"Why the Freeze Is a Mistake"

by Milton Friedman

Newsweek, 30 August 1971, p. 22

I applaud President Nixon's proposed reductions in both taxes and Federal spending. I applaud also his action in ending the fiction that the dollar is convertible into gold. But I regret exceedingly that he decided to impose a 90-day freeze on prices and wages. That is one of those "very plausible schemes," to quote what Edmund Burke said in a different connection, "with very pleasing commencements, [that] have often shameful and lamentable conclusions."

Freezing individual prices and wages in order to half inflation is like freezing the rudder of a boat and making it impossible to steer, in order to correct a tendency for the boat to drift 1 degree off course. The "price level" has been rising at something like 4 per cent per year, or one-third of 1 per cent per month, or 1 per cent in 90 days. Surely, you will say, preventing so minor a rise can do no harm. Why the outcry? Because the 1 per cent is the average of changes in literally millions of individual prices, some rising 10 or 20 per cent or more, others falling 10 or 20 per cent or more. These price changes reflect changes in conditions of demand and supply affecting particular goods and services. They are the way that we steer the economy. Preventing them leaves the economy rudderless, yet it does nothing to alter the basic force producing the average 1 per cent rise in prices. That basic force is a more rapid rise in money demand for goods and services than in the physical supply.

Of course, individual price and wage changes will not be prevented. In the main, price changes will simply be concealed by taking the form of changes in discounts, service and quality, and wage changes, in overtime, perquisites and so on. Even 60,000 bureaucrats backed by 300,000 volunteers plus widespread patriotism were unable during World War II to cope with the ingenuity of millions of people in finding ways to get around price and wage controls that conflicted with their individual sense of justice. The present, jerry-built freeze will be even less successful.

But to whatever extent the freeze is enforced, it will do harm by distorting relative prices.

The freeze has reminded me forcefully of a personal experience during World War II, when I was working for the U.S. Treasury Department. In the course of a presentation to the House Ways and Means Committee on the need for additional taxes to prevent inflation, I was interrupted by one member who exclaimed, "Why do we need to worry about inflation in considering taxes? We have just passed General Max [the measure that put a ceiling on all wages and prices]. It is now up to Leon Henderson [director of the Office of Price Administration] to control inflation." I had barely embarked on a learned discourse about how General Max would not work unless it was reinforced by measures to reduce purchasing power, when he interrupted me again. "I understand that," he said. "Mr. Henderson may fail, but we have discharged our responsibility by giving him the power. Now it's up to him."

Similarly today, every proponent of more government spending who had been restrained by fear that the spending would be inflationary will breathe a sigh of relief and say, "Full speed ahead.

The price freeze will hold back inflation." The proponents of tax cuts, and even the Federal Reserve Board, which deserves most of the blame for producing the inflation, will react similarly. The result is likely to be more inflationary pressure, not less.

Whatever happens to the *actual* cost of products to customers or of labor to employers, *stated* prices and *stated* wages will be largely frozen. These are the prices and wages that enter into officially computed index numbers. These numbers will therefore show a dramatic improvement—and depart increasingly from reality. If the freeze were simply ended after 90 days, the indexes would spurt, even though the prices actually charged and the wages actually paid did not. This will create a dilemma for Mr. Nixon. He has a tiger by the tail. Reluctant as he was to grasp it, he will find it hard to let go. The outcome, I fear, will be a further move toward the kind of detailed control of prices and wages that Mr. Nixon has resisted so courageously for so long.

How will it end? Sooner or later, and the sooner the better, it will end as all previous attempts to freeze prices and wages have ended, from the time of the Roman emperor Diocletian to the present, in utter failure and the emergence into the open of the suppressed inflation. Fortunately, as Adam Smith once put it, "There is much ruin in a nation."

Reprinted in: (1) Milton Friedman, *An Economist's Protest: Columns on Political Economy*, pp. 15-16. Glen Ridge, New Jersey: Thomas Horton & Daughters, 1972. (2) Milton Friedman, *There's No Such Thing as a Free Lunch*, pp. 125-127. LaSalle, Illinois: Open Court Publishing Company, 1975.

Compiled by Robert Leeson and Charles Palm as part of their "Collected Works of Milton Friedman" project.

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10/25/12