

Article

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Collective Bargaining Results

Douglas A. Smith

The author of the following article discusses the relationship between inflation and collective bargaining. Collective bargaining cannot in a vacuum create inflationary wage increases. Rather, it is the interaction of mark-up or target-return pricing and profit-based wage demands that sets off the spiral of discretionary increases in wages and prices. In the author's opinion, it would be necessary to strive for intelligent methods of reducing the conflict between good industrial relations and a stable price level or face the consequences of the actions of those who seek to impose unworkable controls on the collective bargaining system.

This paper is primarily concerned with Part III of the Task Force Report¹ entitled « Collective Bargaining and Other Public Policies ». Having been responsible for some of the background material for Part III, I have been asked to give my evaluation of that section of the Report.

My general view on the question of inflation is that during the past several years, it has constituted the single most pressing problem of economic policy. Therefore I regarded as very important the goal of

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* I am particularly indebted to Professors Crispo and Montague for their advice and encouragement. They must, of course, be absolved from all heresy that remains.

1. Task Force on Labour Relations *Canadian Industrial Relations*, Ottawa, Queen's Printer, 1968, 250 pages.

the Task Force in Part III of determining the effect of collective bargaining on inflation. The problem of arriving at policy proposals in this area was made more difficult because of the degree of professional disagreement in the literature over the definition and significance of cost-push inflation. Although the Report ultimately gave the subject an almost balanced treatment, I feel that the degree of professional disagreement was overstated and a stronger weight was given to the extreme demand-pull position than was justified by published works. Reference to the Report will show that statements referring to *any* impact of collective bargaining on the price level are presented in language that is almost apologetic. I do not believe that any apology is needed for a position that collective bargaining and other institutional forces can have undesirable price level effects.

The three explanations of inflation that are reasoned with sufficient generality to be termed theories are demand-pull, cost-push and structural or demand-shift inflation. The first should be almost irrelevant for this particular discussion because it is a truism that if inflation is entirely demand-pull, collective bargaining can have no independent effect. During periods of strong excess demand, prices and wages would be pulled up in the absence of both large corporations and strong unions. The problem that has recently beset most industrial countries is, however, different. It involves price level increases of a persistent nature during periods of moderate or even deficient demand. An explanation for this phenomenon that involves the discretionary power of labour and management to produce results in the labour and product markets that depart from the competitive model is termed cost-push inflation.

To begin with, I will acknowledge the dangers of trying to identify the causes of a particular inflation through the use of tests that deal with broad macroeconomic aggregates alone. As Samuelson and Solow² point out, statements attributing inflation to cost-push factors simply because aggregate wage changes exceed aggregate productivity gains are obviously false. Such reasoning says nothing about *why* wages rose. Therefore, such pieces of information are virtually useless to all but editorial writers. To effectively differentiate cost-push from demand-pull factors, we require relatively objective and quantifiable measures of cost and demand which would then be related to actual changes in wages and prices. If prices and wages were

2. P. A. SAMUELSON and R. M. SOLOW « Analytical Aspects of Anti-Inflationary Policy » in *American Economic Review*, May 1960.

more related to cost than demand factors we would call the inflation cost-push or vice-versa for demand-pull. The problem to date has been the lack of appropriate measures of cost and demand.

In the report of the Task Force, the only attempt at such a measure can be seen in Table 13 which shows base rate changes compared with the unemployment rate for the years 1953 to 1967. Combinations such as a 4.6% increase in base rates with an unemployment rate of 7% or 8.6% in base rates with unemployment of 4.1% do not appear, in my view, to be consistent with a view of inflation that stresses *solely* demand elements. This does not mean that I attribute all inflation to cost factors. In fact, the opposite is closer to being true. However, I believe that at various times collective bargaining and corporate pricing practices can exert an independent upward push that can be harmful to the pursuit of price stability.

In stating that collective bargaining should not be entirely absolved from responsibility for price level variations, I feel that it is quite important to emphasize that collective bargaining alone is not to blame and that executives and editorial writers who equate cost-push with wage-push and blame it all on trade unions do so because of a failure or a lack of desire to understand the subject. Collective bargaining cannot in a vacuum create inflationary wage increases. It must be reinforced by the ability of the corporation with which the union negotiates to pass on the wage increase in the form of a price increase. This must therefore be a sign of the power of the corporation to exercise discretion in the product market. Otto Eckstein in his article « A Theory of the Wage-Price Process in Modern Industry »³ also makes this same point that it is not collective bargaining *per se* that is the problem but rather it is the interaction of mark-up or target-return pricing and profit-based wage demands that sets off the spiral of discretionary increases in wages and prices. Only if management has some degree of discretion in allowing wage increases can collective bargaining gain wage increases that exceed those that would be determined by economic conditions.

The fault that I find with the analysis of Part III of the Task Force Report is that it was sufficiently vague and compromising as to allow easy misinterpretation. I believe that the blame for this lies with the Task Force because there was a tendency to treat the subject almost as a political rather than an economic issue. I feel that the literature on the subject (although admittedly largely American) and the performance of wages and

3. O. ECKSTEIN « A Theory of the Wage-Price Process in Modern Industry » in *Review of Economic Studies*, XXXI, n° 4, 1964.

prices in relation to demand conditions justifies less conditional statements on the subject. It is my considered opinion that very few economists would take the position that collective bargaining can have no influence on the price level. My view of the position of some of the strictly demand advocates of the Task Force was that they felt that Milton Friedman represented the majority opinion of economists. Although a great economist, I believe that Friedman represents a polar extreme on this subject and his views should not be imputed to the majority.

This brings us to the next problem in a discussion of inflation, that being the policy alternatives flowing out of our analysis of the causes of inflation. My reading of the Task Force Report is that institutional pressures can have an impact on the price level at times and with many conditions attached. In spite of the conditional tones, this is the inescapable conclusion because of the policy recommendations of the Task Force. They state that monetary and fiscal policies alone do not constitute a reasonable solution. Therefore they cannot believe in pure demand inflation. A view that the tools of monetary and fiscal policies alone are not adequate is not to say that monetary and fiscal policies are powerless against inflation — to the contrary, I have every confidence that monetary and fiscal policies could stop anything short of a Brazilian hyper-inflation. But it is with the employment effects of such policies that I would be concerned.

I fear the effects of unemployment more than those of inflation and it is for this reason that I feel constructive steps must be taken to keep prices reasonably stable. Without such action, it is only a matter of time until continued deflationary steps finally check inflation by generating a sufficiently large recession. For this reason, I am opposed to the use of monetary and fiscal policies alone and agree with the Task Force when they urge the creation of an Incomes and Costs Research Board (subsequently re-titled by the government).

The next thorny question to be faced has to do with the actions that should be taken by the Prices and Incomes Commission. I agree entirely with the position of the Task Force that the Commission should be granted the maximum possible degree of independence and that it should be empowered to subpoena whatever information it requires in its research work. Other than this, the Task Force is not explicit in what the Commission should do but it is explicit in what it should not do. Specifically, it should not be a purveyor of the dread wage-price guideposts. I am not entirely certain that I agree with this for reasons that I will enumerate.

Wage-price guideposts as a technique of economic policy have come in for much criticism particularly following their collapse in the United States. However the guideposts have also had their defenders, notably Ross, Solow and Eckstein and the most recent and comprehensive survey of the subject ⁴ predicts their return. Evidence on the effectiveness of the guideposts is sparse but the limited evidence that does exist suggests that the guideposts did have some beneficial effect during the years that they were employed. The evidence of which I speak is an article by Perry ⁵ which tests the impact of the guideposts through an equation that predicted the wage increases that would have occurred without the guideposts and then compares these estimates with the actual figures. Perry's work was for the period 1962 (q.1) to 1966 (q.1) and for further confirmation, I have extended his analysis using later data so that we have a continuous series from 1962 (q.1) to 1968 (q.3). The obvious rationale for extending the residuals (actual — estimated) to 1968 is to determine if the pattern of the residuals continues negative after the termination of the guideposts thereby casting doubt on the results. Table 1 and Chart 1 show the regression residuals which are consistently negative during the guideposts era. These data are based on Perry's ⁶ wage equation which is as follows.

$$W_t = -4.313 + 0.367C_{t-1} + 14.711U_{t-1} + 0.424R_{t-1} + 0.796\Delta R_t$$

$$\begin{array}{ccccccc} & & (0.054) & & (2.188) & & (0.068) & & (0.176) \end{array}$$

$$R^2 = 0.870$$

In this equation, \dot{W}_t is the quarterly wage change, C_{t-1} is the lagged change in the CPI, U_{t-1} is the inverse of the unemployment rate, R_{t-1} is the logged value of corporate profits and ΔR_t is the quarterly first difference of R. Perry's wage equation was fitted for the period 1947-60 and is of sufficiently good fit that we would expect it to be accurate in the era of the guideposts. I would expect the residuals to lose significance by early 1967 which is close to the actual pattern. The residuals would stay significant after the mid-1966 failure of the guideposts with the National Association of Machinists because restraint from earlier settlements would affect later settlements so that the guidepost impact would tail off with some type of distributed lag. This appears to be the case although I

4. John SHEAHAN, *The Wage-Price Guideposts*, Washington, Brookings, 1967.

5. G. L. PERRY, «Wages and the Guideposts» in *American Economic Review*, LVII, No 4, Sept. 1967.

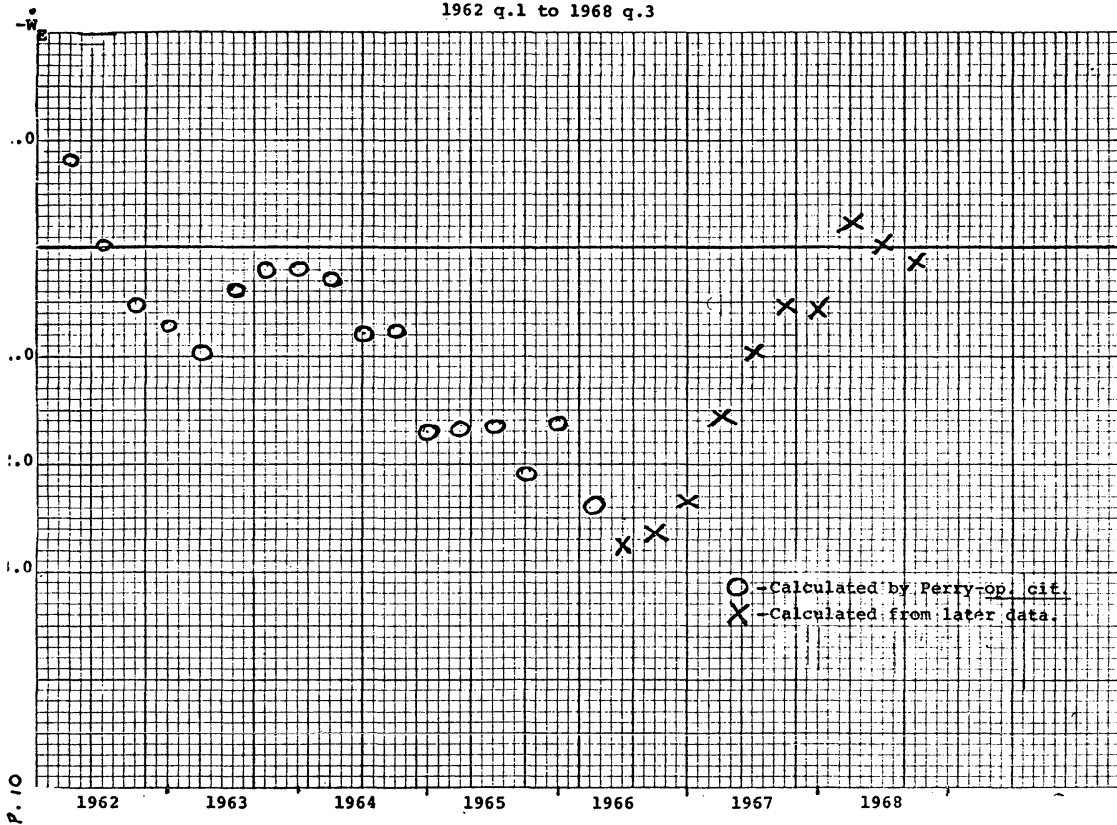
6. G. L. PERRY, *Unemployment, Money Wage Rates and Inflation*, Cambridge, M.I.T. Press, 1966.

TABLE 1 — ACTUAL MINUS ESTIMATED QUARTERLY WAGE CHANGE

<i>Year — Quarter</i>	$\dot{W}_a - \dot{W}_e$
1962 — 1	+0.84
2	+0.07
3	-0.52
4	-0.71
1963 — 1	-0.97
2	-0.37
3	-0.19
4	-0.18
1964 — 1	-0.27
2	-0.77
3	-0.73
4	-1.72
1965 — 1	-1.68
2	-1.63
3	-2.11
4	-1.61
1966 — 1	-2.48
2	-2.77
3	-2.63
4	-2.36
1967 — 1	-1.54
2	-0.96
3	-0.53
4	-0.58
1968 — 1	+0.26
2	+0.09
3	-0.17

SOURCE : 1962 q1 to 1966 q1 — Perry, *op. cit.*, p. 899
 Later figures computed from data for 1966-68.

Chart 1
Scatter Diagram of Regression Residuals
 1962 q.1 to 1968 q.3



in no way mean to imply that I consider this to be conclusive evidence. As Perry puts it, however, this evidence does tend « to shift the burden of proof » to the sceptics.

The question that this whole issue raises for industrial relations is whether there is a conflict between good industrial relations and satisfactory wage-price performance. The recent Air Canada strike is probably a good illustration of the problem. I doubt that the strike would be termed an emergency except by those who view all strikes in that light. Therefore, I feel that the action of the government in allowing a long strike was commendable particularly in comparison with the « peace at any price » policy of its predecessor. Peaceful settlements are not a mark of good industrial relations if the settlement is based on the belief that the size of the wage increase doesn't particularly matter since it can be covered by a price increase. Government policy, as apparently exemplified by Air Canada, is to have some set of implicit norms. Enforcement is more difficult for private concerns yet selective government policies in this area could be very effective. Since profit increases from 1963-1966 were a spur to large wage increases, taxes should be geared more selectively to prevent such destabilizing profit spurs. On the wage side, the government could let it be known that selective tariff cuts would occur in sectors with large wage gains, thereby lowering management's wage ceiling. Industries with strong wage-price performance would be hard pressed to logically oppose such tariff cuts. This policy would not be identical to the U.S. guidepost approach, but to enforce it, the government would, at least implicitly, require some sort of guideposts.

These ideas are certainly not the only possibilities nor are they without drawbacks. Yet, I feel that we must recognize the inevitability of such innovations in the future. Those of us whose primary interest is industrial relations may have to reshape some of our ideas with respect to normative techniques of dispute settlement if present techniques continue to create unacceptable economic results. Labour specialists appear to greet such bodies as the new Prices and Incomes Commission with yawning disdain instead of searching for ways to integrate its approaches into our present industrial relations framework. I feel that the future will not allow us to continue that attitude. Measures to control wage-price performance are still in their early stages. We must strive for intelligent methods of reducing the conflict between good industrial relations and a stable price level or face the consequences of the actions of those who seek to impose unworkable controls on the collective bargaining system.

CONSÉQUENCES DE LA NÉGOCIATION COLLECTIVE

Nous examinons dans cet exposé la troisième partie du Rapport de l'Équipe spécialisée en relations du travail intitulée : « Négociation collective et autres politiques gouvernementales ». Depuis ces dernières années, l'inflation constitue le problème le plus pressant à résoudre dans le domaine des politiques économiques. Un des buts majeurs de l'Équipe spécialisée était de déterminer à quel point la négociation collective pouvait être une cause d'inflation.

Les spécialistes ne sont pas d'accord sur la définition et la signification exacte de l'inflation par les coûts. Le Rapport traite le problème d'une façon assez équilibrée, quoiqu'à notre avis, plus de poids que nécessaire fut donné à la position extrême de l'inflation par la demande.

Le problème qui a récemment touché les pays industrialisés inclut des hausses du niveau des prix pendant des périodes où la demande est demeurée stable ou a même diminuée. Une explication de ce phénomène impliquant le pouvoir discrétionnaire des syndicats et des patrons d'obtenir des résultats sur le marché du travail et du produit en dehors du modèle compétitif, s'appelle l'inflation par les coûts. Si les prix et les salaires étaient davantage reliés aux coûts qu'à la demande, nous aurions une définition de l'inflation par les coûts, et vice-versa pour l'inflation par la demande. L'absence d'instruments appropriés qui pourraient mesurer les coûts et la demande constitue un problème encore aujourd'hui.

Nous croyons qu'à diverses périodes la négociation collective et les politiques de prix des corporations pourraient exercer une poussée ascendante nuisible à la stabilité des prix. La négociation collective ne peut pas créer seule des hausses de salaires inflationnistes. Elle doit être accompagnée par ce pouvoir des corporations qui transfère le coût des augmentations de salaires au consommateur par la hausse des prix. Ce n'est pas la négociation collective en soi qui crée le problème. C'est plutôt cette interaction du retour aux salariés des coûts qu'ils provoquent et des demandes d'augmentations de salaires visant au profit qui produit le spirale de hausses discrétionnaires des salaires et des prix.

Cette troisième partie nous semble suffisamment vague pour provoquer de fausses interprétations. Nous regrettons que l'Équipe spécialisée ait traité ce sujet comme s'il s'agissait d'un phénomène quasi politique, plutôt qu'un phénomène proprement économique. Mais nous craignons davantage les effets nocifs sur l'emploi que sur l'inflation : c'est pourquoi des mesures constructives doivent être prises pour assurer une stabilité relative des prix. L'utilisation de politiques monétaires et fiscales seulement n'est pas suffisant ; nous appuyons l'Équipe spécialisée dans sa recommandation de créer un Bureau de recherche sur les revenus et les coûts.