

“Administered Prices,, and Public Policy

1. — Research on what are termed “administered prices”, whether undertaken privately by individual economists or promoted by public authorities, has generally been prompted by pressing practical concern. Considerations of method, the clarification of which may serve as a useful introduction to this analysis, make this research all the more important.

It is generally accepted that the principal subject for study in political economy — as a form of scientific research — is the intervention of the State in the field of economic relations, but that, none the less, there are also other interventions in economic life, due to other organised groups: local or international institutes, trade unions, agricultural and industrial organisations, business corporations and so on. Yet this second field of research has still not been properly explored, although there is no doubt about its importance, if only because of the present dimensions of some of these organised bodies and groups and of the widespread effects of their policy decisions. Hence the interest of the study of phenomena which, like that of “administered prices”, belong to this second field of research, and which lead one, among other things, to tackle the question — also still open — of the relations between the policy of these organised bodies or groups and public policy.

A further ground for interest is the considerable empirical evidence collected and published in connection with the discussions on “administered prices”. Not that this material has yielded consistent conclusions. Indeed, the very evidence submitted by some as decisive has been judged irrelevant by others. Nevertheless it has undoubtedly enriched our knowledge of the interplay of motives underlying the behaviour of economic entities, and there is no need to stress the usefulness of this knowledge in any attempt to move beyond the simple motivation model assumed by economic analysis as an initial approximation, and often maintained unchanged even at levels of research with more realistic aims.

Lastly, this abundance of empirical evidence has prompted the comment that economists were, in the telling words of one writer, faced with "a phenomenon in search of a theory" (1). However, the developments of this research provide a wealth of stimuli for methodological thought, especially on the relations between economic analysis and the problems of practical policy. These relations are constantly in need of fresh examination, because the more deeply you go into the matter, the more you find that the clarification so far given on many aspects is unconvincing. But it will be possible to grasp this point more fully as the present study proceeds.

2. — Up till now the technical expression, or if you prefer, technical jargon, used in this connection has been "administered prices", but no accurate definition of the concept was given. This is the fate of all those expressions that, as they become current, circulate on the basis of their face value, without their conceptual content ever having been clarified.

If we are to proceed more systematically, it is necessary to remember that the first use of the expression in question goes back over twenty-five years, and is mainly connected with the contributions of an American economist — Gardiner Means. We refer, of course, to the moment at which the term appears in a carefully worked out context which is designed to justify its adoption, and not to the occasional use of it by somebody ahead of his time, whom historical research can always manage to discover.

"By an administered price", Means affirmed in a paper in 1934 to the American Statistical Association, "I mean one which is set by administrative action and held constant for a period of time". "In administered prices, therefore", he added, "the price is rigid, at least for a period of time, and sales fluctuate with the demand at the rigid price".

He went on to explain that "administered prices" were "basically different" from "market prices" which result from the interaction between buyers and sellers in a competitive market, and that the distinction postulated would not coincide with the traditional one between competitive prices and "monopoly prices".

(1) JOHN M. BLAIR, "Administered Prices: A Phenomenon in Search of a Theory", *American Economic Review, Papers and Proceedings of the Seventy-first annual meeting*, May 1959, p. 431 et seq.

In principle, the latter prices may vary on the market not less than competitive ones, even if they are determined in a different way and are not necessarily characterised by the considerable rigidity which is said to be typical of "administered prices" (2).

There is no doubt that the terminology is not a very happy one, especially in view of its possible ambiguity as regards the alleged "administrative" character of the prices in which we are dealing. It is however obvious that, in the sense with which we are concerned, the term is not meant to refer to the intervention on the part of external administrative authorities, but to decisions adopted by the management of productive units, and corresponding to a conscious price policy on their part.

It is essential, in any case, to go back to that distant study to have a genuine, explicit definition of "administered prices" or "inflexible" prices, as Means constantly added. In the broad current of subsequent research, the meaning and qualification of the terms are taken for granted, and the possible linguistic snags obviously seemed of minor importance in comparison with the complexity of the question of substance raised in Means' writings.

This paper, according to an authoritative commentator, gave rise to "one of the most vigorous controversies in recent economic literature" (3). And it is easy to realise how many questions — of theory, of empirical verification, and of policy — are connected with the specific consideration of the existence of flexible prices and inflexible or rigid prices in real economic systems (4). The discussion set out to investigate the nature of, and the factors affecting the flexibility or rigidity of price, and to try to reach a statistical measurement of the phenomenon; to analyse the effects of the phenomenon itself upon the level of economic activity (particularly with reference to the relations between flexibility of wages and employment), to ascertain in the same way the long run repercussions of the degree of price flexibility, or the consequences to be expected

(2) Cf. GARDINER C. MEANS, "Price Inflexibility and the Requirement of a Stabilizing Monetary System", *Journal of the American Statistical Association*, June 1935, p. 401.

(3) The expression is JOHN M. BLAIR's, cf. "Economic Concentration and Depression Price Rigidity", *American Economic Review*, May 1955, p. 566.

(4) As Gustavo Del Vecchio has observed, "if one takes into account the existence of rigid prices and non-rigid or flexible prices, one comes up against a more complex system, but more in line with reality". Cf. G. DEL VECCHIO, *La sintesi economica e la teoria del reddito*, Padova, Cedam, 1950, p. 218.

in respect of the efficient use of resources, and hence of the functioning of the economic system. And this, to mention only the basic fields of research, without coming down to any specific points involved in each of these (5).

During the war, attention was diverted to other pressing problems, and the whole controversy was shelved. However, it was bound to arise again sooner or later, as in fact it has recently. But of course, in this new phase, research and discussions on "administered prices" are taking place within an economic context very different from that obtaining in the thirties.

At that time, the concern underlying the discussion flowed from a persistent and marked deflationary situation; whereas at present widespread fears are caused by the creeping inflation which seems to be establishing itself irreversibly in economic systems. And as the general conditions against which discussions take place change, there comes a change in the way "administered prices" are held responsible. In a nutshell, in the years around 1934, these prices were regarded by Means and his followers as being largely responsible for the severity of the depression at that time. Whereas, in more recent years, the charge brought against "administered prices" is that they feed and support a particular type of inflation, which is in fact defined as "administrative inflation". This expression is certainly not very elegant, and is intended to indicate broadly that this form of inflation is essentially determined by the increases in "administered prices". In both cases, the experience that economists have in mind is that of the United States, but the considerations advanced are general in scope, and are of interest mainly for that reason.

It is on this precise attribution of responsibility, as will be readily understood, that the discussion more directly relevant to policy is pivoted. And since it is with problems of policy that we must deal, we shall have to examine these charges, both old and new.

3. — In the research carried out in 1934 and in the years immediately following, Means recalls the re-equilibrating function attributed to price changes in the model of a competitive economic

system. We know that these changes, and the high degree of flexibility of the prices they reflect effect the readjustment necessary for a satisfactory use of resources and for an approximate equilibrium of the economic system itself.

As against this hypothetical process, as Means remarked, empirical investigations indicate a marked limitation in the changes over a substantial number of prices: those very prices, in fact, which he regards as administered, using the definition set out above.

He then seeks to establish in quantitative terms the relevance of the phenomenon to the economy under examination (*i.e.* that of the United States); to explain the factors determining the phenomenon itself; and, lastly, to evaluate its effects and implications in respect of policy.

Means' measurement of this phenomenon is based on the ascertainment of the frequency of price changes for a given number of goods during a specific period. The survey covers about 750 items taken from a well-known monthly index of wholesale prices (that of the Bureau of Labor Statistics) from 1926 to the end of 1933: over the eight years under investigation, the survey shows that the distribution of prices tends to be U-shaped, one extreme comprising prices subject to frequent changes, the other comprising prices that change less frequently, or in some case not at all. Hence the demand prompted by the survey (which obviously excluded the sector of public utilities regulated by tariffs) for the explicit recognition of two different systems of determining prices — that based on the unceasing and reciprocal action of market forces, which is at the root of the "flexible" prices of the traditional economic analysis; and that based, on the contrary, on the policy decisions of managements, which gives rise to prices established administratively and kept constant for appreciable periods of time.

Means, as has been noted, was interested in the degree of frequency of price changes for each single item observed, and not in the amplitude of price changes. However, his survey also indicated that, in the years of acute depression under consideration, the prices subject to the most frequent changes were also those which suffered the greatest decline, while prices with the fewest changes were also those that underwent a more modest reduction. In 1932, for instance, "flexible prices" fluctuated around a level equal to half that of 1929, while the "administered" prices were only 10 per cent below the pre-depression level.

(5) See, also, for further bibliographical references, the full essay of RICHARD RUGGLES, "The Nature of Price Flexibility and the Determinants of Relative Price Changes in the Economy", in the volume *Business Concentration and Price Policy*. A Report of the National Bureau of Economic Research, Princeton, University Press, 1955, p. 441 et seq.

The explanation of the phenomenon outlined by Means also rests on an empirical basis; in particular, it emerges from the link between the rigidity observed in the given prices and the degree of economic concentration in the corresponding productive sector. To the documentation of the trend towards concentration in the modern economy, Means, alone and in collaboration with Adolf Berle, had devoted studies, which are widely known and have also resulted in prolonged arguments (6). He draws, then, on his specialised knowledge in throwing light on the correlation indicated between rigidity of prices and the degree of industrial concentration. To quote his own words: "As we go from the "atomistic" to the concentrated industries, we find more administered prices and the administered prices becoming more rigid. In spite of many exceptions, the more concentrated the industry, in relation to its market, the more inflexible do prices become" (7).

He takes a severe view of the consequences of this state of affairs (as already noted) in connection with the slump at that time. "If all prices had been flexible", Means writes, "it is doubtful if we would have had a serious depression after the stock crash of 1929. Where prices are rigid, however, a general drop in demand has quite different and most disastrous results. Instead of producing lower prices, the drop in demand produces a drop in sales and production. In this manner, rigid prices can expand an initial small fluctuation of industrial activity into a cataclysmic depression...". And in fact the whole depression might properly be described as a general fall in prices in the area in which there is price flexibility, and a decline in productive activity in the area of rigid prices (8).

In concrete terms, the distinction was identified with the one between the agricultural sector "in which practically the whole impact of falling demand worked itself out in falling prices" and the industrial sector, in which the contraction affected above all the level of production and employment. Accordingly, the discussions at

(6) Cf. MEANS' article "The Growth in the Relative Importance of the Large Corporation in American Economic Life", published in the *American Economic Review*, 1931, and recently reprinted in the volume *Enterprise and Secular Change*, Readings in Economic History, collected and edited by F. C. LANE and J. C. RIEMERSMA, London, G. Allen and Unwin, 1953, p. 125 et seq. Also, by A. A. BERLE and G. C. MEANS, the volume *The Modern Corporation and Private Property*, New York, MacMillan, 1933.

(7) G. C. MEANS, "Price Inflexibility etc.", *cit.*, p. 407.

(8) Cf. G. C. MEANS, "Price Inflexibility etc.", *cit.*, p. 411.

the time also reflected, to a great extent, the clash of interest between the two sectors.

The polemical vigour of Means in indicating the consequences of rigid prices in the crisis did not, however, lead him to affirm that the elimination or the containment of their area should be a condition for the reinforcement of stability. He believed that administered prices were an expression of the degree of control over the market which some firms can exercise, even if they are not in a position of actual monopoly, and that they were destined to remain present in modern economies, because they were inherently linked with the tendency towards concentration, and with the forms of industrial organisation prevailing in such economies. The task to be faced was therefore not that of eliminating these prices, but that of putting on an institutional plane the adjustments imposed by their very existence (9).

This attitude neither anticipates, nor does it coincide with, the one assumed by Keynesian economists, where price rigidity is concerned. For their part, as we know, they concluded by attributing to rigid prices a stabilising function in the cycle, thus completely reversing the views prevailing until that time: in their opinion, prices more resistant to deflationary pressures helped to support the aggregate income (10).

Means held the opposite view, namely that the rigidity of prices was a basically disruptive phenomenon (in the absence of institutional correctives), and yet an integral part of the modern economic system, in as much as it was fundamentally connected with the irreversible process of industrial concentration (11). This connec-

(9) What I mean — explained MEANS — is "that inflexible, administered prices are incompatible with automatic economic adjustment. Our economy has developed to the point where we simply cannot rely on the actions of individuals or enterprises acting independently to produce overall co-ordination and an effectively functioning economy. Unless we are willing to forego the benefits of modern technology, we are faced with the real task of figuring out how economic co-ordination can be achieved in the presence of inflexible, administered prices". Cf. G. C. MEANS, "Note on Inflexible Prices", *American Economic Review*, March 1936.

(10) Cf. in particular A. H. HANSEN, *Fiscal Policy and Business Cycles*, New York, W. W. Norton, 1941; and, for a survey of the thought of other authors, J. K. GALBRAITH, "Monopoly and the Concentration of Economic Power", in *A Survey of Contemporary Economics*, Philadelphia, Blakiston Co., 1949, p. 114.

(11) "In their general significance... the rigid prices reflect the long progress of economic concentration and appear to be an internal part of modern industrial organization, resting on modern technology". Hence, the conclusion that we should accept rigid prices

tion forms the focal point of his research and, at the same time, the most direct link between the earlier phase of research, which we have been considering so far, and the phase of the recent revival against a background of different economic conditions.

That the link between concentration of production and price rigidity constituted the most significant aspect of the contribution of this economist became evident in the course of the debates which followed it, and which consisted, almost exclusively, of differences of opinion as to the soundness of the statistical evidence presented by Means. This evidence was therefore subjected to a subtle, and one might almost say captious scrutiny, in a whole series of refutations and replies which dealt with the data used, the working methods, and the results.

To give one example, it was objected that the enquiry was based on quoted prices, or list prices, and not on actual prices, which might differ to a considerable extent from the former, as a result of discounts, various rebates, the absorption of transport expenses and other reductions, which cannot be assessed accurately, but were probably practised on a scale by no means negligible during periods of depression. The result of this approach was artificially to accentuate the tendency to rigidity, even discounting the fact that one point had been overlooked: for some items there might have been changes in quality even though the price remained static (12).

It was also emphasised that an elaboration taking monthly price indexes as its starting point was destined to obscure *per se* the changes that occurred at a different interval, whether weekly or daily, and that was another reason to increase the doubts as to the scope of the conclusions reached (13).

Lastly, it was contested that the results brought out by a limited inquiry could be extended to the whole price system, and above all

"as inherent in our modern economy and build our economic institutions around them in such a manner that inflexible administered prices cease to be a disrupting factor". Cf. G. C. MEANS, "Price Inflexibility etc.", *cit.*, p. 408.

(12) Cf., in particular, W. L. THORP and W. F. CROWDER, *The Structure of Industry*, Temporary National Economic Committee, 1941. Objections as to the adequacy of the data have been repeatedly raised, among others, more recently, by M. J. BAILEY in "Administered Prices in the American Economy", included in a collection of writings published by the Joint Economic Committee of the United States Congress with the title: *The Relationship of Prices to Economic Stability and Growth*, Washington, 1958.

(13) On this point, see T. SCROVSKY, "Prices under Monopoly and Competition", *Journal of Political Economy*, 1941, p. 633 et seq.

be interpreted as incontrovertible evidence of the progressive extension of the area subject to the phenomenon of rigidity (14).

This enumeration, admittedly summary, although it may not do justice to the acuteness of the analyses carried out in support, or in criticism, of the various theses, does at least make it possible to understand how the discussion, as it became wider and more complicated, began to touch on a considerable number of problems. Nevertheless, it was precisely the possible correlation suggested between economic concentration and price rigidity which gave a focus to the discussion, if only for the necessary precision it furnished to the loose definition of "administered prices" given by Means. By showing as their distinctive feature the fact that they were "set by administrative action and held constant for a period of time", as we know, he included in effect so vast a category that it could cover almost the whole of the prices charged in the retail sector; but this is not what worries people when they discuss the "administrative control of prices" in the sense of ability to choose between various possible prices on the part of the sellers, as opposed to the mere acceptance by them of the prices "made" by the market. The type of "administrative" price-fixing which really merits attention is the one that stems from the processes of concentration and from the dominating position which it ensures to a restricted number of firms in individual markets.

Considerations of this kind were advanced as early as 1936, when Galbraith had occasion to observe that it was not correct to present price rigidity as being due solely to a practice followed by the management in fixing prices; the rigidity should on the contrary be considered as "the joint product of the monopoly power and the nature of administration" (15). Similar considerations are repeated by the economist who was the first to reopen the controversy after the war, Blair, since he too points out that the "administered prices" with which we must mainly deal are those occurring in the industries of an oligopolistic character, in which the adjustment to a decline in demand usually takes the form of a reduction in the level of

(14) For a general discussion on the question and for further bibliographical indications, see E. S. MASON, "Price Inflexibility", *The Review of Economic Statistics*, May 1938, p. 53.

(15) Cf. J. K. GALBRAITH, "Monopoly Power and Price Rigidities", *Quarterly Journal of Economics*, May 1936, p. 462 et seq.

production, rather than of prices (16). This confirms that the relation between the process of concentration and the rigidity of prices also constitutes the unifying link in time of the controversy.

The most recent phase thereof, not less than the earlier phase, presents a number of approaches. In order to make possible a more systematic exposition, it will therefore be better to try to work back from the intricacy of polemics to the main ideas behind them.

4. — A first approach, taking up Means' objectives and his techniques of analysis, set out to give more convincing empirical evidences of the connection between economic concentration and price rigidity. If we compare the behaviour of the prices of products belonging respectively to the so-called "atomistic" area of production to that in which concentration predominates, one of the drawbacks is that the comparison itself reflects not only the diversity in the degree of concentration, but also the possible influence of other factors, such as the elasticity of demand, the structure of costs, the availability of data, and so on. Accordingly, if, as between the two areas, an increase in the rigidity of prices is observed, this cannot be attributed with certainty to the fact of concentration, because it might depend on, or at any rate be conditioned by, the other factors mentioned.

In order to overcome this difficulty, Blair therefore thought of comparing the behaviour of the prices of the same products (in the "atomistic" area and in that of concentrated industries) in two different phases of depression at such a distance in time as to include a period in which there was an undoubted and admitted strengthening of the process of concentration. That being so, the influence of other possible variables might be assumed to be unchanged, and the differences observed in the behaviour of prices be attributed with greater reason to the development of economic concentration.

Following this line of argument, Blair compared the behaviour of prices during the 1929-1933 depression and during the one experienced in the United States between 1890 and 1897, that is, immediately before the substantial movement of concentration that

(16) JOHN M. BLAIR set off "the timely revival of an old controversy", by his inquiry: "Economic Concentration and Depression Price Rigidity", *American Economic Review*, May 1955, p. 566 et seq. By the same writer, see also the article cited in note (1).

took place at the turn of the century. Now, the essential results of the research, which was obviously complex and laborious in its technical details, seem to bear out Means' thesis. In both depressions, prices are shown to be flexible in these sectors which present or retain, in both periods, a sufficiently atomistic structure (as, for example, in the case of agricultural, food, textile and timber products). Where, on the contrary, the rigidity of prices increased, it is generally correlated with the process of increased concentration, as appears — and very markedly — in the case of iron and steel products (17).

On the data used in this analysis, as on the possibility of attributing general validity to its results, reservations have been made similar to those noted above (page 8), and it is not therefore necessary to dwell further on them. It is necessary, on the other hand, to point out that Blair succeeded, as was his intention (18), in drawing the attention of economists to the contrast between the flexibility and rigidity of prices. It was not, however, as he believed, only the re-emergence of new periods of depression in the post-war years which made it necessary to reconsider the problem. It was rather the persistence — already observed in 1953-1954 and more strongly in 1957-1958 — of the tendency for prices to rise even in periods of stagnation and of declines in production. This phenomenon, which has conferred on the most recent waves of economic decline the well-known character of "inflationary depressions" has led people to wonder, among other things, whether and to what extent this was determined by the price policy followed by some firms, that is, by the practice of "administered prices".

In the studies devoted to this question in recent times, particular importance has therefore attached to the analysis of the role of administered prices as an inflationary factor: and a second approach to research can then be singled out — the one that adopts this particular angle.

Lastly, a third line of research has set out to establish a better balance between the mainly empirical character of the studies of

(17) Cf. J. M. BLAIR, "Economic Concentration and Depression Price Rigidity", *cit.* In the area of flexible prices, the decline is higher, in general, in the 1929-33 period, as was to be expected given the unusual severity of the depression at that time (cf. p. 573).

(18) *Ibidem*, p. 582.

the phenomenon in question and the need to make a more thorough examination of its theoretical rationale (19). Of course, the different objectives of the investigation are often found together even in one analysis (20); but, for convenience of exposition, it is preferable to adhere to the distinction outlined above.

5. — Gardiner Means has once again intervened in the discussion with an affirmation that "administered prices" are, in present conditions, decisive factors making for inflation. In accordance with his usual methodology, he has been at pains to make the facts speak for themselves. In his new contribution, he has analysed the movement of wholesale prices from 1942 to 1958 for numerous products, grouped according to his favourite criterion of distinguishing between sufficiently competitive sectors of production, where there is flexibility of prices, and the highly concentrated sectors of production, where there is a margin for the "administrative" fixing of prices and wages. Now the increase in prices which followed the jettisoning of war-time controls was patent mainly in the price sector most sensitive to market influences, as was to be expected in view of the typically monetary character of the inflationary process at that time. Whereas from 1953 on, and in particular in the two years 1957-1958, the increases were registered mainly in the oligopolistic sector of industry, and took place even

(19) In connection with Blair's survey, it has, for example, been observed that "there would perhaps be less resistance, on the part of many economists, to the acceptance of the idea that concentration leads to price rigidity if they were given a good theory to explain why this should be so. It is true that [...] some degree of market control is necessary for price rigidity. But what has not been shown is why those possessing market control should find price rigidity desirable".

As possible schematic explanations of price rigidity "in a phase of depression", the following suggestions have been made: the reluctance of management to reduce quoted prices (not necessarily those actually charged) in order to avoid possible unfavorable effects on public opinion when there is a rise later, once the crisis has really been overcome; the desire to reduce to the minimum cyclical fluctuations in demand; the fear of leading potential buyers to expect further reductions in prices, with the consequent postponement of purchases, especially for durable goods (cf. *American Economic Review*, May 1955, pp. 600-601).

(20) *A fortiori*, the observation is valid for the volumes of essays, like the most valuable ones, published on the occasion of the two parliamentary inquiries carried out in the United States on the question which we are examining, with substantial participation of the most outstanding economists of the country. Cf. *The Relationship of Prices to Economic Stability and Growth*, already cited, and the subsequent series of *Hearings on "Administered Prices"*, Washington, 1959 — in particular, parts 9 and 10 ("Administered Price Inflation: Alternative Public Policies").

under conditions of stagnation and recession, thus confirming, in Means' opinion, the different origin of the most recent inflationary pressure: the origin, he felt, was to be sought precisely in the fairly wide margin of decision of the big firms in fixing their prices, and also in the power of the large trade unions to determine wages (21). The explicit inclusion of wages fixed through trade union action in the category of "administered prices" is in fact the most important difference between Means' recent survey and the 1934 one (22). Another difference which should be pointed out is that while, in a period of depression, the accent was on the lack of flexibility downwards of certain prices, today the stress is on their flexibility upwards — determined by decisions of the management, and not by market conditions (23). This shift of emphasis has also been the subject of some pungent criticism which, by the way, does not seem justified (24). At bottom, the phenomenon to which it is intended to refer is that of a certain strategy in the oligopolistic fixing of prices. Now, clearly a strategy is not a

(21) The documentation supplied by Means is included *in toto* in part 9 of the *Hearings on "Administered Prices"*, *cit.*, pp. 4746-56.

(22) It is interesting to unearth the following statement by Means in his article on "Price Inflexibility", *cit.*: "It should be noted that, in the United States, labor organization has been only a very secondary influence in producing rigid prices. In such concentrated industries as steel and automobiles, union organization has been negligible in strength, yet prices have been inflexible".

His present position takes into due consideration the changes that have since taken place in the "facts", and agrees that "in theory an administrative inflation could arise either from labor seeking to push up wage rates faster than productivity, or from management seeking to increase profit margins, or from a combination of these two". (*Hearings, cit.*, p. 4762). In point of fact, in the particular historical situation under examination, he denies that the inflationary pressure was caused by excessive wage demands. (*Hearings, cit.*, p. 4769). The same conclusion is reached by G. ACKLEY in a balanced analysis of "Administered Prices and the Inflationary Process", *American Economic Review*, May 1959. On this issue contrasts of opinion assume a highly emotional character and often lead to an attempt to spread the blame. In any case, as Ackley observes, "If prices as well as wages are set by an essentially political process, economists should have guilty consciences about casually concluding that only labor's excessive wage claims can be responsible for creeping inflation, when these claims can be judged excessive only because they are inconsistent, at stable prices, with the also politically determined mark up claims of business" (p. 430).

(23) A resounding example, destined in all probability to remain of crucial importance, was furnished by the United States steel industry when, in the second part of 1958, it decided to increase its prices, though operating only at 60 per cent of capacity.

(24) Cf. G. HABERLER, "Internal Factors Causing and Propagating Inflation", roncoed paper at the "Round Table on Inflation" of the International Economic Association, Elsinore, 1959.

one-way affair, but is adapted to circumstances, now adopting rigidity, now pushing prices up, as the circumstances require.

As against this, the remarks made in general as upon Means' approach are still valid, in the sense that the factual documentation collected, with laudable industry, is not conclusive, as he seems to think, since it lends itself to divergent interpretations. It is admitted that the price increases in the most recent period are met with in the highly concentrated sector of industry, but is it not possible that this phenomenon turns on the fact that it was precisely this sector which experienced a buoyant rise in investments, and could it not be a case of a delayed adjustment of prices in a sector which, at the time, was more closely subjected to war time controls?

This is in effect to affirm the need to give a theoretical basis to the relation outlined between "administered prices" and the inflationary process: and there has been no lack of economists who have set out to provide one.

The oligopolistic rationale in fixing prices is indicated, for example, in a behaviour which usually does not propose to achieve the full maximization of profits (of course, at the level that would be permitted in such cases, by the dominating position of a restricted number of big firms in the market). The oligopolistic sector thus disposes, in the view of the economist who has outlined this interpretative model, Galbraith, of "a quantum of what may be called unliquidated monopoly gains" (25), and realizable, in consequence, at the discretion of the firms themselves through the increase in prices, up to the level corresponding to the effective maximization of their profits.

Now, in deciding these possible increases in circumstances of particular importance — in connection, let us suppose, with contested increases in wages or with official rises in the rates of interest — the oligopolistic firms would succeed in maintaining, and even in increasing, their profits, quite apart from attributing the resultant rise in prices to the conduct of other operative factors (organized labour or the monetary authorities) instead of to their own actions.

(25) Cf. J. K. GALBRAITH, "Market Structure and Stabilization Policy", in *The Review of Economics and Statistics*, May 1957, p. 124 et seq. Among the criticisms advanced against Galbraith's theoretical model, see in particular that of W. J. BAUMOL, "Price Behavior, Stability and Growth", in the volume *The Relationship of Prices to Economic Stability and Growth*, cit., p. 49.

The logic of this model leads us to assign decisive weight to the oligopolistic sector in the development of the latest inflationary tendencies, and also to deny the efficacy of counterinflationary action of a monetary or fiscal character, which in any case would place the burden of the readjustment only on the competitive sector (26).

Another shrewd economist, Baumol, agrees that the criterion followed by oligopolistic firms in fixing prices is not that of profit maximization. In fact, in his view, the prevailing objective that such firms generally have in mind is "to maximize not profits, but sales volume".

Therefore, provided the profits keep at a level considered "satisfactory", the management concentrates on increasing sales, not profits; and if there is an unrealised profit margin, it is deliberate, it is not a manoeuvre on the part of the management, because it represents the alternative the management is prepared to sacrifice in order to achieve the target regarded as more important. It would follow that any measures to reduce total demand and to increase interest rates — since they affect the volume of sales — would not fail to strike the oligopolistic sector as well, and reduce its contribution to inflation.

The logic of this interpretative model leads one to attribute less weight to the oligopolistic sector in relation to the inflationary process examined (to which the competitive sector is not extraneous either) and to reaffirm the efficiency of restrictive monetary or fiscal measures (27).

Other economists, from the specific examination of the relations between "administered prices" and inflation, have moved on to more general considerations about the actual process of the determination of prices in the big corporations, bringing out in particular the institutional transformations that have occurred in the sense that, once a certain magnitude is reached, we end up by attributing either directly or implicitly to the firms themselves a status more or less

(26) "... monetary and fiscal policy do not make contact with present forms of inflation, at least in a useful or practical way". Thus, J. K. GALBRAITH in the *Hearings*, cit., p. 4928.

(27) Baumol warns us that he is not "to be interpreted to hold the position that different monetary and fiscal policies *all and always* fall with exactly equal weight on the competitive and oligopolistic sectors of the economy". Cf. *The Relationship of Prices to Economic Stability and Growth*, cit., p. 56.

similar to that of public utilities (28). The not infrequent official reminders or appeals to the sense of responsibility of the big firms, for instance, "to recognize the considerable public implications of the prices fixed for their goods and services" have themselves been adopted as a confirmation of that "public utility conditioning" which now surrounds large companies. In fact, the affirmation (advanced by Lanzillotti) that the large-scale units of production "tend to behave more and more like public utilities" (29) has given rise to a dispute in the *American Economic Review* in 1959 in as much as the affirmation itself seemed at one point too summary and likely to generate the conviction that the firms dominating the market do not seek to derive the greatest possible advantage, but rather observe a public-spirited line of conduct (30).

Lanzillotti has not been slow in clarifying the limits of his analogy; his intention was only to stress that, in both types of case, price policy appears to depend on the predetermination of an average rate of return on investments, while for the rest no judgement was given on the "fairness" of the rate itself (31).

Moreover, even in the same article containing the affirmation under discussion, Lanzillotti has not failed to observe that the possibility open to the management of big corporations to choose between various lines of action was "a fairly clear manifestation of economic or market power", and raised serious questions of public policy. "What is the net impact of these policies", he wondered,

(28) The expression reproduces that of R. F. LANZILLOTTI ("quasi-public utility status") in a study of his own: "Some Characteristics and Economic Effects of Pricing Objectives in Large Corporations", published in the volume referred to: *The Relationship of Prices to Economic Stability and Growth*, p. 441 et seq.

(29) Cf. R. F. LANZILLOTTI, "Pricing Objectives in Large Companies", *American Economic Review*, December 1958, p. 940. This essay is presented by the writer as an interpretative synthesis of an investigation promoted by the Brookings Institute, the results of which have been more extensively illustrated in the volume "Pricing in Big Business", by A. D. H. KAPLAN, J. B. DIRLAN and R. F. LANZILLOTTI, Washington, 1958.

(30) Cf. *American Economic Review*, September 1959. The critical observations of ALFRED E. KAHN were particularly vigorous, both in bringing out the ambiguity made possible by Lanzillotti's expression and in reaffirming "the economist's traditional concern with market power and his corresponding assumption that, to the extent such power exists, it will be exercised in the interest of those who possess it" (p. 678).

(31) See Lanzillotti's reply in the same number of the *American Economic Review*, p. 679 et seq. The other essays by the same writer already cited illustrate profusely the behaviour that he considers typical of the big companies in price fixing: the search, that is, for "a pre-determined profit target rate of return on investment [...], frequently balanced with market share considerations".

"on economic growth and stability? More specifically, do target-return pricing, profits planning, and the attendant price behavior tend to promote or inhibit stability and growth"? The importance of these questions is obviously not diminished by the fact that they are only advanced in this connection, since the writer observes that an adequate reply would have called for more extensive research on the policy objectives of the big firms and detailed studies on the programming of prices, profits and investments on the part of individual companies in the various phases of the cycle (32).

In this way, as usually happens when we are dealing with a question coming within the area of imperfect competition and oligopoly, a large number of important questions remains open. Nevertheless, if we sum up the lessons of the research carried out so far, and consider its implications as regards policy, the range of alternatives resulting from it may be stated in the following terms.

One policy that might be adopted towards the phenomenon of administered prices is abstention from any public intervention. And this must be recorded not so much for the sake of completeness or because it has been explicitly put forward by some writers (33) as because of the current realization that even "laissez faire" constitutes a form of policy. More particularly, an attitude of abstention cannot be regarded as "neutral" towards the various interests at stake.

Another possible policy likewise excludes the need for new forms of public intervention to deal with the practice of "administered prices", but only to the extent that it considers valid, or at any rate effective, the controls provided by existing anti-monopolistic legislation. An attitude of this kind has found various supporters in the United States of America (34); and we have deliberately recalled the experience of this country, because it shows that vastness of market and deeply rooted tradition of legislative measures to curb the concentration of economic power do not *per se* eliminate the emergence of tendencies such as those examined here in connection with the concrete process of price determination. And, it is obviously useful to keep in mind this experience in the institutional

(32) Cf. the article cited: "Pricing Objectives in Large Companies", p. 940.

(33) "It is my opinion that the subject of administered prices in the free or unregulated part of the economy is not of itself a proper concern of public policy, nor a subject worthy of the attention of the Congress". See M. J. BAILEY in the article: "Administered Prices in the American Economy", *cit.*

(34) Cf. Parts 9 and 10 of the *Hearings on "Administered Prices"*, *cit.*

developments connected with European economic integration, which is now laboriously under way and which affects us much more closely (35).

A different attitude is adopted by those who consider that the controls provided by anti-monopolistic legislation, and also by the monetary and fiscal measures referred to above, though applicable because of the contribution that may rightly be expected of them, are not instruments sufficient to check the tendency towards « administered prices ». The need for further and specific measures of public intervention, which is recognized in such cases, leads to suggest different courses of action.

The mildest would be that combination of appeals, warnings, and pressure from above which are the concrete forms of intervention exercised through so called « moral suasion ». The most drastic line would call for the prior notification to previously established public organs of any intentions to increase prices, and an institutionalized debate on the justification and on the extent of these increases, specially in the case of some sectors that have a guiding function in the almost periodical rises of prices and in their subsequent spread.

The atmosphere of public interest conditioning the decisions of the big firms concerning prices, which even now materializes — as we observed above — when recourse is had to official invitations, warnings or appeals to moderate such increases, is decidedly accentuated when the application of the projected increases is systematically subordinated to the debate that has been called for, in Parliament or in other appropriate forums. But this is precisely the result envisaged by the supporters of a procedure of this kind.

It is not a question of interfering in the functioning of the market, writes Galbraith, but of bringing the public interest to bear on what is now private price fixing (36). And Lerner, in his turn, makes an explicit reference to the way of regulating prices adopted

(35) This is particularly so if the thesis ably sustained by Scitovsky is shared, according to which the advantages of European economic integration may be expected from its effects on the intensity and the nature of competition rather than from a greater impulse to productive specialization between European countries. Cf. T. Scitovsky, *Economic Theory and Western European Integration*, London, G. Allen and Unwin, 1958; in particular, p. 68.

(36) Cf. *Hearings on "Administered Prices"*, *cit.*, p. 4932. In the same publication, there is also a reference to the thinking of the writer cited on the concrete procedure to be followed in carrying out the projected public debates in connection with the problems of the United States.

in regard to public concerns. In the same way, he affirms, as public utility prices can be and are being regulated so as to prevent monopolistic exploitation of consumers that would take place if the level of prices were excessive, so « administered » prices and wages can, and should, be regulated in order to prevent both inflationary pressure due to the policies of the sellers, and the depression that may follow as a result (37).

In concrete terms, the public authorities of various countries have frequently had recourse of late to appeals and warnings calling for a conscious and joint effort on the part of the various economic sectors in order to avoid or contain rises in prices likely to have inflationary repercussions (38). This persuasive action has in general proved sterile, but is not however without significance, in as much as it implies the recognition of the importance of that « area of discretion » of which the big firms dispose in fixing prices (39) — an importance which some persist in contesting and underestimating (40).

(37) Cf. *The Relationship of Prices to Economic Stability and Growth*, *cit.*, p. 267.

(38) Documentation on this point is provided, not only by numerous official American publications on the state of the country's economy, but by the appeal for price stability addressed to the productive categories by the British Chancellor of the Exchequer in December 1958, and by the request for a study on the price and wages situation submitted by the German Chancellor of the Federal Republic of Germany to the Central Bank with a view to informing public opinion. That study, made public in January 1960, indicates, among other lines of action useful for keeping down prices, a more liberal import policy, increased rationalization of the distributive system, and greater influence over the big companies' practice of fixing prices.

(39) This phenomenon is at times set against the policy of price support in the agricultural sector, and this latter tendency is denounced as a factor making for rigidity or the constant rise in prices. This, however, is another story, and any distortions or tensions provoked by this policy are no reason for losing interest in those originating in the practice of « administrative prices » or for regarding them as legitimate.

(40) G. Haberler, in this respect, takes an extreme position in the above quoted article (cf. footnote 24) when he contests « the basic assumption of the widespread existence of monopoly power in numerous industries designated as concentrated » and when he criticizes even the use of some economic terms, even if widely used, such as « oligopolistic », given to certain industries (p. 28). According to his thesis, in the sectors « competition is not atomistic, but it is nonetheless very real »; this thesis is reinforced by a reference to the well-known Schumpeterian long period reasoning and to its echo which is to be found in Galbraith's book on the American capitalism.

Now, it seems that it is really going to far if, on the basis of well grounded reasoning aimed at illustrating the irreversible aspects of productive concentration resulting from technological progress and the very advantages that derive from it in the raising of the standard of living, the point is reached of denying the possibilities of dominating the market, which in any case is the outcome. After all, consumers live in a succession of short periods, and

Moreover, the most penetrating policy considered — the last one — has not hitherto developed beyond a possible model of action, but it is just as significant as the rest, since it bears witness to the autonomous position of the economist concerned with the problem of policy with exclusively scientific aims and to the fact that it is frequently ahead of its times in its vision with regard to the decisions adopted in practice. In a field of research inevitably subject to sectional influences, it is this spirit of inquiry that in the end is bound to be decisive if constructive ideas are to prevail over vested interests and if there is to be an effective control by society of economic forces.

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to them the pressure of monopolistic power, exercised by those who have the opportunity to use it, appears, from direct experience "very real". On these problems, see P. SYLOS LABINI, *Oligopolio e progresso tecnico*, Milano, 1957.