Bringing down the fever of inflation—albeit at tremendous human and economic cost— is the easy part. The tough part is to keep it down. The United States reduced it before, three times just between 1970 and 1982, using similar sadomasochistic recessionary baths. But it always flared again, each time rising higher than it had been before the recession.

One way to prevent that, right now, is to tie wage and salary increases to gains in productivity, instead of basing them on cost-of-living adjustments (COLA’s).

For more than three decades, many labor agreements with both union and nonunion workers have relied heavily on COLA’s. The crucial point that has been often overlooked is that the COLA pattern was established when inflation was rather low and productivity gains relatively high: the annual rate of inflation hovered around 2 percent until the late 1960s and productivity gains averaged 3.2 percent per year from 1947 to 1966. (In those faraway days, a typical contract provided a penny-per-hour pay raise for every 0.3 of a point increase in the quarterly consumer price index.) COLA’s were not inflationary, because raises could be paid out of increases in productivity.

But since the late 1960s inflation has soared, while productivity has fallen. Meanwhile, COLA’s boosted wages in many of the nation’s basic industries to the point where the industries became uncompetitive. For example, in 1980 autoworkers earned $16.08 per hour in the United States, as against $6.89 in Japan and only $7.98 even in the inflation-ridden United Kingdom. And in addition to making the United States uncompetitive in many areas, COLA-based wages immunized covered workers against inflation and discouraged them from making sacrifices to curb it.

Guidelines: Now is the time to abandon COLA’s and being negotiating raises based on productivity gains. A precedent for this approach was set when President Kennedy’s wage-price guidelines were pegged to productivity trends. According to John W. Kendrick, one of the country’s leading productivity experts, they worked quite well, until the financing of the Vietnam War overwhelmed the whole system. Of course, those were government-sponsored guidelines, while the ones discussed here would have to be worked out by labor and management. Such a plan faces serious technical difficulties, as well as some political obstacles.

The technical problem is that productivity gains are difficult to measure, especially for individual industries, above all in services (gas stations, barber shops). One solution might be to use overall national data as the basis for future raises, much as the national consumer price index is now used for COLA’s. Or the overall figures could serve as a starting point for negotiating specific settlements. For example, a highly productive industry could agree to pay workers x percent on top of the national rate. At the same time, if major productivity gains result from nonlabor factors such as technological breakthroughs, wages could be adjusted accordingly.

National productivity measurements are quite reliable. They are calculated by the highly regarded Bureau of Labor Statistics, which is beholden to neither labor nor management. The BLS already provides figures that reduce the effect of short-term fluctuations in productivity due to business cycles. (Productivity falls in recessions, rises in recoveries.) Further steps might be taken to smooth out the measurement so that wages would not jump around.
Another point to consider is that labor productivity is affected not only by the workers themselves, but also by management and the work environment. This argues for tying management’s bonuses to productivity, and strongly suggests that raises based on productivity would work best if combined with quality-of-work-life programs designed to allow workers to participate in management decisions and thus directly influence this source of productivity. Ultimately, it would be best to tie incentives to the data for each industry, indeed each corporation— even for a single plant and the divisions within it. The smaller the unit, the greater the opportunity for labor to contribute to the benefits that result from higher productivity.

Will labor agree? The situation right now seems particularly propitious because for the first time in many a moon inflation is low while productivity is gaining. Productivity gains for 1983 are projected at 3 to 3.5 percent. Inflation, so far this year, is actually below this rate. Whether in the future inflation will remain low and productivity high is anybody’s guess, but obviously a shift away from COLA’s would be a major factor in keeping inflation down, since labor costs amount to almost two-thirds of production costs. Many COLA’s do not fully compensate for inflation to begin with, so workers would lose little if anything by shifting away from them now. That COLA’s are no longer sacrosanct in labor circles can be seen from the fact that in recent negotiations quite a few unions have agreed to give them up.

‘Givebacks’: But why would management agree? Business people tend to be so dismayed by COLA’s that many seem quite willing to pay the price to rid industry of them, just in case inflation gets out of hand again. One captain of a metals industry stated that while he would not mind letting labor share in future productivity gains, wages are now too high in many basic industries for the United States to be competitive. Industries, he says, need more “givebacks” like those already obtained, to some extent, in steel. As I see it, there is no conflict here. An industry could negotiate givebacks with workers, and also agree from then on to share productivity gains.

Above all, there is something basically wrong with the implicit assumption that if something is attractive to labor, it must be to the disadvantage of management, and vice versa. The beauty of basing wage increases on productivity gains is that it highlights the point that both sides share an interest— as does the nation— in a stronger American economy, growing more with less inflation.