. Expanded demand, credit, and income generate influences

1/ Steiner, George A., Economic Problems of War, New York: John Wiley and Sons, Inc., 1942
2/ Economic Mobilization in a Democracy, Mobilization Branch, Industrial College of the Armed Forces, Washington, D.C., April 1949
3/ Steiner, George A., Economic Problems of War, New York: John Wiley and Sons, Inc., 1942

ANNEX 3

which exert great pressure on commodity prices; the control of prices is one method of controlling the new stream, which must be kept in its channel if a strong national economy is to be preserved.

2.Objectives to be achieved :-Price Control, to be an effective instrument of our national economy in time of war, must, without interfering with the full mobilization of our resources, assist in attainment of the following objectives:

- a. 1/Maintenance of relative price levels commensurate with normal peacetime activity.
- b. Prevention of economically unhealthy inflationary trends.
- c. Timely attraction of adequate materiel and services to war production by means of price action.
- d. Keeping costs of war as low as possible.
- e. Orderly and rapid transition from peacetime to war economy, and from war to peacetime economy.

METHODS OF CONTROL, AND ACCOMPANYING PROBLEMS

3.Fiscal Measures :- a. There are some respected economists 2/3/who believe that price control in a democracy in time of war can be most simply achieved by fiscal action alone. There is obvious logic in their hypotheses:

(1) Taxes in time of war should be increased to such a degree that all surplus or unusual purchasing power in the hands of consumers will be absorbed by taxes.

1/Economic Mobilization Plan, Annex No. 8, Price Control, Industrial College of the Armed Forces, Washington, D.C., 22 June 1948

2/Swanson, Dr. R.B., "Taxation in War", American Economic Review, June 1947

3/OPA Under Review, Department of Research, Industrial College of the Armed Forces, Washington, D.C., March, 1947

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(2) War is fundamentally a current expense in terms of goods and services consumed by war production; postponement of payment in terms of dollars is a matter of political expediency.

(3) Enforced savings will absorb that portion of abnormal purchasing power remaining after taxes.

b. The application of such stringent fiscal measures has, however, apparent disadvantages:

(1) Political inexpediency; by far the greatest proportion of inflationary money is in the hands of people of the normally low-income brackets, whose full, patriotic support of the war effort would be jeopardized.

(2) The slowness and inflexibility of our tax system. In order to meet inflationary trends effectively, tax rates would require adjustment so frequently as to require an extremely complicated and agile tax system.

(3) The doubtful compatibility of severe taxation and compulsory savings.

c. Such fiscal measures as severe taxation and enforced savings, despite their unacceptability as sole means of combating inflationary influences on prices, have, if discreetly used, a vital place in war economy.

2/A most important problem is the control of that portion of inflated incomes that will not be controlled by price-fixing alone. 3/The government must drain this additional purchasing power into the Treasury by moderately severe taxation and by borrowing savings. 4/Bor-

1/Steiner, George A., Economic Problems of War, New York: John Wiley and Sons, Inc., 1942

2/Brown University Economists, Introduction to War Economics, Chicago: Richard D. Irwin, Inc., August 1942

3/Hirsch, Julius, Price Control in the War Economy, New York: Harper and Brothers, 1943

4/Steiner, George A., Op. Cit.

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rowing savings from non-banking lenders is not inflationary; however, the debt must eventually be paid. If the people do not respond well to a program of voluntary lending, the government must resort to enforced saving.¹/In a modern war economy, when the maximum resources of the nation must be mobilized, compulsory savings is a logical and reasonable fiscal policy.²/By savings, either voluntary or enforced, people of the lower-income groups can make an important contribution toward reduction of their future tax burdens.

4. Regulatory measures:--Within the category of regulatory measures will be considered those measures which are required, in addition to a sound fiscal program, to maintain a healthy price situation in time of war mobilization. Specifically, the fields of price-fixing and credit controls will be discussed.

5. Indirect Price Control intends that ³/lower prices of basic commodities will result in lower prices of all finished products. The proponents of indirect controls believe that inflationary prices may thus be prevented with minimum disturbance of established practices.

a. Such a method has limited application if a mobilization should begin in a period of relatively slack production, low employment, and low income.

b. However, ⁴/the prices of unregulated items

¹/Ibid.

²/Katona, George, War Without Inflation, New York: Columbia University Press, 1942

³/Economic Mobilization Plan, Annex No. 8, Price Control, Industrial College of the Armed Forces, Washington, D.C., 22 June 1948

⁴/Baruch, Bernard M., American Industry in the War, New York: Prentice-Hall, Inc., 1941

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enter into the costs of production of basic or critical commodities, and the inflationary increases of unregulated items prices will compel frequent upward revision of prices of regulated items. Furthermore, prices of unregulated items may increase to such a degree that commodity price relationships will become dangerously distorted, and disproportionately low prices of regulated items may attract economically unsound consumption of regulated items. An extreme example of such unsound consumption is to be found in the history of butter price regulation in Germany during and after World War II,¹ when the price of butter was fixed, and the prices of lubricating greases were not fixed. The prices of lubricating greases advanced to such a high level that butter was used for lubricating grease, despite a vital need for edible fats.

c. If indirect or selective controls are applied to basic or sensitive items at the beginning of mobilization, those controls must soon be replaced by direct controls over all commodities, as production expands.

d. The most appropriate use of indirect or selective price controls is during the period of transition from war to peacetime production. During that period of reconversion, control of selected prices should be released, gradually, item by item, as production of consumer goods increases; qualitative controls, rather than quantitative, are desirable during this period.

¹/Hirsch, Julius, Price Control in the War Economy, New York, Harper and Brothers, 1943

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6. Direct Price Controls, by means of which prices are frozen at levels relative to a selected earlier period, is the most expeditious and most equitable 1/form of price regulation. As administered during World War II in the United States, this method 2/allowed for differences in quality, payment for intangibles, varying competitive conditions, and was adjustable to peculiar price and cost situations. If properly planned and well coordinated with other emergency measures of economic mobilization, and if allowed to operate soundly without interference as a result of pressure by organized groups seeking inequitable advantages, direct price control appears the most efficient method of stabilizing prices at acceptable levels. To be fully effective, controls must be applied to all items, essential or non-essential, to prevent diversion of purchasing power to economically wasteful luxury goods.

7. Credit Controls :-a. In war or peace, credit is vital to the operation of our great industrial system. However, in time of commodity scarcity and inflated income, the normal effects of unrestricted credit are undesirable.

b. The expansion of Treasury and banking credit is necessary for funding war production; but 3/qualitative credit controls should be established to restrict banking credit to enterprises which are essential to war production, and such controls may offset, in part,

1/Economic Mobilization Plan, Annex No. 8, Price Control, Industrial College of the Armed Forces, Washington, D.C., 22 June 1948

2/OPA Under Review, Department of Research, Industrial College of the Armed Forces, Washington, D.C., March, 1947

3/Steiner, George A., Economic Problems of War, New York: John Wiley and Sons, Inc., 1942

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the inflationary effects of government borrowing.

c. Consumer credit, particularly in the area of durable consumer goods, must be restricted. Installment-plan sales of automobiles, washing-machines, refrigerators, and comparable items, increases the demand for those scarce items, and at the same time inflates the purchasing power of money in the hands of consumers.

8. Government contract pricing policies during World War II exerted undesirable influences on our price structure.¹ The Reconstruction Finance Corporation, The Commodity Credit Corporation, Defense Plant Corporation, and other specialized agencies were vested with final determination of contract prices. There was no agency empowered to coordinate the pricing activity of those agencies; prices and fees established by them were not in accord with OPA-controlled prices.

a. Future war-time government procurement, whether on fixed-price, cost-plus-fixed fee, or any other basis of price determination, must be so coordinated that contract fees or prices are compatible with industry-wide prices stipulated by price control agencies.

b. Procurement agencies of the federal government were handicapped to a considerable degree ²/by legal technicalities which precluded the development of long-range, firm plans by suppliers.³ Future legislation must permit the nation to profit by the economic

¹/Henderson, Leon, Price, Profit, and Wage Control, Industrial College of the Armed Forces, Washington, D.C., 8 May, 1947

²/Ibid.

³/Purchase, Mobilization Branch, Industrial College of the Armed Forces, Washington, D.C., 6 February 1948

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advantages to be gained by long-range contracts with suppliers.

9. The problem of marginal production :

a. During a war emergency, the national economy requires the use of materials whose production is unprofitable in a peacetime economy; for example, deposits of low-grade mineral ores, or scant timber reserves. During World War II, the price of lead and zinc ores increased so much that it became possible for small, inefficient operators to reap a profit from "mining" slag piles, the waste from more extensive operations in peacetime. The attraction of such marginal production becomes a special pricing problem in time of war.

b. Four methods of solving that problem have been proposed, 1/2 the 'bulk-line' principle, subsidies, government purchase and re-sale, and graded pricing for marginal producers.

(1) The 'bulk-line' method calls for setting a commodity price so high that enough marginal production will be attracted to satisfy the war demand for that commodity. The total production, whether efficiently and cheaply produced or produced by difficult, inefficient and expensive methods, would be sold at the same rate. This is economically unsound, because of the excess price paid for that portion of production which is cheaply attained.

(2) Subsidies are widely applicable for

1/Henderson, Leon, Price, Profit, and Wage Control, Industrial College of the Armed Forces, Washington, D.C., 8 May 1947
2/Brown University Economists, Introduction to War Economics, Chicago: Richard D. Irwin, Inc., August 1942

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attracting marginal production. For example, if twelve cents per pound were determined to be a reasonable market price for efficiently produced copper, let twelve cents per pound be paid to copper producers for that portion of production which is profitable at that price; for all production above that quota, within the requirements for war production, let twelve cents be paid on the commercial market, but allow a government subsidy to reimburse the producer for that portion of production which is otherwise unprofitable. The cost of subsidies should not be allowed to exceed the savings resulting from the low fixed market price of the commodity concerned.

(3) Government purchase and re-sale was practised to a limited degree during World War II; a notable example was alcohol, which was purchased at whatever price allowed separate producers fair profits, but was re-sold at a uniform fixed market price. This technique is applicable to commodity areas in which differing production costs, due to different materials and processes, generally obtain, and is especially applicable to imports.

(4) Graded pricing for marginal production allows the direct payment of prices commensurate with industry-wide production costs, modified to pay increased prices for marginal production. This scheme rewards the more efficient producer by graduating prices directly proportionate to above-quota production. The producer receives direct payment, rather than subsidy payment, for marginal production. This method is especially valuable in a commodity area whose producers are few, but whose total output is large.

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10. Agricultural commodities :-

a. 1/There is no economic basis for the doctrine of farm income parity, which is attained when prices are such as to give farmers a real income equal to that enjoyed by them during the period 1909-14. This doctrine can be sustained only on the grounds that it is politically acceptable.

b. Future war-time conditions will not permit us the luxury of considering the farmer apart from all other producers. The same methods of price control, with such modifications as may be required for the sake of simplicity of administration, are applicable to farm production and industrial production.

11. Public support of Price Controls :-

a. The most troublesome aspect of price regulation is that of obtaining the support of the nation, producers and consumers alike. During the early days of World War II, 2/although there was no legal basis for the operation of the Office of Price Administration and Civilian Controls, public support of that agency, inspired by patriotism, was enthusiastic; there were no organized political blocs opposed to any effort of the OPACC. On the other hand, during the closing days of legal control of prices, although there was a firm legislative basis, upheld by the superior courts, for OPA operation, price control broke down under pressure by organized groups and lack of support by the unorganized majority of our population.

1/Brown University Economists, Introduction to War Economics Chicago: Richard D. Irwin, Inc., August 1942
2/Henderson, Leon, Price, Profit and Wage Control, Industrial College of the Armed Forces, Washington, D.C., 8 May 1947

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b. The people must be educated to tolerate a lower standard of living during a future war emergency.¹ It is far easier to conscript millions of men to risk their lives in combat than to obtain the cooperation of those same men in denying themselves the non-essential comforts whose production is a hindrance to the war effort. Enlistment of public support for an effective program of price control demands a skilful and courageous education program, which must call forth patriotic support without jeopardizing public confidence by calling attention to the bugaboo of inflation.

MOBILIZATION PLANNING FOR PRICE CONTROL

12. General :- Like all other field of mobilization planning, planning for price control in the event of mobilization ^{2/3} must be made well in advance. It is desirable that enabling legislation be prepared and passed by the Congress now, authorizing the President to direct planning for any future war emergency, and authorizing the President to direct immediate implementation of those plans when the need arises. There is now no legislative authority for control of prices, except for limited authority to control rental prices.

13. Machinery for administration of controls :-

a. ⁵ Current mobilization planning envisages

¹/Hirsch, Julius, Price Control in the War Economy New York: Harper and Brothers, 1943

²/Henderson, Leon, Price, Profit, and Wage Control, Industrial College of the Armed Forces, Washington, D.C., 8 May 1947

³/Economic Mobilization Plan, Annex No. 8, Price Control, Industrial College of the Armed Forces, Washington, D.C., 22 June 1948

⁴/Ibid.

⁵/Ibid.

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a price control agency within the framework of an expanded National Security Resources Board. Such an organization is ideal, inasmuch as the expanded National Security Resources Board will control allied problems of economic mobilization, in addition to price control.

b. However, there is no adequate planning agency at that high level. It is highly desirable that our immense resources of industrial knowledge, of economic technology, and of business management be tapped now for continuing studies of price control problems.

c. A nuclear administrative staff, capable of rapid expansion 1/should be established now, within the structure of the National Security Resources Board, to incorporate the experience of World War II and the knowledge of our industrial and economic leaders into planning for a future emergency.

14. Specific Problems to be solved by such a price-control planning agency include, but should not be limited to:

a. Basic price relationships which are desirable to maintain in a war economy.

b. 2/Appropriate control techniques to be applied to specific commodity areas and functional areas.

c. Coordination of emergency military procurement and civilian price policies.

d. Public education concerning the advantages of price and wage stability in a war economy.

End of Annex 3

1/Henderson, Leon, Price, Profit and Wage Control, Industrial College of the Armed Forces, Washington, D.C., 8 May 1947

2/Heflebower, Dr. R. B., Economic Stabilization, Industrial College of the Armed Forces, Washington, D.C., 17 May 1948

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ANNEX 4 : OUTLINE OF RECOMMENDED LEGISLATION
TO ESTABLISH A PRICE CONTROL AGENCY

1. It is recommended that the Congress enact legislation authorizing the establishment, within the structure of the National Security Resources Board, of an agency whose authority and responsibilities will include:

a. Continuing studies and determination of price relationships to be maintained in the event of mobilization for war.

b. Organization of a nuclear administrative and technical staff for price control, capable of orderly and rapid expansion in the event of mobilization.

c. Current and continuous planning for price control, and implementation of those plans at the direction of the President.

d. Final authority on all matters of price determination, including goods and services procured by the Armed Forces.

e. Particular attention to a program to obtain public support for price controls, when and if such controls are implemented.

2. It is further recommended that the Congress authorize the President to direct the implementation of price controls at the time and to the extent that the President may deem advisable.

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