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# **The Political Economy of Price Controls**

**with a foreword by Mancur Olson**

**Lars Jonung**

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# THE POLITICAL ECONOMY OF PRICE CONTROLS





# The Political Economy of Price Controls

The Swedish Experience 1970–1987

LARS JONUNG

with a foreword by  
Mancur Olson

Avebury

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# Preface

This book has arisen as a result of my work as an economic expert for the Price Control Committee during the years 1977–1981. The Committee was set up in order to evaluate government price control policy in Sweden. My role was to study the impact of price controls on the rate of inflation and inflationary expectations. The study was designed to concentrate on the macroeconomic effects of price controls. However, I became increasingly concerned with the microeconomic effects of price controls, that is, on their effects at the level of the individual company. Professor Erik Dahmén, a member of the Committee sceptical of the value of aggregated studies, was also interested in the experiences of individual companies.

Erik Dahmén, who had contacts with several companies subject to price controls, suggested that we should visit one of these companies, Gullfiber AB, at its head office in Billesholm, in southern Sweden. It turned out that Gullfiber's senior management had a well-documented account of the contacts that had taken place between the company and the Price and Cartel Office (SPK) – the authority responsible for the practical implementation of price controls. This material was put at my disposal. It was subsequently supplemented by a number of interviews carried out with senior representatives of the company. This led to a report that was presented to the Price Control Committee.

The report received a mixed reception. The two economists who were members of the Committee proposed that it should be included as a separate appendix to the Committee's final report. This proposal was opposed and blocked by the other two members of the Committee who were drawn from

central government administration. Their principal argument was that the SPK would then be entitled to demand that their views on the implementation of price control policy should also be granted space in a special appendix. This was not considered to be an appropriate procedure for an official government report. The Committee supported the view that an alternative form of publication should be found for the Gullfiber study. This suggestion gave birth to the idea of the present book.

During my work on the Gullfiber study, I came into contact with other companies that had been subject to price controls. Accordingly, I decided to extend my study to include another four companies that also had well-documented accounts of their experiences of price controls, namely Siporex AB, AB MoDo Consumer Products, AB Tegelcentralen and Lilla Harrie Verkstads AB. These four studies were carried out by Jan Rydenfelt under my guidance. Chapters 3–6 are largely the result of his work and follow the same general outline as that adopted for the Gullfiber report. In addition, he also carried out most of the calculations presented in Chapter 7.

From an early stage, the Business and Social Research Institute (SNS) in Stockholm showed a great interest in the publication of the experiences of the five companies along with a general discussion of the role of price controls in the Swedish mixed economy. In the Swedish version of this book, published by SNS in 1984,<sup>1</sup> the five company case studies are part of a broad appraisal of both the micro- and macroeconomic effects of price controls.

The negotiations conducted between the SPK and the companies subject to price control comprise the central part of this book (Chapters 2–8). This bargaining process is not dealt with in any other part of the Price Control Committee's comprehensive report. The examination of both the macroeconomic effects and the political economy of price controls presented in Chapters 9 and 10 is largely based on the work that I carried out on behalf of the Price Control Committee. Moreover, this book also takes account of the experience of price controls during the years 1981–87, that is, after the Committee published its final report in 1981.

The English translation is expanded by comparison with the original Swedish version in the following ways. First, the price control policy of 1984–1987 is considered. Second, an interview with Staffan Burenstam Linder is included in a separate appendix (Appendix 3). He was Minister of Commerce for several years when price controls were applied. Third, Mancur Olson has written a foreword to the English translation. Finally, a number of minor revisions have been made as part of the translation.

I owe a great debt to those who have helped with this English version. Axel Leijonhufvud inspired me initially to start this venture and he has given me valuable comments on this work. A generous grant from the Bertil Ohlin Fund of the Swedish Royal Academy of Sciences made the translation possible. Financial support from the Jan Wallander foundation is gratefully acknow-

ledged. Alan Harkess transformed skilfully my Swedish into English. Richard Brooks suggested numerous improvements.

I have benefited from seminars held in the Spring of 1987 on this book at the World Bank, Washington DC, Carnegie–Mellon University, and at the Center for European Studies at Harvard. Erling Petersson has helped me with the statistical work. I have received valuable comments from Michael D. Bordo, Allan H. Meltzer, Mancur Olson and Hugh Rockoff. Finally, the usual academic disclaimer applies to this book.

Lund, August 1988

Lars Jonung

## Note

- 1 By sheer coincidence, the Swedish version of this book was published and presented at a press conference on April 9, the starting date of the price freeze of 1984 announced retroactively on April 12.



# Foreword

MANCUR OLSON  
UNIVERSITY OF MARYLAND

This book is, in my opinion, pertinent in an important way even to readers who have no specialized interest in Sweden or in the firms whose experience with price controls is emphasized in this book. As one who is not at all an expert on Sweden or its price control policies, I do not have a basis for drawing conclusions on any of the political disputes and policy issues in Sweden that are considered in this book. But as an economist I do have direct grounds for my conviction that readers from a wide variety of countries should find it significant for their own concerns.

Perhaps paradoxically, it is partly the *detailed, disaggregated* character of this study that accounts for its *general* pertinence. The study is based partly on the surprisingly elaborate records of five firms on their interaction with the Swedish price controls authorities. Sweden has had selective price controls for an exceptionally long time. It also is a society that takes government rules seriously and at the same time assumes that the requests, correspondence, and consultations of private firms with government agencies will get a meaningful hearing. As a result of these factors and various lucky accidents, this study has been based on a unique source of information. I have not come upon anything quite like this record before and Lars Jonung's inquiries suggest that there probably is not a parallel study in any other country. Many points of interest

about regulatory behaviour and political economy as well as about inflation and macroeconomics emerge from this unique record.

One that Lars Jonung emphasizes is that a complex and costly pattern of bargaining developed between the Price and Cartel Office (SPK) that 'administered' the price control and the firms that were subject to the price control. This price control office has by no means been without power and can have a big impact on firms, but (as I interpret Lars Jonung's account) it does not by any means always get its way. I was struck, for example, by how the labour unions supported one of the firms in its bargaining with the SPK. This bargaining might make for better prices than would price control without it, but the social costs are apparently considerable, especially when high-level public officials (whom I believe are usually people of considerable education and industry) and high-level managers (whose surely valuable time might otherwise be spent trying to make their firms more productive) are involved. Lars Jonung has estimates on some of these costs. His study is certainly consistent with the conclusion of the Norwegian economist Leif Johansen that a society can pay a considerable price for arrangements that unnecessarily add to the amount of bargaining that takes place.

Though the written records and the duration of price control in Sweden may be unusual, I believe the conclusion that there is a tendency for price controls to generate a large amount of bargaining would also apply in other societies, at least in the long run. My hunch is that in any democratic society (and in some non-democratic societies) with long-lasting price controls there is bound to be a lot of bargaining, for in almost every society there is some political power in the possession of the firms, workers, and communities in the markets affected by the price control.

The paradox that it is the local, firm-level details that help give this study its wider interest, is perhaps best illustrated by going into two points that the record in Lars Jonung's book suggests to me, but which he does not emphasize. One of these points is that cumulatively colossal losses can result from having the 'wrong' prices in many markets, even when each of these markets is apparently of only trivial importance. The other point is that, if a modern economy with price controls is to work satisfactorily, any central price-determining authority needs (among other things) even more information than most of us suppose – a computer-overloading, mind-boggling amount. I hope the reader will bear with me as I try to show, in demonstrating these two points, why disaggregated information of the kind in this book is sometimes of such general importance.

We are naturally attracted to the single crucial piece of evidence, or the single compelling argument, or the decisive experiment, that settles a matter. It is nice when the murder mystery is solved with a brilliant analysis of a single neglected clue; we are properly awed when Pasteur in a single experiment demolishes the previously respectable theory of the spontaneous generation of bacteria. The appeal of the single compelling consideration is also evident in

macroeconomics. As some economists see the subject, there is virtually only one variable, the quantity of money, that is decisive; according to others, the overwhelmingly important consideration is the level of aggregate demand in relation to the fixed (or sticky) level of wages (or of wages and prices), where all wages (or all wages and prices) are treated as a single aggregate. The familiar monetarist and Keynesian theories (like the new equilibrium macroeconomic theory) contain valuable insights that I believe it is most important to master, yet we must remember that to a large extent they direct our attention to broad aggregates rather than towards individual markets.

For many issues there is no one salient clue or one dramatic logical deduction that can settle matters: it is only the accumulation of vast amounts of detailed information that can give us the enlightenment we need. Sometimes, in the words of the student of biological evolution, Stephen Gould, 'God is in the details.' A sufficiently large number of tiny achievements may sometimes accumulate to produce a colossal success and a vast number of tiny injuries can lead to catastrophe. In one sense, the computer has only the intelligence needed to remember numbers or letters of the alphabet and to do simple arithmetic with a number system of base two; but when we first see a computer flawlessly and quickly handle a million calculations, or remember all the letters and spaces in a book-length manuscript, we are awed. The converse situation was made evident to me once when a friend described the victim of an administrative situation with thousands of minor impositions as 'being pecked to death by ducks'; whether ducks can do us in or not, we can certainly die of a thousand small cuts as well as one large one.

As I see it, an analysis of price control (or of price and wage control) is bound to mislead us if it focuses on a single supposedly compelling advantage or disadvantage or on all prices or all wages as a single aggregate; the only adequate analyses are those that convey a sense of the many tens of thousands of consequences of any effective system of price controls on many tens of thousands of separate markets.

The full importance of the details in different markets struck me once when, by a strange coincidence, I read George Orwell's *1984* in, of all cities, Berlin. In the totalitarian society of Orwell's profound imagination, there are not only memorable lies, tortures, and other momentous evils, but also a series of temporary shortages of trivial items, such as shoelaces, razor blades, and toothbrushes. The regime in Orwell's dystopia has wondrous technologies and capacities for repressing dissent and individuality, but its bureaucracy nonetheless is apparently unable regularly to process enough information and to manage enough details to prevent a series of striking shortages of minor items. I do not want to exaggerate, or to go beyond the bounds of my very limited knowledge of the German Democratic Republic, and suggest that that society is nearly identical with the totalitarian state of Orwell's dramatic imagination. But details can be important. The same time that I read Orwell's book I happened to learn of an East Berlin couple who had every resource and

authorization needed to buy an automobile in two years, and who were already buying spare parts for it! There were shortages of certain automobile parts and it paid to hoard them against the possibility they would be needed but not be available. During the same weeks that I heard this story there was an unusual heat wave and a temporary shortage of beer in East Berlin. The level of income in East Berlin was fairly high, but there were nonetheless many shortages and queues.

We must ask why those of us in the developed nations of the West take it for granted that, if we require any frequently needed part for any common make of car, it will almost always be available, if not immediately at our local supplier then by shipment from afar in a few days. If a car that cost us, say, ten thousand dollars is unusable for lack of a hundred dollar part, we might be willing to pay a hundred and fifty or two hundred dollars or more for the part rather than go without it. But if firms make a normal rate of profit when they get a hundred dollars for a part, they will make an abnormally if not fantastically high rate of profit if the price goes up by 50 or 100 per cent. So when there is a shortage of any commonplace part for any commonplace car (or indeed an enduring queue for any product for which the price varies freely), there are great profits to be made from supplying more and the shortage normally ends. This makes life more convenient for all of us, but it may be especially important for the capital-short low-income person who has to get along with an old used car.

Of course, freely varying prices do much more than ensure that we can buy shoelaces and toothbrushes whenever we need them. I am *not* here referring to the well-known point that, in a society with perfectly competitive markets, these markets will ensure an allocation of resources that is perfectly efficient, in the sense that no other allocation of resources can generate as much welfare out of any given distribution of income. The perfectly competitive market is a sometimes instructive abstraction that can make it possible to understand some problems that are too complex to analyse without the aid of simplifying assumptions, but it is not an adequate description of the wider array of markets in any real society.

Let us suppose for illustration that we have instead a market at another extreme, where there is only one seller and only one buyer. The monopolist and the monopsonist will each have an incentive to bargain with the other, and if both are rational and self-interested they will not cease bargaining with each other until they have maximized total gain; if the aggregate profit of the two can be increased, it has to be possible to make both parties better off. In most cases the marginal costs of the seller, at least in the short run, will rise or at least not fall as output increases, and the value of this output to the buyer will in the relevant range diminish, so there will normally be a unique quantity traded between the buyer and the seller at the point where joint profits are maximized. It follows that there is normally only one price for the good that will maximize joint gains. Any arbitrarily set price, unless by chance it happens to be the same



price that achieves an equilibrium from successful bargaining, will lead to social loss; it will prevent some mutually advantageous trades from being realized. Of course, the relevant costs and demands change rather frequently, so any price that is fixed for any length of time, even if it was initially at an optimum level, will soon be at a socially inefficient level and gains from trade will again be lost. In purely competitive markets, prices other than market-determined prices will also deny both buyers and sellers some gains from trade.

The situation when there is monopoly on only one side of the market can be quite different, as I will argue later, so what I have said is by no means sufficient to reach any policy conclusions. But it is, I hope, sufficient to show that to understand the consequences of price controls we must look closely at individual markets. The prices in each of tens of thousands of different markets make a difference: they determine how much of the potential gains from trade are realized, and even such things as whether beer is available in the hottest summer days. The significance that prices and price changes have in each of tens of thousands of different markets makes it impossible to understand price controls, or to make sensible policy decisions about them, without going beyond any single dramatic demonstration, and beyond macroeconomic models which treat all wages or all prices as a single aggregate. One must, in short, go into the facts of specific markets, such as those considered in this book.

We need such careful and detailed studies as this to call attention, for example, to the fact that the *buyers* of a product sometimes press price control authorities to allow a *higher* price for that which they buy. Most of the more sweeping arguments about price controls would not lead one to suspect that buyers of a good would want to argue for allowing a higher price. But Lars Jonung shows that the Swedish sugar beet growers association argued for allowing *higher* prices for sugar beet machinery. On reflection, there is nothing surprising about this: presumably the Swedish sugar beet growers are hurt by a price that is too low to make sugar beet machinery available, and hurt in the same way we would all be hurt by prices for automobile parts that were too low to make it worthwhile for firms to provide the repair parts we need. More generally, this type of example illustrates the point that disequilibrium prices deny mutually advantageous gains to both buyers and sellers.

They also sometimes deny gains to those in other markets. When a disequilibrium price in one market reduces the amount traded in that market, it reduces the demand for factors of production that would be used by the firms making the product. Lars Jonung finds that unions in firms subject to price control wanted the firms to be allowed to obtain higher prices. This could at times be due to the union local's desire for a larger surplus for the firm, which it could later hope to transfer to its members through higher wages or better working conditions. But it can at times also be due to concern that too low a price for the firm's product will reduce the firm's output and its demand for labour, thereby endangering the jobs of its employees; Lars Jonung describes

situations where this may have been the case. Naturally, the communities in which a firm with a severely constrained price is located, may also be harmed.

The book also describes interesting instances that remind me of the inadequacy of the profit rate of a firm as a determinant of whether it should have a higher price. A society may easily gain from higher prices for a firm that is already making exceptionally high profits, and it may also gain from still lower prices for firms that are already losing money. If a firm faces exceptional demand for its output it may well be making exceptional profits even if the price it receives is much lower than it would otherwise be because of price control. But at least in the short run a firm in such a situation will almost always have rising marginal costs. Some marginal production may not be profitable at the controlled price even though the firm profits handsomely on the units it does sell, so the firm will satisfy less of the demand than it would have satisfied with a higher price. Thus even some of those who buy the output of a firm with exceptionally high profits can sometimes gain from a still higher price for their vendor. Conversely, a society may gain from lower prices for firms that are already losing money.<sup>1</sup>

I hope that what has just been said makes it clear why I believe that the wrong relative prices in thousands of different markets, even if they are markets for relatively minor products such as repair parts for automobiles, can lead to colossal aggregate losses. But this is not the only reason for which, in my opinion, we need disaggregated information of the kind in this book. Another issue we can understand only if we have the disaggregated view offered here has to do with the information requirements of a modern economy. How much information would the Price and Cartel Office in Sweden, or comparable offices administering price controls in any country, need to determine what prices are appropriate in a given market at any given time? Lars Jonung recounts many requests to the firms from the SPK office for further information. But how could one know the appropriate prices in each market with even a hundred times as much information? Determining a correct price would require knowing both the production functions of the producing firms and the utility functions of countless consumers (or, if the good is an intermediate good, the production functions and factor and product prices of the firms that used the intermediate good). And what incentive would all the firms and consumers have to reveal all the information honestly if the information would be used to determine a policy that would affect their interests? Thus extensive and expensive as the meetings and correspondence Lars Jonung describes are, they could not be sufficient to enable a price control agency to determine a socially rational price.

Though price control is certainly a blunt and unsubtle instrument, I personally think, perhaps in contrast to Lars Jonung, that it would be going much too far to jump from my plea for highly specific factual studies like the one in this book, to the conclusion that no government should ever, even for the shortest period, adopt any system of price or wage controls whatever. This

is a huge issue with many different aspects and it would be quite impossible to discuss it properly in a foreword such as this. The inadequacy of any simple, universal, and dogmatic analysis of this matter can perhaps best be illustrated by looking at cases where there is monopoly on only *one* side of the market.

In such a case, in contrast to the bilateral monopoly and purely competitive cases I have considered above, an arbitrarily chosen price may either increase or decrease the gains from trade. The price that is the most advantageous to charge for a firm with some monopoly power is of course somewhat above the socially-efficient price. Thus, if the price control system or authorities should succeed in setting a price that is closer to the competitive or marginal cost price than the price the firm has an interest in charging, the efficiency of the economy will tend to increase. Perhaps this sometimes happens in the beginning of a period of price control during a mild inflation: prices are often fixed at the existing nominal level, but uncontrolled prices (such as import prices) or prices that cannot be monitored (such as those of smaller firms) then perhaps rise in relation to the fixed prices of firms with monopoly power. If other changes do not call for a totally different set of relative prices, there will be an interval during which the controlled price in the monopoly firm will be marginally lower in relation to other prices than it would otherwise have been, and (if we set other problems of price controls aside) this can temporarily increase social efficiency. I think this may help to explain why some market economies seem to have worked well shortly after the first imposition of price controls in a mild inflation; most prices are not much different than they would have been without price controls and some monopoly prices that were too high may be relatively a little lower.

But prices that remain fixed by fiat over any long period are very unlikely indeed to have this possibly redeeming virtue; as a repressed inflation gets worse any fixed prices are likely to become lower than marginal costs, and the diverse changes in technologies, resource availabilities, and demands that occur over any substantial period will make any old prices increasingly arbitrary and wasteful. Lars Jonung has also reminded me that, at least in the long run, the system of price control is also likely to be influenced in socially inefficient ways by the organizations that represent the regulated firms and by other organized interest groups, and for this and other reasons he would be sceptical that price controls would be appropriate even in the brief special circumstance I have described. Thus I emphasize, once again, my point is not to make any policy pronouncements but to urge attention to the importance of the conditions in individual situations and particular markets, and thus to argue the case for disaggregated inquiry.

Lars Jonung points out that some price control authorities sometimes had a different interpretation of some of the situations he describes. As one who has no specialized knowledge of the history of Swedish price controls or of their application to the five firms considered here, I emphasize again that I am not competent to make any judgement about any such differences. If some other

scholar with a different perspective on these matters than Lars Jonung has, should prepare a similarly careful and detailed study, that would be most welcome; it is important to look at the facts about how price control affects particular firms and markets from every angle. Should such a book appear in the future, I hope that readers will give it careful attention, as I hope they will give Lars Jonung's book now.

## Note

1. In some cases, average costs will decrease for each firm as output increases, and the faster elimination of some firms may more quickly increase output and thereby lower costs per unit for other firms, or in other circumstances also speed up the reorganization of economic activity in ways that move resources away from those activities with a greater social cost than social value, towards those activities where they will produce net gains.



# Introduction

The standard economic theory of price controls is found in almost every principles text. It predicts that the introduction of a control, setting the maximum price permitted below the equilibrium price, will cause a shortage (an excess demand), a reduction in the quantity exchanged, an increase in the number of private-allocation schemes and probably the development of black markets. This theory, often illustrated by episodes of various controls of rents and food prices, is usually taken to be exhaustive. Indeed, one reason why it is considered a suitable topic for introductory instruction is that little or nothing is added to this simple model at higher levels of training in economics.

This book tells a different story. It shows that the consequences of price controls do not necessarily follow those predicted by the common textbook model. Instead a major effect of controls is to set a political process into motion, the outcome of which is much more difficult to predict than suggested by the textbook approach to controls. This process involves the firms subject to controls, their suppliers and customers, the government agency administering the controls, higher level government organizations, labour unions, industry organizations, as well as politicians, both at the local and state level. Hence, the title of this book: *The Political Economy of Price Controls*.

The book is based on a unique set of company records made available to the author by a number of firms subject to price controls, complemented by interviews with various employees of these firms. The principal feature of the

book is a detailed description of the contacts and negotiations between individual firms and the public authority responsible for the administration of controls, the Price and Cartel Office (the SPK). The author has not been able to find in the post-war literature on price controls in Western economies any comparable analysis of the relationship between the regulatory agency and the companies subject to price controls. This literature deals primarily with econometric estimates of the aggregate effects of controls on wages and prices.

This book examines the evidence from the Swedish programme of price controls that began in 1970. Sweden followed initially the international trend towards reliance on controls to 'combat inflation' as numerous industrial countries used price and wage controls in attempting to reduce inflation in the early 1970s. However, the Swedish experience of controls 1970–1987 is unique by international comparison in at least three ways.

First, price controls have been part of economic policy for a longer period than in most other Western European economies. Second, prices but not wages have been controlled. Typically, prices and wages have been regulated simultaneously in European countries relying on controls. The strong political position of the labour union movement in Sweden has prevented direct controls on wages. Third, price controls have been applied in a very selective manner as an attempt at fine-tuning anti-inflationary policies. This was in particular the case in the 1970s.

Prior to the introduction of price controls in the 1970s, price formation in Sweden was 'free' in the sense that companies were not obliged either to notify any government agency of changes in their prices or to apply for exemption from controls in order to alter their prices. Price controls confronted companies with a completely new situation. This policy intervened directly in the pricing decisions of individual firms. Various forms of controls were used, ranging from legal sanctions to administrative pressure and negotiations between the Price and Cartel Office and individual companies.

Considering Sweden's strong socialist traditions, one might suppose that the programme of price controls created a system based on centrally determined prices in which the Price and Cartel Office acted both to set prices and to administer control, that is a system of price determination usually associated in economics textbooks with that of centrally planned economies. However, this study of the actual outcome of the program of controls does not lead to this conclusion. On the contrary: as stated above, price control policy became in effect a political process consisting of a series of protracted negotiations, bids, offers, threats, counter-threats, concessions and so on. In other words, the system of controls was a move towards the bargaining economy, a concept introduced in recent years by Scandinavian economists to describe the development of the mixed economies of Northern Europe, rather than a step towards the centrally planned economy.<sup>1</sup>

The book consists of four parts. Part I (Chapter 1) describes the main features of Swedish price policy. Part II (Chapters 2–8) deals with price control policy

from the company standpoint. The macroeconomic aspects of price control policy are discussed in Part III (Chapter 9). The political economy of price controls is examined in Part IV (Chapter 10). The final chapter (Chapter 11) summarizes the Swedish evidence on price controls.

Four appendices follow the main text. Appendix 1 gives monthly data on the degree of price controls and the rate of inflation for the period 1970–1987. Appendix 2 presents the views of the Anti-trust Ombudsman (the NO) regarding price controls. In Appendix 3 Professor Staffan Burenstam Linder, Minister of Commerce 1976–1981, gives his views on the controls. The political economy of price control measures introduced during the Nixon administration in the United States is discussed in Appendix 4.

Two further points should be made. First, the term ‘price control policy’ in the Swedish context refers both to legally binding price controls, that is controls introduced as a result of government decisions, and to the price monitoring procedures which are based on instructions issued by the government to the Price and Cartel Office. Second, this book is concerned with price controls that are used for the declared purpose of limiting rises in the general level of prices. This form of price control should be viewed as a counter-inflationary measure. Swedish price controls directed at specific markets, for example the markets for credit, foreign exchange, housing and agricultural produce, and thus motivated by reasons other than those of stabilization policy, are excluded from the discussion of this book.

## Note

1. However, it is sometimes noted that the allocation of resources in centrally planned economies is determined to a substantial extent by bargaining between various decision-making units.





# PART I

## THE INSTITUTIONAL BACKGROUND



# 1. Swedish Price Control Policy

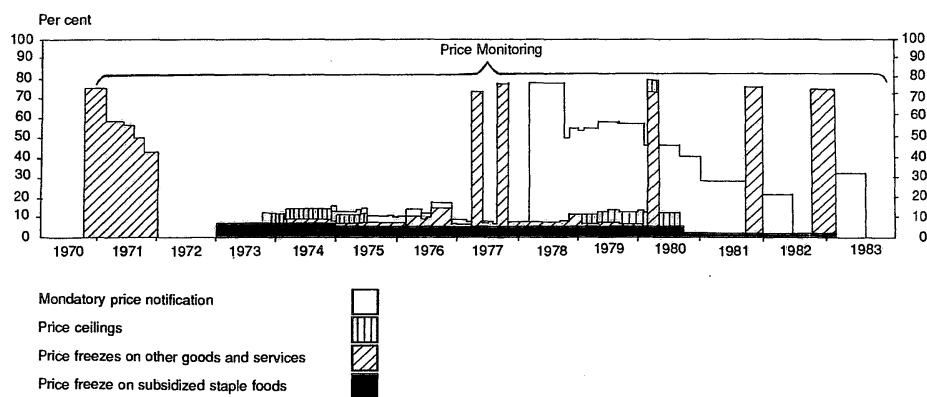
## **Price controls according to the Price Control Act**

The price control policy introduced in Sweden during World War II was abolished in the early 1950s. Throughout the remainder of the 1950s and the 1960s price formation was relatively free from government regulations, with the exception of certain sectors such as the housing, credit and agricultural produce markets. The Price Control Act of 1956 provided for limited use of price controls. This legislation, which was of a standby nature, was not implemented during the 1960s. However, at the end of August 1970, a price freeze was imposed on a number of foodstuffs.<sup>1</sup> This event marked the beginning of a new period of price control policy. The price freeze of 1970 which was introduced under the emergency provisions of the Price Control Act of 1956 was phased out during 1971 and was finally withdrawn in December of that year. In December 1972 the Price Control Act was put into operation again and has been in force since that date.<sup>2</sup>

Legislative changes introduced in 1973 extended the instrument of price controls without altering the main principles of the legislation. New forms of price control were introduced. Previously 'an appreciable risk for a serious rise in the general price level in the country' had to prevail in order to bring price controls into operation. This stipulation was now altered to 'a risk for serious price increases in important sectors of goods and service production'. Hence these legislative changes paved the way for a more selective regulatory policy and more frequent use of price controls.

The amendments to the Price Control Act in 1973 authorized four types of direct price control measures: price freeze; ceiling price; pledged price; and mandatory prior notification. In the event of a price freeze, a firm's prices are frozen at the level which prevails when the measure comes into effect. A price freeze may also be retroactive, in the sense that a price can be reduced to the level that existed at a point in time prior to the price freeze.<sup>3</sup> The Act does not stipulate any time limit for the retroactive period. A ceiling price implies that a firm is not permitted to raise its price above a certain maximum level. A pledged price means that a firm agrees not to exceed a certain price. Mandatory prior notification implies that a firm is obliged to report and justify planned price increases to the price control authorities at least one month in advance.

Swedish price control policy since 1 July 1973 has been based on a combination of the Price Control Act of 1956 and the amendments to this Act introduced in 1973. The operation of the various forms of legally binding price control measures during the period 1970-1983 is described in Figure 1.1 and Table 1.1. As seen from the figure and the table, use has been made of both general and selective measures of price control during this period. Figure 1.1 contains six major columns which refer to periods of general price freeze covering 70-75 per cent of private consumption. The first general price freeze in 1970-1971 marked the beginning of the price control policy of the 1970s and 1980s.



*Note:* The diagram refers to the share of price-controlled goods and services at the end of each month. Almost all private consumption except housing was also subject to price monitoring between February 1971 and December 1983. The system of price monitoring was first introduced in February 1971 in conjunction with the abolition of the 1970-71 price freeze. An extensive system of price monitoring was in operation from the beginning of January 1972.

**Figure 1.1** Share of total private consumption of goods and services subject to price controls under the Price Control Act, January 1970 – December 1983

In conjunction with the devaluations of the Swedish currency, the krona, a temporary general price freeze was put into effect during the spring and autumn of 1977. During the spring of 1980, a price freeze lasting two months was introduced in order to facilitate a collective wage agreement in the labour market. The devaluation in September 1981 was accompanied by a general price freeze which lasted until the end of December 1981. A general price freeze was brought into operation in conjunction with the devaluation of the krona in October 1982. It remained in effect until February 1983.

The system of mandatory prior notification which was introduced during the spring of 1978 covering approximately 70 per cent of total private consumption was prompted by a desire to keep the inflation rate within the limits of the inflation clause stipulated by the then current central wage agreement. The proportion of goods and services covered by mandatory prior notification was gradually reduced during the following four years 1978–1982. In June 1982 mandatory prior notification was abolished for all remaining categories of goods and services. However, following the 1982–83 price freeze, it was reintroduced for approximately 30 per cent of goods and services during the period March–September 1983.

Figure 1.1 also indicates that a price freeze equivalent to approximately 5–7 per cent of total private consumption was in operation between January 1973 and October 1980. This price freeze covered a number of subsidized staple foods such as milk, cheese and meat. Price controls on milk were removed at the beginning of 1983. As shown in Figure 1.1, price freezes and mandatory prior notification have been the principal forms of legally binding price controls.

The selective nature of Swedish price control policy is readily apparent from Table 1.1, which lists thirty-one categories of goods and services that were subject to selective controls during the period 1973–1983. These controls were applied in addition to the general controls introduced during the period. Table 1.1 is based on a classification into five categories: food products, household goods, passenger cars, building materials and miscellaneous. (See Chapter 10 for an analysis of the choice of goods and services subject to selective controls.)

Once a sector or commodity has been subject to selective controls, it is often the case that the controls are subsequently renewed, see for example coffee, sanitary towels, petrol, wood products and pulp wood. In practice, selective price controls have tended to become protracted. The price freezes on cheese, beef, pork and canned meat lasted for more than seven years while that on milk was in operation for about ten years<sup>4</sup>.

Following the devaluations of 1981 and 1982, price controls have been used less selectively, and instead have been tied to various stabilization policy measures. In 1983 the government announced as a goal for its economic policy that the rate of inflation should be 4 per cent during 1984. However, in the spring of 1984 the rate of inflation was expected to rise above this goal. As a

**Table 1.1. Goods and services subject to selective price controls under the Price Control Act, 1973-1983. Schematic classification into five categories**

Food products	Household goods	Passenger cars, petroleum products	Paper, wood products, building materials	Miscellaneous
Chicken (6 Sep. 1976–31 Dec. 1980)	Toiletries and cleaning products (18 June 1975–24 Mar. 1976)	Petrol, fuel oil (19 Oct. 1973–30 June 1975; 18 Nov. 1978–12 Sep. 1980)	Building materials, etc. (15 Mar. 1974–21 Dec. 1975)	Hides, skins, leather goods (3 Mar. 1976–10 Oct. 1978)
Canned and frozen foods (3 May 1976–21 Dec. 1976)	Nappies and soft paper products (15 Mar. 1974–24 Mar. 1977; 24 Oct. 1978–25 Jan. 1979)	Passenger cars, spare parts (4 Aug. 1976–21 Dec. 1976)	Wood and carpentry products, etc. (7 Sep. 1973–21 Dec. 1974; 16 June 1976–22 June 1982)	Agricultural machinery (11 Sep. 1974–2 Feb. 1976)
Flour, bread (15 Mar. 1974–22 June 1982)	Sanitary towels (24 July 1974–21 Dec. 1975; 16 June 1976–24 Mar. 1977)	Auto batteries (18 Nov. 1978–25 Jan. 1979)	Pulp, fine paper, kraft & cardboard (7 Sep. 1973–24 Mar. 1977)	Fertilizers (11 Sep. 1974–2 Oct. 1975)
Margarine (28 May 1975–24 June 1976)	Electrical household appliances (21 Dec. 1974–21 Dec. 1975)		Pulp wood (7 Sept. 1973–21 Dec. 1975; 16 June 1976–22 June 1982)	Trucking (2 Sep. 1975–13 July 1976; 18 Dec. 1977–31 Dec. 1980)
Potatoes (24 Nov. 1975–24 June 1976)			Mineral wool, insulating panes & cellular plastic (25 Mar. 1977–22 June 1982)	Room rentals (19 May 1979–31 Aug. 1979)
Coffee (26 June 1975–4 Aug. 1977)			Cement roofing tiles (21 Dec. 1977–10 Oct. 1978)	
Subsidized staple foods, cheese, beef, pork, cured meat (1 Jan. 1973–21 Oct. 1980); milk (1 Jan. 1973–24 Sep. 1983)			Bricks (27 Jan. 1978–3 May 1978)	
			Plate glass (4 Aug. 1978–10 Oct. 1978)	
			Plastic flooring (24 Oct. 1978–18 May 1979)	
			Kitchen cupboards & wardrobes (28 Mar. 1979–16 May 1980)	
			Plywood (28 June 1980–21 Oct. 1980)	

*Notes*

1. This table is not comprehensive; in many cases, the price control category was adjusted for certain goods. The duration of price controls in the table covers all categories of measures according to the Price Control Act.
2. The dates in parentheses refer to the duration of price controls. The measures include price freezes, price ceilings, maximum price pledges and mandatory prior notification.

consequence of this anticipated development, a freeze on prices and rents were instituted. The price freeze lasted from April to June 1984 and following special legislation in Parliament, the freeze on rents went into effect on June 28th and was ended by November 1st the same year. In spite of the goal of 4 per cent inflation during 1984, the actual rate turned out to be about 8 per cent.

In 1984, the government and representatives for the unions and employers reached an agreement aimed at restricting the increase in wages during 1985 to 5 per cent. The agreement was based on the requirement that the rate of price inflation should not exceed 3 per cent during 1985. An 'unexpectedly' high rate of inflation in January– February 1985, which was registered at the same time as the central wage bargaining process was started, induced the government to introduce a general price freeze in March 1985.

At the same time, the government agency in charge of price controls (SPK) was ordered by the government to negotiate with individual firms or groups of firms concerning their prices. The idea was to eliminate the controls as 'price agreements' were established. Gradually, as such agreements came into effect, the price freeze was dismantled and finally abolished in October 1985. The price agreements generally lasted into early 1986. The government's goal of 3 per cent inflation turned out to be unattainable; the actual rate for 1985 was almost twice as high.

A general price freeze was introduced anew in February 1987. The driving force behind this step was the fact that the rate of inflation during 1986 was found to be 0.02 percentage points above the level stipulated in the central wage agreement of 1986 as the critical level that gave the unions the option to renegotiate the current wage agreement. The unions decided not to use this right but asked the government to 'restrict' the rise in prices during 1987. As a consequence of this request, the government responded with the price freeze of 1987.

The SPK was instructed in June 1987 by the government to negotiate with firms and industries in order to obtain agreements about prices set during 1987. As such agreements were reached, as a rule covering prices charged prior to February 1988, the legally binding price freeze was gradually replaced by mandatory prior notification of increases in prices one month in advance. At the end of December 1987 the price freeze was abolished. See Appendix 1 for data on the coverage of the price freezes of 1984, 1985 and 1987.

## **Price monitoring**

In addition to the measures implemented under the Price Control Act, the Swedish Price and Cartel Office has also been monitoring prices ever since the agency's inception in 1957. Initially, price monitoring was generally passive in character. The function of the Price and Cartel Office was to collect and analyse data on price movements and price formation. However, in the early



1970s, the Price and Cartel Office was instructed by the government to play a more active role in price monitoring. In conjunction with the dismantling of the 1970–71 price freeze, the government directed the Price and Cartel Office to ‘extend and intensify its price monitoring activities’. This meant that the Price and Cartel Office was required to notify the government of ‘price movements that might warrant special measures’. In July 1973 changes were made in the government’s directives to the Price and Cartel Office. The SPK was instructed ‘to conduct consultations with companies, organisations and other bodies concerned with price setting in order to influence prices in a direction favourable to the interests of consumers’.

Price monitoring is based on a notification procedure whereby a number of companies chosen by the Price and Cartel Office are required to submit information to the Price and Cartel Office on intended price changes not more than one week after the decision has been taken to alter prices.<sup>5</sup> However, this statutory requirement based on the Mandatory Notification Act not only applies to changes in prices but also to variations in quality and quantity, terms of payment, and in package size. All of these changes are considered to be equivalent to an alteration in the price of the product. Notification is also required for new consumer products. Information also has to be provided to the Price and Cartel Office regarding the reasons for the price changes. This notification procedure, which became very extensive during the 1970s, covered approximately 900 leading manufacturing and import firms and 1600 service firms. Hence this notification procedure enabled the Price and Cartel Office to monitor the price movements of nearly all the goods and services included in domestic private consumption with the exception of the housing sector.<sup>6</sup>

Approximately one quarter of all price notifications have led to a request by the Price and Cartel Office for supplementary information concerning the reasons for the price increases. In about 10 per cent of these cases, the Price and Cartel Office has asked for discussions with the companies concerned. In accordance with its directives, the Price and Cartel Office has endeavoured during these discussions to influence price formation in ‘a direction favourable to consumers’ that is, it has tried to limit or prevent price increases. In certain cases, the information provided to the government by the Price and Cartel Office as a result of its consultations with individual companies has, in effect, constituted a recommendation for government action to introduce legally binding controls under the provisions of the Price Control Act.<sup>7,8</sup>

There are strong grounds for treating price monitoring as an integral part of price control policy. The Price Control Commission examined the relationship between the legally binding measures based on the Price Control Act and the price monitoring procedures which do not give rise to any legally sanctioned control of prices. The Commission concluded that these two types of measures were closely interrelated and ought to be considered as an ‘integral system’ when examining the effects of the price controls.

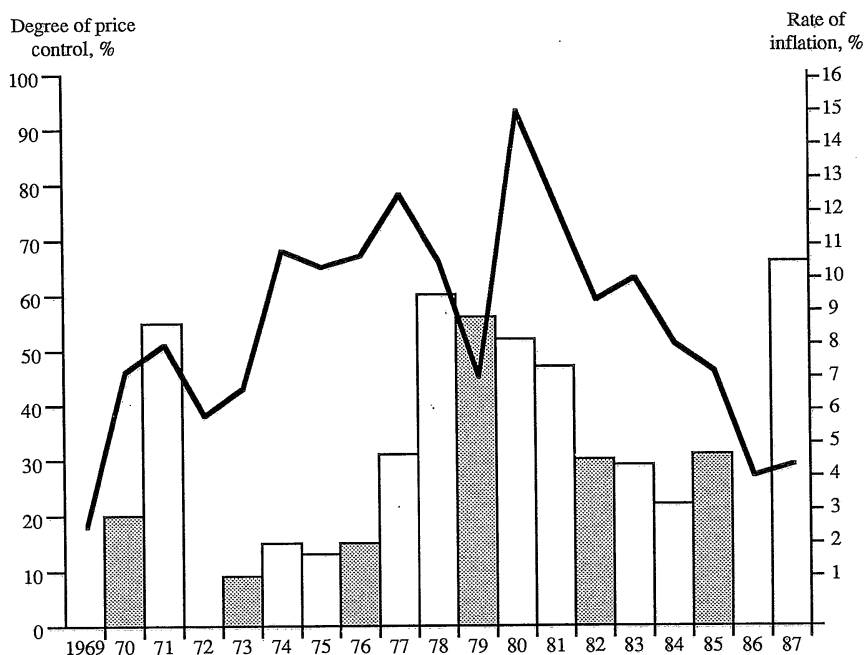
During the 1970s, government policy on prices has been based on the close interplay of the price monitoring conducted by the Price and Cartel Office, government guidelines for this monitoring process and Government intervention under the provisions of the Price Control Act. As a result, the pricing decisions of individual companies have been subject to both continuous scrutiny and direct intervention via price controls or other related measures. Although price controls are, in formal terms, of short duration and only apply to certain sectors, developments since 1972 in the area of price policy have significantly contributed to what is, in effect, a system of permanent price controls. Accordingly, the continuous public scrutiny and direct intervention into company price decisions outlined above can be viewed as a functional system of price control. It should be noted that price monitoring also covers areas such as investigations, registrations and information which are not inherently regulatory in character. However this does not affect our conclusions regarding the principal features of government policy on prices.

Hence in the context of an evaluation of the effects of price control policy, it would not seem possible to maintain a strict line of demarcation between formal price controls and price monitoring procedures. On the contrary, it would seem to be of essential importance to consider these measures as part of an integral system of a price control policy.<sup>9</sup>

A minority of members on the committee were less negatively inclined towards price control policy than was the case with the majority of committee members. However, this minority also held the view that 'in many cases' legally binding price controls were identical with price monitoring. The view that price monitoring is a form of price control is also supported by the fact that companies actually perceived price monitoring in these terms. This emerges clearly in Part II of this book which is concerned with the actual dealings that individual companies have had with the Price and Cartel Office. Thus the term 'price control policy' will be used below to refer to both the price controls that operate under the legal provisions of the Price Control Act and the non-legally binding procedures of price monitoring.<sup>10</sup>

### **The extent of price control policy**

Due to the many different types of controls, monitoring procedures, and contacts and negotiations, it is difficult to find an unambiguous measure of the extent of price control policy. The degree of price control shown in Figure 1.2 represents a minimum measure of the coverage of price control policy. It measures the percentage share of total private consumption of goods and services subject to price controls under the Price Control Act during the period 1969–1983 expressed as annual averages of monthly figures as displayed in Appendix 1. Thus, the degree of price control covers the various forms of price controls listed in Figure 1.1 by means of a summation of price freezes, price ceilings and mandatory price notification.<sup>11</sup> Price monitoring which has



Source: Appendix 1.

Notes: Price control indicated by columns

Rate of inflation indicated by continuous line

Election years are shaded

The degree of price control measures the percentage share of total private consumption of goods and services subject to legally binding controls, expressed as an annual average of monthly data. If the price monitoring by the Price and Cartel Office is included in the measurement of the degree of price control, almost all private consumption of goods and services with the exception of housing was covered by price controls during most of the period 1970–1987. No legally binding controls were in effect in 1972 and 1986.

**Figure 1.2 Degree of price control and the rate of inflation 1969–1987**

existed alongside the price controls implemented under the Price Control Act is not shown in Figure 1.2. If price monitoring were to included, almost all private consumption in Sweden excluding the housing sector was subject to price controls. Figure 1.2 also displays the rate of inflation that prevailed during the period 1969–1983. The rate of inflation was high and variable compared to the experience of the 1950s and 1960s.

The first period of general price freeze during the autumn of 1970 and the whole of 1971 raised the degree of price control from 20 per cent in 1970 to more than 50 per cent in 1971. No legally binding price controls were in operation during 1972. During the period of Social Democratic government 1973–1976, price controls were primarily selective, that is, aimed at specific groups of goods and services. The degree of price control during this period varied between 9 and 15 per cent per annum.

The price control measures of the non-Socialist coalition governments of 1976–82 were largely linked to general stabilization policy, that is, to the devaluations in 1977, the guarantee provisions (cost of living clause) in the wage agreement for 1978–80, the collective wage negotiations of the spring of 1980 and the devaluation of September 1981. On these occasions either a general price freeze or mandatory prior notification of price increases was brought into operation. As a result, the degree of price control varied between 30 and 60 per cent per annum during the period 1977–1981.

The October 1982 devaluation which followed the election in September when the Social Democratic Government came to power, was accompanied by a general price freeze from October 1982 to February 1983. This contributed to a degree of price control during 1983 of almost 30 per cent. The price freezes of 1984, 1985 and 1987 gave rise to a degree of price control of 22, 32 and 69 per cent, respectively. (See also Table 10.2 and Appendix 1.)

Another indication of the extent of price control policy is provided by Table 1.2 which shows the number of applications for exemptions from price controls, appeals, prior notifications and infringements of price controls during the period 1973–1979. The table illustrates different aspects of the administration of price controls. The Price and Cartel Office received around 7 800 applications from companies for exemption from price controls. About 20 per cent of these applications (1 500) were rejected by the Price and Cartel Office and approximately 60 per cent (4 800) were either wholly or partially approved. In a substantial number of cases, no action of any kind was taken by the Price and Cartel Office. Two hundred and fifteen appeals were made by companies against the rejection of applications by the Price and Cartel Office. In 17 cases, the government upheld these appeals either wholly or in part. The remainder were either rejected or did not lead to any action being taken.

The system of compulsory prior notification of planned price increases gave rise to over 28 000 notifications being made by companies to the Price and Cartel Office during the years 1973–1979. Furthermore, Table 1.2 indicates

**Table 1.2 Applications for exemptions from price controls, appeals, prior notifications and infringements of price controls dealt with by the Price and Cartel Office (SPK) during the period 1973–1979**

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Number of applications for exemptions received by the SPK:	7 804
of which:	
wholly approved	2 560
partially approved	2 197
rejected	1 500
no action taken, no objection, undecided, etc.	1 547
Number of appeals to the government (approx).	215
Number of prior notifications to the SPK of planned price increases of goods and services subject to mandatory prior notification	at least 28 000
Number of infringements of price controls dealt with by the SPK:	903
of which:	
no action taken	308
written objection	585
referred to the Public Prosecutor for further action	10

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*Note:*

The table covers only the administrative measures that arose as a result of legally binding price controls. Price monitoring and the notification procedure gave rise to a substantial number of notified price increases to the Price and Cartel Office. However, there is no exact measure available of the volume of price notifications. According to Yngve Lindén, the Head of the Statistical Section at the Price and Cartel Office, it was of the order of 100 000 notifications during the 1970s.

that the Price and Cartel Office, which also has responsibility for ensuring that companies comply with price controls, reported 903 instances of infringements of price controls. Ten of these cases were subsequently referred to the Public Prosecutor.

Table 1.2 illustrates the measures taken and the administrative procedures followed – both by the Price and Cartel Office and by companies – as a result of the introduction of legally binding price controls in the period 1973–1979. However, as will be seen in Part II, this description is far from comprehensive: price controls gave rise to a substantial amount of administrative work in companies subject to controls. Moreover, Table 1.2 does not take into account the price notifications and discussions that arose as a result of price monitoring. As can be seen from the commentary to the table, these have been estimated to be of the order of 100 000 during the 1970s. The price freeze of 1970–71 brought about measures similar to those demonstrated in Table 1.2 for the period 1973–74. The price freeze during 1970–71 gave rise to 7500 applications for exemptions. One-fifth of these were rejected. Just under 2 000 infringements of price controls were also reported during this period. Ninety of these cases led to legal proceedings. Of 14 cases which had been heard by the end of 1971, 12 had resulted in prosecution. The price freeze of 1981–1987 also gave rise to a considerable volume of applications for exemptions, appeals and reported infringements as shown in Table 1.3. The total numbers for the price freezes of 1981, 1982–83, 1984 and 1985 are 8080 applications, 183 appeals and 187 infringements. No data is available for the freeze of 1987. (The freeze on rents in 1984 gave rise to similar administrative measures (see Table 1.3).

## **The role of the Price and Cartel Office**

The headquarters of the Price and Cartel Office (Statens pris- och kartellnämnd, the SPK) are situated in Stockholm. During the financial year 1980–1981, the staff in Stockholm consisted of about 200 full-time posts. Approximately 30 of these posts represented additional staff resources that were made available in conjunction with price controls implemented during the 1970s. A substantial proportion of the other personnel at the Price and Cartel Office were closely involved with control policy as a result of the various investigations carried out by the Office. At the county level, the Price and Cartel Office has a field organization based on the Price Department of the County Administration Boards. In 1980–1981, these departments had a staff of 75 of whom 21 were engaged in questions relating to price control. These numbers were roughly the same during the whole period 1970–1987.

As we have seen above, the Price and Cartel Office is the authority which administers price control policy: it issues injunctions, reviews requests for exemptions, receives price pledges and ensures that price control regulations are observed. In accordance with its responsibility for price monitoring, the Price and Cartel Office also handles contacts and negotiations with firms. The Price and Cartel Office is also required under its directives to inform the government whenever price movements in a specific sector might warrant

**Table 1.3 The administration of general price freezes 1981–1987**

Date of price freeze	Number of applications for exemptions	Number of appeals to the government	Number of infringements of price freezes reported to the SPK
1981 (Sep. 17–Dec. 31)	1277	41	16
1982 (Oct. 9 – Dec. 31)	1648	12	34
1983 (Jan. 1 – Feb. 28)	1384	34	54
1984 (Apr. 14 – June 30)	1711	52	34
1985 (Mar. 13 – Oct. 18)	2060	44	49
1987 (Jan. 28 – Dec. 20)	n.a.	n.a.	n.a.
Total	8080	183	187
The freeze on rents 1984 (June 28 – Oct. 31)	105	18	9

*Source:* The Annual Report of the SPK, various issues.

*Comment:* The table covers administrative measures due to price freezes in the period 1981–1987. No data was compiled by August 1988 concerning the administration of the price freeze of 1987.

implementation of the Price Control Act, that is whenever there arises ‘a risk for serious price increases in the country in important goods and service sectors’.

The obligations of the Price and Cartel Office constitute a right of initiative. It carries out assessments – on the basis of the government’s guidelines for price monitoring – regarding the particular sectors and companies that ought to be reported to the government. These evaluations are inevitably arbitrary since there is no clear-cut method for determining whether price increases are ‘justified’ or ‘unjustified’. It is then up to the government to decide whether price control measures under the Price Control Act should be introduced. Over

a period of years a close measure of collaboration has been established between the Price and Cartel Office's monitoring activities and reports to the government, and the government's subsequent legal enforcement of price controls. In many instances, individual firms have not been able to distinguish between the different forms of monitoring, negotiations and legally binding controls.

The Price and Cartel Office has thus assumed a dominant role in establishing the policy of price controls primarily due to its continuous contacts with and monitoring of a wide range of price-setters. The strong position of the Price and Cartel Office in relation to individual companies is also due to the agency's access to vital information regarding the financial situation of companies through the reporting system. Moreover individual companies have also been aware that the Price and Cartel Office may submit a report to the government – which will in turn introduce the sanctions contained in the Price Control Act – if it considers that the company is being insufficiently cooperative. The central role played by the agency in the policy of price controls will be discussed in Part II below in relation to the experiences of individual companies as well as in Part IV, which deals with the political economy of price controls.

## Conclusions

Price controls were in frequent use in Sweden during the period 1970–1987. In spite of the fact that the preliminary work on the amendments to the Price Control Act, introduced in 1973, stipulated that price controls should remain in force for relatively short periods of time, price controls undoubtedly became a permanent feature of Swedish economic policy after 1970. In this context, it should be noted that there was never any precise definition of the length of 'short periods of price control'. In reality, price control policy including price monitoring has led to prolonged and recurring periods of control in a wide range of sectors throughout the Swedish economy.

In terms of international comparisons, Swedish price control policy possesses a number of striking features. First, there is a marked emphasis on direct intervention into the pricing decisions of individual firms or sectors. The various forms of controls that are used for this purpose, including consultations, negotiations and administrative pressures, will be examined in detail in Part II of this book. A striking aspect of Swedish price control policy is thus its selective nature. In most other countries, price controls have been operated on a less discriminatory basis. Second, controls on price increases in Sweden have not been accompanied by any corresponding direct controls on wage movements. No constraints have been placed on price increases that are due to contractual wage agreements. The majority of industrialized countries that have attempted to implement some form of incomes policy have usually



imposed both wage and price controls. The strength of trade union and employer organizations in the Swedish labour market combined with a tradition of 'free' collective bargaining are the most probable explanations for government reluctance to introduce wage controls while regulating prices.

## Notes

1. In the view of the Social Democratic Government of the day, an emergency situation had arisen in August 1970. This was shortly before the general election to be held in September. The political aspects of price controls are dealt with in Chapter 10.
2. The Price Control Act is an enabling act which means that Parliament is required to renew the legislation annually in order that it can remain in force. These annual extensions have been granted every year since December 1972. It was most recently extended in December 1987.
3. The date from which the price freezes operated did not usually coincide with the date of the actual decision to implement the price freeze.
4. The marked concentration on price controls of foodstuffs emerges clearly from Table 1.1. This is largely explained by the high proportion of household expenditure devoted to the purchase of food. The actual selection of goods and services subject to price controls is discussed in Chapter 10.
5. The notification procedure is based on the provisions of the 1956 Mandatory Notification Act. This act was introduced in order to compel companies to submit information to the Price and Cartel Office on the prices charged by firms. The price monitoring activities of the Price and Cartel Office are described in more detail in SOU 1981:42, Appendix 8.
6. Price monitoring has been so extensive that the Price and Cartel Office has used data from the reporting system and supplementary price measurements to construct and publish a continuous monthly price index for private consumption. This series is generally comparable to the consumer price index compiled by the Central Bureau of Statistics.
7. Price monitoring was made somewhat less restrictive in June 1982. However, new government directives to the Price and Cartel Office in February 1983 reintroduced stricter monitoring procedures.
8. There are no exact figures available for the total number of notified price changes, requests for supplementary information or for consultations between the Price and Cartel Office and individual companies. See the comment to Table 1.2.
9. See SOU 1981:40, pp 12–122.
10. The evidence provided by the Anti-Trust Ombudsman (NO) in Appendix I also lends support to this interpretation.
11. Pledged prices are excluded. The coverage of this measure can hardly be calculated since individual firms have made pledges concerning their prices. The other types of legally binding price controls have been applied generally, ie, to groups of commodities or services – not to individual firms. Pledged prices have been used for three commodities: bread, chicken and potatoes.
12. This is also evident from the description in Part II. The problem of finding a clear, unambiguous method of estimating the 'correct' price change is a classic one in the literature on price control. See for example, Grayson-Jackson (1974).

## PART II

# THE MICROECONOMICS OF PRICE CONTROLS



# 1. Introduction

In order to assess the role played by price control policy, it is essential to analyse its effect on individual companies. In the Swedish debate on price controls, two lines of argument have been put forward. On the one hand, price controls have been interpreted as a relatively harmless policy measure that has been administered in a flexible fashion by the SPK. According to this view, price controls have not created any major problems for individual companies. The other line of argument maintains that the opposite is in fact the case: price controls have had a seriously damaging effect on companies and thereby on the economy as a whole.

One possible approach to the assessment of the effect of price controls at the company level is to analyse material from the archives of individual companies subject to controls. It is this approach which forms the basis for the case studies in Chapters 2–8.

Five companies, Gullfiber AB, Siporex AB, AB MoDo Consumer Products, AB Tegelcentralen and Lilla Harrie Verkstads AB, have provided such archive material. The conclusions derived from these studies are naturally dependent on the material that the companies made available. This raises a number of questions. Is the material biased in favour of the company and against the regulatory authority? Does the material omit important parts of the companies' contacts and negotiations with the regulatory authority? In order to answer these questions, it is useful to examine the origins and basic characteristics of the source material. For this purpose, we will study the material made available by Gullfiber AB.

Gullfiber kept detailed records of their contacts with the SPK concerning the price freeze imposed on mineral wool during the period 1974–75. Employees of the company made comprehensive notes immediately following meetings and conversations with representatives of the SPK. These memoranda provide a detailed account of the contacts and meetings between Gullfiber AB and the SPK, the arguments put forward by both sides, as well as the various estimates presented for prices, costs and production. These records also include a description of the general atmosphere in which the meetings were conducted. The archive material also sheds light on the planning and discussions within Gullfiber both prior to and after meetings with the SPK.

The records kept by Gullfiber AB almost certainly provide an accurate and realistic account of the company's experience with regard to the price freeze on mineral wool. The memoranda were written on a continuous basis, immediately following contacts with the SPK. The purpose of these records was to provide the company with a basis for its planning and policy decisions in relation to the price freeze on mineral wool. Hence this material would also have a bearing on the company's overall operations. These records were kept solely for the company's own internal use and at no point were they considered to have an external use. Consequently, there is little reason to expect that Gullfiber tried to influence or steer the content of this documentation in a manner favourable to itself or detrimental to the interests of others. Moreover, the company's memoranda are also in complete accordance with the contents of the correspondence between Gullfiber AB and the SPK.<sup>1</sup> The same general comments on Gullfiber's source material can also be made in relation to the records of the other four companies. Although the latter were not nearly as comprehensive as in the well-documented case of Gullfiber, these companies' experience of price controls, as will be seen in Chapters 3–8, was largely similar to that of Gullfiber. This lends support to our contention that company archive material is not subject to any marked degree of bias.

Another central question concerns the representative nature of the case studies. Can they be considered as examples which typify the operation of price control policy or do they only represent certain unique aspects of this policy? This question is discussed in Chapter 7. The conclusions drawn from the five case studies are compared with the results from an interview study carried out by the Government Consultant Organization on behalf of the Price Control Committee.

A relatively large volume of archive material is available for most of the five companies. Consequently, it has been necessary to eliminate some of the archive material in order to convey the essential nature of the contacts between the companies and the SPK as well as to avoid repetition and the inclusion of material which is not strictly relevant to this study. Long discussions and company estimates of costs and revenues have been summarized in a few lines without the exclusion of any vital information. The analysis of the company records has been supplemented by interviews with various members of staff in

the different companies. The latter have also subsequently checked in detail this description of the process of price controls in their respective companies.

Although the memoranda and the correspondence are frequently comprehensive in their coverage, it is almost certainly the case that not all of the contacts and consultations between the companies and the SPK have been documented. In particular, a greater number of telephone calls and internal discussions would appear to have taken place than could be established on the basis of the company records. Nevertheless, the general impression and the conclusions drawn from these accounts of the operation of price control policy can hardly be altered by the fact that they do not cover all of the contacts and discussions.

The assessment of the operation of price control policy in Chapters 2–6 is arranged in a chronological ‘diary format’. A large number of direct quotations have been made from crucial parts of company memoranda, internal reports and from correspondence between the companies and the SPK. The quotations are usually presented unabridged. When this is not the case, the omitted section is indicated. In some instances, the names of the individuals who represented the companies or the SPK are given in parentheses.

It should be borne in mind that these case studies are accounts of how price control was experienced by individual companies. Memoranda and records kept by employees of companies whose products are subject to price control represent the tangible evidence of what is purely a company-based view of price controls. This perspective is essential in order to analyse the microeconomic effects of price controls. A description of price controls from the perspective of the regulatory authority may have led to a different interpretation of actual events. This is confirmed by our contacts with officials from the SPK regarding the contents of the next chapter. However, it should be pointed out that these officials did not question the factual accuracy of these case studies. Rather, they suggested that the process of regulation was more ‘friendly’ in character than suggested by the case studies.

The author tried to persuade officials from the SPK to describe price controls from the perspective of the regulatory authority for the Swedish edition of this book. However, these attempts did not meet with a positive response.

## Note

1. The archives of the SPK contain information referring to the price controls imposed on Gullfiber’s products. However, for reasons of official secrecy, this archive material is not available to the general public. In conjunction with discussions held by the Price Control Committee into the question of Gullfiber’s experience of price controls, representatives from the SPK stated that an examination of the SPK archives would not provide any additional information to that already available in Chapter 2 below. Moreover, according

to the same SPK sources, the SPK archive contained substantially less information on contacts between Gullfiber and the SPK than the large body of material on price control available from Gullfiber's own archives.

## 2. Price controls on insulation materials.

### The case of Gullfiber AB 1974 – 1976

#### **Gullfiber AB**

Gullfiber AB, which has its head office in Billesholm in Skåne originates from Höganäs-Billesholms AB, a mining company which operated in north-western Skåne during the first three decades of this century. As a result of the depression of the 1930s and the import of cheap coal, the company was forced to close down its coal mining operations. In order to provide alternative employment, a subsidiary company started up the manufacture of glass wool.

Following the purchase of a patent from the French company, St Gobain, the production of glass wool increased markedly. During the 1970s there was a substantial growth in the demand for insulation materials owing to the marked rise in the price of oil and other sources of energy. Gullfiber underwent a period of rapid expansion, increasing its turnover from 200 million SEK in the early 1970s to 800 million SEK by the end of the decade. The company's investment programme grew at a substantially faster rate.

Today, Gullfiber manufactures mineral wool and other insulation material. The company has 55 per cent of the Swedish market for mineral wool while the state-owned Rockwool AB accounts for the remaining 45 per cent. Production is based on glass wool and uses an advanced, capital-intensive technology.



## Price controls 1974–75

### *Dramatis Personae (in order of appearance)*

#### Price and Cartel Office (SPK)

Lennart Göransson	Head of section
Karl-Johan Jargenius	Head of section
Lars Starell	Head of section
Lars Axling	Head of section
Olof Pontusson	Head of department
Åke Englund	Director General
Curt Ohlsson	Head of division
Stefan Saläng	Head of section
Åke Hallman	Head of division

#### Gullfiber AB

Einar Eriksson	Deputy Head of Marketing
Malte Johansson	Managing Director
Bertil Lundell	Head of Marketing
Willy Malmros	Deputy Managing Director
Göte Boman	Director
Knut Aronsson	Employee

#### Others

Hans Risberg	Director, building materials section of the Federation of Swedish Industries
Göte Rossing	Ombudsman, Swedish Factory Workers' Union
Mr Linden	Representative from AB Becker
Mr Linderöth	Representative from AB Gyproc
Mr Sunne	Representative from AB Euroc
Tage Larfors	Member of Parliament, Katrineholm
Bengt Dennis	Under Secretary, Ministry of Commerce
Einar Ågren	President, Swedish Factory Workers' Union
Folke Pehrsson	Industrivärden (Gullfiber's owner)
Mr Lindfors	Ombudsman, Swedish Factory Workers' Union
Mr Lundgren	Ombudsman, Swedish Factory Workers' Union
Mr Hellgren	Factory Workers' Union branch official, Katrineholm

Mr Skoog

Factory Workers' Union branch official,  
Katrineholm

Mats Lemne

County governor, Södermanland

*11 September 1973. SPK visits Gullfiber*

Lennart Göranson and Karl-Johan Jargenius from the SPK visit Gullfiber's head office in Billesholm. The reason for the visit is the price freeze on prefabricated timber houses, which was introduced in June 1973. As a result of this price freeze, timber house manufacturers requested that the price of insulation material should not be allowed to rise. The discussion between representatives from Gullfiber and the SPK concerns the company's costs and market situation as well as the prices charged for Gullfiber's products. SPK officials express 'some concern' over the company's prospective price rise of around 10 per cent. In the view of the SPK, the prices of raw materials and other inputs for timber house manufacture should be held more or less unchanged since the prices of timber houses are subject to the price freeze.

*10 January 1974. Gullfiber informs the SPK of price increase*

Gullfiber informs the SPK by letter of a 7 per cent increase in the price of mineral wool that came into operation on 12 December 1973. The letter contains details of the increases in the costs of mineral wool production that occurred during 1973. The largest price increases were recorded for raw materials and energy which had risen by 64 and 38 per cent, respectively. In total, costs had increased by 22 per cent during 1973. Increases in labour costs were not included in this figure. Against this background, Gullfiber considers that a price increase of 7 per cent is 'very modest'. Details are also provided of the increases that had taken place in Gullfiber's principal raw material costs, i.e. oil, phenol, soda, and sand.

*5 February 1974. Gullfiber raises its prices again*

Gullfiber informs Lars Starell at the SPK that the prices of Gullfiber's products are raised that day by 16 per cent. The new price lists and the letter sent by the company to its customers are also sent to the SPK. This increase in prices is, according to Gullfiber, due to the rise in raw material costs brought about by the oil crisis. However, Gullfiber's shipments of insulation material to the manufacturers of timber houses are exempted from these price increases. (For the latter, the same price list was in operation from February 1973 until June 1974.)

### *28 February 1974. SPK requests information on price movements*

Following a telephone conversation held the previous day with Lars Starell, Gullfiber sends a list of the increases in costs that account for the price rise introduced on 5 February. According to the company, costs rose by 27 per cent over the period February 1973 – February 1974. The 7 per cent increase in prices introduced on 12 December 1973 together with the 16 per cent increase of 5 February 1974 gave a total price increase of 24.1 per cent. In Gullfiber's opinion, this does not fully compensate the company for the 27 per cent increase in its costs.

Gullfiber estimates that the postponement of a price increase until 1 July 1974 on insulation material supplied to the manufacturers of timber houses will cost Gullfiber 2.88 million SEK in lost revenues. This postponed price increase is the direct result of the request from the SPK to Gullfiber to maintain an unchanged level of prices due to the price freeze on timber houses (compare with the description for 9 November 1973).

### *8 March 1974. Introduction of a price freeze*

The government introduces a price freeze on a number of goods, including building materials. The prices that prevailed on 7 March shall apply for the duration of the price freeze.

### *13 March 1974. Gullfiber requests exemption from the price freeze*

Gullfiber applies for exemption from the price freeze. The application covers a number of its products, especially those that include the raw material polystyrene cellular plastic. The request for exemption is justified on the grounds of increased raw material costs, particularly on styropor, the basic raw material used in the manufacture of Styrolit (the product name for Gullfiber's plastic insulation material). Gullfiber wants to raise the price of Styrolit by 35 per cent, an increase which does not fully compensate the company for an increase in costs of 39.6 per cent. Moreover, Gullfiber also wishes to raise the price of insulation cork since import prices have increased during the first half of March by 25 per cent.

Gullfiber had originally planned to increase the price of Styrolit on 15 March. New price lists were already ordered from the printers and were to be distributed on 10 March to Gullfiber's customers and sales outlets. This planned price increase was stopped by the price freeze introduced on 8 March. However, prior to the introduction of the price freeze, Gullfiber's competitors (Ulvex, Sundelitt and Rockwool) had managed to raise the prices of equivalent products to Styrolit by approximately the same amount as Gullfiber's planned increase.

During the period 15 March 1974 – 27 March 1974, a number of telephone conversations take place between Gullfiber and SPK concerning the company's request for exemption (13 March) and the interpretation of the regulations dealing with the price freeze.

### *21 March 1974. SPK requests information*

Gullfiber receives a letter from Lars Starell, SPK, requesting further information regarding the company's request to exceed the frozen prices on plastic insulation material. SPK demands relatively detailed information on nine separate points:

- 1 a specification of the products to be covered by Gullfiber's request for price increases
- 2 current net prices
- 3 average price changes during the previous twelve months including the date and size of these changes
- 4 the value and volume of sales for the years 1971, 1972 and 1973 as well as the budgeted figures for 1974
- 5 categories of customers for Gullfiber's products
- 6 type of sales
- 7 detailed figures on the products covered by Gullfiber's application for exemption
- 8 the purchase prices of inputs including photostat copies of invoices etc.
- 9 'a detailed and *concrete* (SPK's emphasis) description of the company's profitability, financial stability, efficiency and rationalization measures with regard to the present situation, the previous three years and anticipated future developments'.

A request is also made for the annual accounts of the previous three years. In addition to this list of nine points, the SPK also sends two pages of instructions, covering eight separate points in relation to the presentation of data.

### *27 March 1974. Gullfiber replies*

In a letter dated 21 March, Einar Eriksson replies to the SPK's request for information. His reply covers all of the nine points raised by the SPK. A number of appendices and verifications are also submitted. Gullfiber emphasizes that the prices of Styrolit have actually been cut since the company started production in 1968. The company's request to raise its prices is entirely motivated by the increase in raw material costs caused by the oil crisis of 1973. Gullfiber also contends that these cost increases cannot be absorbed by means of rationalization:

since our factories already use the most efficient methods of production (continuous production lines), our demand is that each product should provide returns sufficient to cover the costs of manufacture and marketing. These products (i.e. Styrolit products) are currently unprofitable. Profitability cannot be improved other than by means of an increase in our prices.

The manufacture of Styrolit is carried out at our factory in Katrineholm. If profitability cannot be improved, the only alternative remaining would be to close down the factory at Katrineholm.

#### *27 March 1974. Problems of interpretation concerning the price freeze*

As a result of the price freeze introduced on 8 March, a number of problems of interpretation arise concerning existing agreements between Gullfiber and their customers. In a letter to the SPK, Gullfiber asks for information on the length of time during which prices covered by delivery agreements would remain in force.

#### *5 April 1974*

Following a conversation on the phone with Lars Axling (SPK), Einar Eriksson at Gullfiber writes to SPK to ask for instructions on which prices shall be adopted regarding the delivery of materials covered by the price freeze to the timber house manufacturers. SPK replies two weeks later by phone.

#### *19 April 1974*

Einar Eriksson draws up an internal memorandum concerning Gullfiber's application for exemption from the price freeze. The memorandum describes the conversations and contacts between Gullfiber and the SPK as well as Eriksson's own view of the SPK's impending decision. He also notes that as cork has clearly not been made subject to the price freeze, Gullfiber's cork products can be priced in accordance with the company's own requirements.

#### *22 April 1974*

An internal memorandum analyses the SPK's interpretation of the concept 'frozen price'. This memorandum is a summary of a series of telephone conversations with Lars Axling at SPK.

#### *22 April 1974. The management of Gullfiber in discussion with SPK*

Malte Johansson and Bertil Lundell from Gullfiber visit the head office of the SPK in Stockholm in order to discuss the company's request for exemption from the price freeze as well as the supplementary information submitted by the company. A meeting is held with Olof Pontusson, Lars Axling and Lars

Starell. According to the memorandum drawn up by Gullfiber, the meeting is conducted along the following lines:

Pontusson, (SPK) who led the discussion, had at his disposal a special analysis which was not shown to us. He was particularly interested in the growth of the value of sales per ton and commented at the same time on the requested level of our revenue contribution in relation to previous levels. Pontusson considered that these revenue contribution figures had substantially increased. As a result, we felt it necessary to explain our standard approach to pricing and the introduction of new products.... Pontusson also stated that the company did not wish to make a corresponding increase in its prices for Urecell products. We pointed out that the product was still relatively new and that the company adopted a cautious pricing strategy during the various trial periods....

A discussion ensued concerning the level of revenues that the company had requested for the period from January 1974. No explanation was offered as to what could be considered the crucial factors in relation to an increase in our prices. We contended that our requests were highly modest viewed against the background of current developments in Norway and Finland.... The discussion continued to be very arduous. It was explained by Gullfiber that unless a satisfactory rise in prices could be achieved, the company would be forced to investigate appropriate means of cutting back production. It would certainly not be possible to continue with the planned increase in production. In answer to a question, we replied that Styrolit was manufactured at Katrineholm, Älvängen and Frånö. A reduction in employment as well as lay-offs would almost certainly take place at these factories....

Pontusson then made a statement that we had long awaited. He said that the SPK could not agree to the company's request for a 35 per cent price increase but was prepared to accept a possible 10 per cent increase. We stated immediately that a 10 per cent increase in our prices was equivalent to a rejection of our request.... Pontusson stated that the SPK had introduced the principle that a request to raise prices should be primarily assessed in relation to a company's overall profitability. Hence profitable companies would have less opportunity to increase their prices than companies that had less satisfactory rates of return. This would apply even in cases where companies operated in the same industry. This principle was unacceptable to the company. Pontusson refused to provide us with examples of companies or industries that had been dealt with in this manner. He hoped that we would take him at his word.

Following further discussion, we suggested that the meeting should be adjourned until after lunch that day which would allow the SPK an opportunity for further deliberations and a reassessment of their decision. This proposal did not meet with Pontusson's approval. However, he finally agreed to reexamine the material particularly in the light of current developments in Norway and

Finland. Pontusson promised that the SPK would inform the company on the following day regarding the results of their deliberations.

### *23 April 1974. The discussion with the SPK on exemption continues*

On the day following the meeting between the representatives from Gullfiber and the SPK, Lars Axling (SPK) phones Bertil Lundell at Gullfiber. According to the latter's notes, the conversation went as follows:

Axling stated that the SPK had reassessed our request for exemption in the light of the previous day's meeting with Johansson and Lundell. Following their deliberations, the SPK was prepared to accept a 10 per cent increase in the prices specified in the January 1974 list. These price increases would take effect from 23 April 1974.

Following the meeting between the SPK representatives and Johansson and Lundell, Lars Axling had been instructed to prepare a memorandum on this question which had then been presented to the Director General, Åke Englund, on that afternoon. Englund was of the opinion a 10 per cent increase in prices could be considered as acceptable. A similar price increase would also come into effect on the same day for Urecell products.

In reply to a question concerning price increases for KOMBI floor insulation, Mr Axling considered it doubtful whether this product was covered by price controls. It was therefore agreed that this product was not liable to price controls.... An important reason for this special treatment was that cork was excluded from price controls. However, the SPK expressed a wish to be kept informed on future price movements....

At the meeting held on 22 April, the SPK emphasized that Gullfiber was a largely profitable company. Hence, an increase in revenues from the products in question was not considered necessary. In this context, we naturally replied that a fundamental principle of the company's pricing policy was that each product should cover its own costs. If this criterion was not met, there were two alternatives, namely to increase prices and thereby provide satisfactory revenues or to close down production of that particular product. If the SPK were unable to agree to a satisfactory revenue contribution the company would have no alternative but consider closing down production.

Mr Lundell pointed out that our major competitor in the field of Styropor production had a listed price which currently exceeded Gullfiber's by 23 per cent. Mr Axling replied that Ulvex had requested a price increase based on a listed price of, as far as I understood, 4.20–4.30 SEK per kilo. However, SPK would not give their approval to this price increase.

Appeals against decisions made by the SPK could be registered with the Ministry of Commerce. The SPK would submit their comments to which Gullfiber were entitled to reply. The Ministry of Commerce would then decide on the basis of the existing documents (a letter from the SPK has been received today regarding the proposed increases in prices). Axling enquired as to how we viewed the situation. Lundell replied that the company would naturally proceed along the lines discussed at the meeting on 22 April. A decision has already been made that Gullfiber will not accept any new orders. A joint management and employee council meeting had been

arranged in order to discuss this issue. Axling then enquired about the likely effects on employment in the Katrineholm factory. I replied that this was not solely a question of employment in Katrineholm but at many other places as well. Some indication of the total impact on employment of these cut-backs in production would be available from the investigation that was already being carried out by the company. However, the greatest difficulties would be experienced by some of the company's customers in central Norrland whose deliveries would be either reduced or subject to considerable delay.

*23 April 1974. The SPK allows a limited price increase*

The SPK permits Gullfiber to raise their prices by 10 per cent on products containing Styrolit and Urecell.

*29 April 1974. Gullfiber asks the SPK to reconsider its decision*

In a letter to the SPK, Gullfiber points out that the limited price increase of 10 per cent fails to provide the company with a satisfactory contribution to revenues given the company's 'present exceedingly low level of prices'. This statement is supported by price data for Styrolit products in Sweden, Norway and Finland. In Sweden the price per cubic meter is 98 SEK compared to 110 SEK and 150 SEK in Norway and Finland, respectively. In both of these Scandinavian countries, the price of Styrolit has also risen more rapidly than in Sweden. Gullfiber concludes:

On the basis of these new prices, the company will not be able to maintain production at existing levels. Nor is the company in a position to accept new orders. This will naturally have repercussions for employment in our factories at Katrineholm, Älvängen and Kramfors. During Week 19, joint management-employee councils will be informed regarding these matters as well as about proposed lay-offs of workers....

In the same letter, Gullfiber again requests the SPK to reconsider its decision: 'Taking into account the further information submitted by the company, we urge SPK to give prior consideration to the written and verbal requests that we have made regarding an increase in our prices...'. Gullfiber never received a reply to this letter of 29 April.

*13 May 1974. Gullfiber appeals to the government*

Gullfiber appeals to the Ministry of Commerce against the SPK's decision of 23 April. The appeal outlines the contacts that have taken place between the company and the SPK and provides information regarding the costs of production of Styrolit and Urecell. Gullfiber rejects the view held by the SPK that losses on Styrolit products subject to the price freeze should be covered by



revenues from the sales of more profitable products. The price increases allowed by the SPK are inadequate. The company has consequently been compelled to refuse any new orders and to consider closing down production of Styrolit.

Since no further reductions in costs can be achieved – production is already fully automated – the company is now in a position whereby it is compelled to take other measures in order to reduce losses. Consequently, the company is not accepting any further orders for these products at the new prices and are moreover preparing for a cut back in employment, once existing stocks have been run down.

Finally Gullfiber emphasizes that the company's prices are lower than their competitors due partly to the latter having increased their prices prior to the price freeze.

*14 May 1974. Gullfiber contacts the building materials section of the Federation of Swedish Industries*

Gullfiber writes to Hans Risberg of the building materials section of the Federation of Swedish Industries following a telephone conversation on the previous day between Lundell and Risberg. The letter outlines the principles adopted by the SPK and the company's criticism of the SPK's standpoint.

*27 May 1974. The Swedish Factory Workers' Union is notified*

Gullfiber notifies Göte Rossing of the Swedish Factory Workers' Union of the contacts that have taken place between the company and the SPK. Gullfiber sends to the Ministry of Commerce all the documents concerned with the company's request for exemption from the price freeze together with notification of the SPK's decision and the company's appeal against this decision. Attention is also drawn to the fact that Gullfiber has notified the SPK of further increases in raw material prices planned for 1 July and 1 August 1974. The letter concludes with the following words: 'We would be grateful for your assistance in trying to persuade the SPK to reassess their decision. No further orders have been accepted for Styrolit and this will inevitably affect production in the autumn'.

*29 May 1974. The SPK's Director General receives a delegation.*

Åke Englund, Director General of the SPK, receives a delegation made up of representatives from the Federation of Swedish Industries, the Swedish Association of Joinery Factories, the Swedish Federation of Crafts and Medium-Sized Industries, AB Casco, the Association of Swedish Chemical Industries, the Swedish Floor Contractors' Association, AB Wilhelm Becker,

AB Gyproc, Gullfiber AB, the building materials section of the Federation of Swedish Industries, AB Euroc and Sieverts Kabelfabrik AB. According to the report prepared by Gullfiber's representative, Willy Malmros, after the meeting, the discussion was conducted along the following lines:

In my presentation of the Gullfiber case, particular emphasis was placed on the low level of profitability of our cellular plastic products and the subsequent risk of redundancies in the not-too-distant future in both our own company and among our customers. Mr Lindén (AB Becker) emphasised the length of time that the SPK had taken to deal with his company's request for exemption while Mr Linderöth (AB Gyproc) called attention to the particular problems that had confronted Siporex and Gyproc as a result of the price freeze. Mr Sunne (AB Euroc) also placed considerable emphasis on these problems. Moreover he stressed that Euroc had taken particular exception to a statement made by an SPK official in which it was alleged that Euroc would be well able to absorb its increased costs.

Following this introduction, Åke Englund (SPK) replied

that it was important to keep in mind that the purpose of a price freeze was to freeze prices. In other words, exemptions could only be granted in exceptional circumstances. He was well aware of the difficulties that arose as a result of a price freeze. However, companies should remember that price freezes and their concomitant problems are, in principle, of only short duration.

Regarding the guidelines for exemption, the most important criterion was the protection of employment. Great consideration was given to the particular position of individual companies. Consequently, it was feasible that two companies in apparently identical situations could be treated differently. The fact that a company sold a product at a loss was not a sufficient reason for exemption from the price freeze as long as this situation did not result in lay-offs of employees. Englund contended that there was not a single instance – during either the present or past price freezes – of a company actually laying off workers because of a price freeze. In such a situation, the SPK had agreed to exempt companies from a price freeze in order to protect employment. Obviously the SPK does not view our own redundancy notices as something likely to take effect in the near future. Englund also emphasised that the SPK kept the trade unions informed on these matters.

Moreover, only in exceptional cases, according to Englund, had decisions taken by the SPK with regard to requests for exemptions, been subsequently changed by the King-in-Council. In those cases where decisions had been changed, employment problems had emerged during the intervening period.

Several members of the delegation raised the question as to whether it was reasonable that individual companies were compelled to sell their products at a loss. Once again, Englund stressed that loss-making prices did not constitute the 'exceptional circumstances' required for exemption from the price freeze; this firm line adopted by the SPK was, as Englund had previously stated, due to the essentially limited duration of a price freeze. Asked whether this could be interpreted as an indication that the price freeze would not be extended after 20 June, Englund replied that he did not wish to comment on that point since such a decision was the responsibility of politicians.

In view of the general uncertainty surrounding the SPK guidelines for companies

(a matter of some surprise for the Director General who thought that they were much more widely known), Mr Malmros raised the question as to whether the SPK would be prepared in the future to state the reasons for its decisions. This would help to clarify SPK's approach to these issues as well as providing a better basis for any appeals that companies decided to make. Englund replied that this question had not been discussed within the SPK but that he would give it some consideration.

During a short meeting held afterwards, the members of the Federation of Swedish Industries decided that information on the SPK guidelines was the most pressing issue confronting the Federation's members. In the event of an extension of the price freeze, the situation would become untenable for many companies since they would be compelled to choose between continuing to sell at a loss or closing down production of a particular product. This issue should be raised with the Ministry of Commerce as soon as possible. Consequently, the Federation of Swedish Industries have expressed a wish that Ulf Lindén, Ulf Linderöth and Willy Malmros together with several other representatives from the Federation should form a delegation to visit the Ministry of Commerce. No date was arranged for this meeting since Mr Feldt, the Minister of Commerce, was abroad.

### *31 May 1974. Gullfiber notifies Tage Larfors, Member of Parliament*

Gullfiber informs by letter Tage Larfors, Member of Parliament from the town of Katrineholm, of their contacts with the SPK. Copies of the replies, discussions and exchanges of letters between Gullfiber and the SPK together with an account of the delegation's meeting with the SPK's Director General are included in the letter.

### *11 June 1974. A delegation meets with the Ministry of Commerce*

A delegation consisting of seven representatives, five from the Federation of Swedish Industries, one from AB Gyproc and Willy Malmros, Gullfiber, meets Bengt Dennis, Under-Secretary of State at the Ministry of Commerce. Following a brief survey of the background to the meeting, Malmros summarizes the discussion in the following terms:

Körner (Federation of Swedish Industries) stated that industry had been poorly informed about the guidelines to be used by the SPK in their appraisal of requests for exemption. Körner stressed that industry had wanted to see a rapid withdrawal of the price freeze but this measure had instead been extended to December 20th. Bengt Dennis replied that Parliament had given the government powers to extend the price freeze until 20 December. However, it was at least feasible that the government could abolish the price freeze prior to that date. He admitted that there had been 'some shortcomings' in the provision of adequate information to companies about the guidelines to be adopted for the implementation of the price freeze. He assured the delegation that these procedures regarding information to companies would be revised....

Bengt Dennis also stated that the employment criterion was not the sole grounds on which exemption from the price freeze could be granted. We pointed out to Mr

Dennis that this was a substantially more flexible view than had been adopted by Åke Englund, the SPK's Director General during our meeting on 29 May 1974. Mr Dennis seemed to be slightly perplexed by this statement pointing out that the Ministry of Commerce and the SPK applied the same regulations. We emphasised that the SPK had categorically stated that employment issues were more or less the sole grounds on which exemption from the price freeze could be granted. This line of argument seemed to be somewhat disconcerting for Mr Dennis and it did not seem worthwhile continuing our discussion along these lines....

Subsequently, I gave an account of the difficulties that had confronted Gullfiber as a result of the price freeze. I emphasised that the SPK's insistence on using the employment criterion as the sole ground for exemption from the price freeze could lead to labour market unrest, forcing companies to introduce lay-offs in order to gain an exemption from the price freeze. This would naturally cause concern among the company's employees. These issues ought to be capable of a more flexible solution. The extension of the price freeze has also introduced further distortions into Gullfiber's markets since the company's major competitor has been able to raise its prices. This suggested that the guidelines ought to be revised when a price freeze is extended.

Bengt Dennis stressed that a price freeze was, in principle, a short-term measure. Guidelines for companies would be revised if a price freeze continued in operation for some considerable time. However, Mr Dennis was not able to provide any definition of 'a long-term price freeze'.

Finally both sides agreed that the Ministry of Commerce and the Federation of Swedish Industries should maintain a continuing dialogue on these issues....

#### *19 June 1974. Gullfiber writes to the Ministry of Commerce*

Gullfiber writes to the Ministry of Commerce regarding the SPK's view of Gullfiber's request to raise the prices of cellular plastic products above the levels permitted by the price freeze. The letter concludes with the following words: 'We therefore submit that our original requested increase of 35 per cent should be granted. This would mean a further 10 per cent rise in comparison with SPK's decision of 23 April 1974 and their recommendation of 11 June 1974'.

#### *28 June 1974. The Ministry of Commerce agrees to price increase*

The Ministry of Commerce gives Gullfiber permission to raise its prices by 25 per cent above the levels stipulated by the price freeze.

#### *15 August 1974. Gullfiber asks for a new exemption*

Gullfiber submits a request to the SPK for an increase in the price of Styrolit products by 4.5 per cent on the grounds that the price of the raw material used in the production of Styrolit had been raised by 0.30 SEK per kilo to 4.10 SEK per kilo on 1 August 1974.

### *11 September 1974. The SPK rejects Gullfiber's application*

The SPK rejects Gullfiber's application of 15 August. No explanation is offered for the rejection of the company's request for exemption from the price freeze.

On the same day, a discussion is held within Gullfiber regarding company strategy in the event of a withdrawal of the price freeze on building materials on 20 December 1974. The meeting draws attention to the uncertainty surrounding price control policy after this date. There is general agreement that 'the present strict guidelines' would cease to apply since this would lead to losses among industrial companies. It is estimated that the mineral wool industry has been unable to compensate itself for 25 per cent of its recent rise in costs.

Contacts made through the Building Materials Section of the Federation of Swedish Industries indicate that Rockwool, Gullfiber's major competitor in the mineral wool market, needs to raise its prices by approximately 30 per cent in order to 'provide an adequate yield on invested capital' and to promote industrial expansion. However, Gullfiber's management considers that such a 'shock increase' would be politically inadvisable. Instead, a smaller price increase of 15–20 per cent should be introduced once the price freeze is withdrawn. Later in 1975 when the cost situation was 'clearer' a further increase could be introduced in order to cover the remaining non-compensated increases in costs. It was essential to maintain as low a price level as possible in order to deter potential new competitors. A recommendation is made for a carefully planned series of price increases to be put into effect once the price freeze ceases to operate: 'Gullfiber should seek to introduce a series of phased price increases in order to restore profitability to its previous level, taking into account the long-term repercussions of these price increases on the company's competitive position, political standing and its customer's interests'.

### *18 September 1974. Gullfiber appeals to the Ministry of Commerce*

Gullfiber appeals to the Ministry of Commerce against the decision of the SPK to reject its request for exemption from the price freeze. The principal grounds for the company's appeal are the substantial increases that have taken place in the cost of imported Styropor.

### *17 October 1974. The SPK contacts Gullfiber*

The SPK phones Gullfiber in order to enquire about the prices that the company would charge once the price freeze is withdrawn. As a result of this conversation, arrangements are made for two representatives from Gullfiber to visit the SPK in Stockholm in order to discuss price issues.

22 October 1974. Gullfiber's management visits the SPK

A meeting is held at the SPK head office in Stockholm attended by Bertil Lundell and Göte Boman from Gullfiber and Curt Ohlsson and Lars Axling from the SPK. The purpose of the meeting is to discuss price movements of mineral wool. According to the notes of the meeting kept by Göte Boman, the following discussion ensued:

*C. Ohlsson (SPK):* Our contacts with raw material suppliers indicate that Gullfiber has not experienced any major increases in its costs. For example, the price of phenol has fallen, the price of soda is around 500 SEK, the price of rasorit is somewhat uncertain....

*B. Lundell (Gullfiber):* The price of soda is now above 500 SEK. The price of phenol has certainly fallen but Gullfiber has to pay well above average prices for additional quantities. This is also true in the case of soda. It is now impossible to get hold of rasorit – it has been replaced by kolomarit.

*C. Ohlsson (SPK):* Would it be true to say that Gullfiber is working at full capacity at present?

*B. Lundell (Gullfiber):* Yes, we are working flat out at present due largely to the current temporarily high levels of exports. However, we do not anticipate any significant exports in the future notwithstanding the higher levels of prices prevailing in West Germany, France, England etc. The main problem here is that mineral wool is a highly sensitive product that does not 'travel well'....

*C. Ohlsson (SPK):* Nevertheless, Gullfiber has succeeded in increasing its market share at the expense of Rockwool. Isn't that the case?

*B. Lundell (Gullfiber):* Yes, that's correct. The major factor here has been the high level of activity in the construction industry. Activity will probably now shift towards manufacturing. At the same time, Gullfiber needs to generate capital in order to expand its production of mineral wool products.

*C. Ohlsson (SPK):* In formal terms, the Price Control Act will be extended after 20 December. This means that the government is still able to introduce selective price freezes after this date. Nevertheless, the SPK is exploring the possibilities of avoiding further price freezes.

What would happen if the price freeze was withdrawn altogether? *Would Gullfiber be prepared to hold its prices until 31 March if the price freeze was withdrawn?* (Gullfiber's italics)

*B. Lundell (Gullfiber):* If Gullfiber was able to obtain assurances regarding a freeze on wages and raw material prices, this would be a fairly simple matter. It is a difficult situation to assess. A question of such importance would naturally have to be examined by our Board of Management. Our Chairman is ill at present and we would need some time before coming to a decision.

*C. Ohlsson (SPK):* The SPK would appreciate it if Gullfiber could in due time provide at least a non-binding assurance regarding future developments.

*After the meeting, Mr Axling (SPK) informed us that decision-making within the SPK was strongly centralised (italics by Gullfiber).* The final decision was always made by the Director General, Åke Englund. Pressure from the Confederation of Trade Unions (LO) and the Commercial Employees Union was currently being exerted in favour of a withdrawal of the price freeze prior to the start of the central wage negotiations.

The question of Styrolit was raised from time to time during the meeting. Mr Lundell explained the company's predicament; each delivery of the product was carried out at a loss to the company. Indeed the company had considered closing down operations and selling off its machinery. The company did not actually own the plant at Katrineholm which made this operation fairly simple. Mr Ohlsson had not dealt with Gullfiber's appeal since he considered that 4.5 per cent was a relatively insignificant amount. In his view, Styrolit should be dealt with in the same manner as mineral wool. Lundell did not agree with this view. He stated that he would get in touch with Ohlsson in a week's time regarding a decision on this matter.

### *13 November 1974. SPK makes an offer*

In a telephone call to Mr Lundell, Mr Ohlsson (SPK) enquired whether Gullfiber would be prepared to freeze its prices during the first quarter of 1975 in exchange for a withdrawal of the general price freeze. In a letter to Curt Ohlsson (SPK), Bertil Lundell refers to the discussion held at SPK on 22 October and to the telephone call of that day. Mr Lundell refers to SPK's offer to:

agree to a withdrawal of the price freeze on our products in exchange for a voluntary commitment to maintain prices at their existing levels until the first quarter of 1975. As was mentioned at the time, this proposal would have to be discussed at a plenary session of our Board of Management. The earliest date for such a meeting would be at the end of this month when our Chairman will hopefully have returned to work after his illness.

At the same time, we raised the question of our appeal of 18 September 1974 to the King-in-Council, regarding your decision of 11 September 1974 not to agree to an increase in the price of Styrolit products. We understood that our appeal has remained with the SPK for some considerable time. No explanation has been provided for this delay other than a slight hint that it might be connected with your above proposal. We find this relationship difficult to understand and would consequently be grateful if you could give this matter your earliest attention. The contents of our appeal to the King-in-Council must surely be considerably easier to deal with than the question that you have presented to us.

The purpose of this resume is to confirm the subject-matter of our conversation in order to avoid the possibility of any misunderstanding.

### *14 November 1974. Gullfiber requests a decision on their appeal*

Gullfiber requests a decision on the company's appeal of 18 September

regarding an increase in the price of Styrolit above the levels permitted under the price freeze.

*28 November 1974. Gullfiber's management discusses future action*

Gullfiber's management discusses which line of action should be adopted by the company regarding the price freeze and its possible cessation on 20 December. The question has been discussed within the building materials section of the Federation of Swedish Industries by Bertil Lundell and representatives from, inter alia, Gustavsberg, Interoc, Euroc and Rockwool. Two alternatives have been considered. First, Gullfiber could enter into an agreement with the SPK, that is accept a voluntary commitment to hold prices until 31 March 1975. This commitment would be preceded by an increase in prices of 8 per cent. The other alternative is that Gullfiber does not come to any agreement with the SPK but instead awaits the outcome of events. Bertil Lundell analyses this latter proposal in the following manner:

It was discussed in Stockholm that the SPK is now endeavouring to obtain 'voluntary agreements' from as many manufacturers as possible. For the others there are two possible outcomes: that the price freeze remains in force or that it is also withdrawn for these companies. The majority seemed to be of the opinion that the price freeze would be ended on 10 December. There has been considerable speculation that compulsory notification and a right to inspection by the SPK would be used as quid pro quo for the removal of the price freeze. As previously stated, it is probably the case that LO (the central labour union organization) would not wish to have price controls in force during wage negotiations in case they hampered discussions. Therefore it is also quite feasible that the SPK withdraws the price freeze but subjects price increases to bureaucratic delay which would lead to the same net effect as a voluntary agreement.

Mr Lundell summarizes his discussion in the following recommendation: 'I propose that I get in contact with the SPK and inform them that, following discussions by the Board, we are prepared to voluntarily hold prices at the new levels that will prevail after the 8 per cent increase.'

*4 December 1974. Gullfiber makes an offer to the SPK*

Bertil Lundell writes to Curt Ohlsson at SPK regarding SPK's 'proposal for a voluntary commitment from our side to freeze prices during the first quarter of 1975 in exchange for a limited increase in the prices of products that are at present subject to the statutory price freeze.'

Mr Lundell begins by pointing out that when the price freeze was introduced on 7 March 1974, it was stated that it would be a short-term measure. The price freeze has now been in force for such a long time that it seriously threatens the company's viability. Profitability has been reduced 'very substantially' due to



the company's inability to compensate itself for the increases in the prices of raw materials which are largely imported.

At the meeting held at the SPK on 22 October, Mr Ohlsson (SPK) contended that the company's increased costs could be offset by greater capacity utilization. Mr Lundell states that it will not be possible to increase production since capacity has been fully utilized during recent years. It is rather the need to invest in new capacity that poses problems for the company.

Unless Gullfiber receives some compensation for the increases that have taken place in its raw material costs, it is hardly conceivable that the company would be prepared to make further investments when profitability continues to decline which has been the case for most of this year. In the present situation, the authorities seem to wish to create opportunities for a reduction of domestic and industrial heating costs. One established method that has been recommended by the authorities is that of improved heating insulation. However, this presupposes that the economic resources are available. It is in this context that the company could make an important contribution to the country's economy. It is quite possible to import insulation materials from abroad but this can only be done at much higher prices. For example, the present price level on the continent is 40–60 per cent above that in Sweden, excluding transport costs. An extension of the price freeze after 20 December 1974 will have very serious repercussions on our company's profitability....

Against this background, Gullfiber states that it is 'prepared to meet the SPK request' to impose a voluntary price freeze until 31 March 1975 provided that the company is able to introduce 'a modest increase in the prices of products that are at present subject to the price freeze'. Gullfiber proposes that these price increases, which would still not provide full compensation for the increase in costs, be introduced as follows:

- a) The factory prices of building insulation materials would be raised by 12 per cent. An increase of 16 per cent would apply to the corresponding prices for technical insulation materials which are principally supplied to industry.
- b) The mark-up that is used to calculate the wholesale price list is reduced by 5 per cent. It is this price list that applies to consumer purchases of building insulation materials. Approximately 40 per cent of the total volume of insulation materials is sold according to this warehouse price list.

#### *9 December 1974. SPK rejects Gullfiber's offer*

Curt Ohlsson (SPK) phones Einar Eriksson (Gullfiber) regarding the company's offer of 4 December. He informs Eriksson that the company's proposed price increases are unacceptable to the SPK. The conversation largely concentrates on the relative merits of Gullfiber's and the SPK's calculations, in

particular concerning the price for soda. According to the notes made by Eriksson, the conversation continued along the following lines:

I informed him of the current price for soda and that at the time of our last order, we had to pay almost double the price for part of the purchased quantity since our supplier had run out of soda due to the general scarcity. It turned out that this increase of 210 SEK per ton had not been included in their calculations.

In Curt Ohlsson's view, it was essential for the SPK to reverse the tendency for industrial companies to raise prices in anticipation of wage cost increases. In order to counter this criticism, I provided him with a breakdown of the increases that had taken place in our variable costs between February and October....

However, the main purpose of Curt Ohlsson's telephone call was to inform us that the SPK had rejected our requested 12 per cent increase in prices. In reply, I asked him what increase would be acceptable to the SPK. He was unable to answer this question since he did not have the necessary figures at his disposal. I offered to send him a detailed account of our increased costs along with the necessary price data to verify these increases. He accepted this offer. The conversation did not result in any specific agreement.

#### *18 December 1974. The price freeze on building materials is prolonged*

The price freeze is abolished for a number of products or replaced by mandatory prior notification of price increases. However, building materials including mineral wool continue to be subject to a price freeze. According to the press release from the Ministry of Commerce, the price freeze is retained for those products where 'one or a limited number of companies dominate the market and where a majority of these companies have already announced that substantial price increases would be introduced following the withdrawal of the price freeze.'

#### *20 December 1974. Gullfiber applies for exemption to the SPK*

Gullfiber applies to the SPK for exemption from the price freeze. The company points out that it has previously proposed a voluntary freeze on prices for the first three months of 1975. However, the SPK informed us by telephone on 9 December that they were unable to accept this proposal. 'No realistic alternative has subsequently been proposed.'

Gullfiber's request for exemption from the price freeze is supported by four appendices containing documents relating to the company's costs since February 1974 including photocopies of suppliers' invoices. The prices of 22 raw materials used in the manufacture of mineral wool are specified according to their invoice dates for February and November 1974. The increase in costs amounts to almost 46 million SEK which is equivalent to more than 20 per cent of the total sales value. Accordingly, Gullfiber wishes to raise the price of building insulation materials by 20 per cent and technical and other insulation

materials by 26 per cent. This is equivalent to an average increase of 21.2 per cent on the company's product mix. The request for exemption is concluded with the following argument:

On previous occasions, we have informally drawn your attention to the considerable difficulties that have arisen for our company as a result of the almost one year long freeze on prices. Through previous contacts, it has been established that the price freeze would be applied in a consistent manner, over a relatively short period of time. However, the company's profitability has continued to decline and it has become necessary for us to obtain compensation for the increases in our costs. In view of this serious decline in our profitability, the company has been compelled to postpone part of its investment programme. Investment has been limited to the completion of existing projects. In spite of favourable market opportunities, the company has felt itself unable to undertake any investment in new capacity. ... Gullfiber would greatly appreciate it if the SPK could examine this matter, which is of the utmost importance to the company, at its earliest convenience. Accordingly we are prepared to meet you at short notice for discussions concerning a detailed evaluation of the breakdown in costs that we have submitted in support of our request for exemption. We are willing to provide you with a verbal presentation of the material and, if required, supply further data which you may consider essential for a rapid and proper treatment of this matter.

*9 January 1975. The government rejects Gullfiber's appeal*

The government rejects Gullfiber's appeal against the decision taken by the SPK on 11 September 1974 to reject Gullfiber's request to exceed the statutorily frozen prices for Styrolit.

*January 1975. Gullfiber provides SPK with additional material in support of its request for exemption*

Einar Eriksson (Gullfiber) phones Lars Axling (SPK) on 8 January. Axling states that he is in the process of drawing up a series of memoranda on the case of Gullfiber with Curt Ohlsson. He agrees to phone back on 13 January for further discussions concerning Gullfiber's profitability.

Following a number of telephone conversations with Axling during January, Eriksson submits further material to the SPK in support of the company's request for exemption. This material provides data on the company's financial position in the form of reports on company liquidity, planned investment projects, estimated mineral wool production, depreciation, interest and amortization payments for 1974-1975 and 1975-1976, cost of binding agents per ton in February and November 1974, and a breakdown of the price increases of raw material into various subgroups. Eriksson sends a total of approximately nine pages of supplementary data on Gullfiber's financial situation.

*20 January 1975. Gullfiber's senior management and trade union representatives meet the SPK*

Malte Johansson and Bertil Lundell from Gullfiber together with Göte Rossing from the Swedish Factory Workers' Union attend a meeting at SPK in Stockholm with Curt Ohlsson, Olof Pontusson and Lars Axling representing SPK. In this instance, the company has sent its senior management to discuss its exemption request with the SPK. According to the report drawn up by Bertil Lundell, the discussion is conducted along the following lines:

Following a general introduction by Malte Johansson and Curt Ohlsson, both sides presented their views on Gullfiber's request to increase the prices of mineral wool products. Curt Ohlsson explained that the general principle adopted by the SPK in these matters was that the SPK should not agree to requests from companies for higher prices that are designed to compensate them for increases in costs that they are themselves able to absorb. At the same time, the assessment of a company's profitability should also take account of possible profits on stocks....

Malte Johansson explained that Gullfiber did not carry a high level of stocks. In fact, the company led 'a hand to mouth existence' since the difficulties encountered in obtaining raw materials prevented the accumulation of stocks. Similarly there was little stockpiling of finished goods due to the bulky nature of these products. As Gullfiber has stated previously, the company has had to absorb, throughout the last year, the entire increased cost of its raw materials with a resultant deterioration in the company's overall liquidity. This has eliminated any possibility of undertaking new investments. Indeed the principal question confronting the company is how it can complete its planned programme of investment amounting to 50 million SEK which is already in progress. In view of these difficulties, the most pressing question for the company is how to avoid a desperate situation particularly since the company has also to pay an investment tax retroactively (although half of this payment has been postponed until the end of June).

Göte Rossing stated that his reason for attending the meeting was that the Factory Workers' Union had a direct interest in the maintenance of a level of company profitability sufficient to pay competitive wages to his union's members. The Factory Workers' Union has an excellent relationship with Gullfiber and are completely satisfied on all issues concerned with work environment, worker participation, consultation etc.

However, on the subject of wages, the union is concerned that at present Gullfiber is approximately 1 SEK per hour below the average wage rate. In view of the type of work involved – continuous three shift work in a noisy environment – company wage levels should rather be above this average rate. A new wage package has been worked out between the union and Gullfiber, including a new wage system. However the introduction of this new wage agreement will inevitably cost the company more money.

These additional wage costs have not been included in the company's request for higher prices. However, Gullfiber is in favour of this new wage agreement and would wish to have the right subsequently to seek compensation, in the form of

higher prices, for these additional wage costs including the increase in costs that will result from this year's annual wage negotiations.

According to the SPK, the company had had a highly satisfactory level of profits during recent years – 'rather on the high side'. The company had certainly experienced higher costs during the present financial year but 'profits would nevertheless appear to be satisfactory'. The SPK was told that the company's net profit figures included 9 million SEK in net profit from Gint and Bilsom whose products, principally for export, had not been subject to the price freeze.

The SPK explained that they had received all the documentation that they required. No further material would be needed over and above the additional information that they had already received by telephone and during the meeting.

In the SPK's view, it would have been advantageous for Gullfiber to have entered last autumn into a voluntary agreement on price restraint accompanied by a lower level of price compensation. This question was raised at various stages of the meeting and gave rise to somewhat contrasting views on the way in which this matter had been handled. However, it emerged clearly that Gullfiber had put forward a proposal in this direction but that the SPK had not taken up this proposal on the grounds that its requested price increase was too high.

The SPK stated that they had found the meeting extremely worthwhile since it had given them a good insight into the information that the company had previously presented to the SPK. At the same time, it provided the SPK with an opportunity to evaluate the company's written evidence in a broader perspective. A memorandum summarizing this written material had now been prepared within the SPK. However, this memorandum had been completed only a short time prior to the meeting and would require further analysis before the SPK could come to any decision regarding our request for exemption. The company would be informed on this matter within two or three days.

### *23 January 1975. New contacts between Gullfiber and the SPK*

The SPK informs Gullfiber that they have requested additional information from Rockwool and that both companies' exemption requests would be dealt with at the same time.

### *24 January 1975*

Gullfiber phones the SPK. Curt Ohlsson (SPK) informs Gullfiber that he has just received all the papers and that he will contact Gullfiber later once he has discussed the matter with his colleagues and has reported the Gullfiber case to the Director General.

### *29 January 1975*

Einar Eriksson from Gullfiber visits the SPK in Stockholm in order to hand over to Lars Axling further information relating to Styrolit. At the SPK, Einar Eriksson happens by chance to meet a representative from Rockwool who is also visiting the SPK for consultations.

On the same day, Gullfiber makes a new request to raise the price of Styrolit products.

*31 January 1975*

Olof Pontusson phones from the SPK and asks to visit Gullfiber's head office in Billesholm in order to carry out certain profitability studies and also to gather some additional data. Gullfiber's senior management make a rapid change in their arrangements and agree to a meeting on 4 February.

*4 February 1975. SPK visits Gullfiber*

Olof Pontusson and Stefan Saläng (SPK) attend a meeting at Gullfiber's head office in Billesholm. Gullfiber is represented by the company's Managing and Deputy Managing Directors Malte Johansson and Bertil Lundell together with Einar Eriksson and Knut Aronsson. Mr Johansson expresses his disappointment that Gullfiber has still not received the promised decision from the SPK regarding the company's exemption requests. In Mr Johansson's opinion, the SPK has deliberately delayed a decision on these matters. In reply, Mr Pontusson points out that it is not customary for the SPK to visit companies. He agrees that Curt Ohlsson at the SPK had stated that the SPK had received all the documentation that they required. However, he had been unable to carry out an examination of the material. When he did so, it was found that additional information was required. A further examination was carried out into Gullfiber's profitability together with an analysis of the company's investment programme, liquidity situation, market developments, and cost trends. Additional information was also provided on the contributions made by Bilsom and Gint to Gullfiber's profits and the distribution of fixed costs and depreciation between different branches of company operations. New tables were compiled showing the profitability of the Gullfiber group.

Mr Pontusson states that he felt that they have received all the necessary information. Any additional information could perhaps be obtained by telephone on Thursday 6 February. He is unable to say exactly when the company will receive word on its exemption request but that it will definitely be within a month. Later on in the afternoon, he states that it will be at the end of next week or at the latest, the week after next.

Mr Johansson of Gullfiber informs the meeting that after consulting the Chairman of the Board, an extra joint management-employee council meeting has been arranged in Katrineholm and Älvängen for 5 February. Both trade union and employee representatives together with municipal government and other local interests have been informed of the notices of lay-offs. The formation of consultative groups is also on the agenda for discussion. Mr Pontusson phones the Director General, Åke Englund at the SPK in Stockholm

in order to arrange for the latter to have a word with Mr Johansson by phone on 5 February, once he has arrived in Katrineholm.

The suggestion is made during the meeting by the SPK representatives that Gullfiber ought to consider selling some of its assets in order to improve the company's liquidity.

*4 February 1975. Gullfiber contacts politicians and trade union representatives*

Gullfiber's managing director holds discussions with Einar Ågren of the Factory Workers' Union and Tage Larfors, Member of Parliament for Katrineholm, concerning the background to the extra joint management-employee council meetings in Katrineholm and Älvängen. Per Engvall, a leading local politician from Katrineholm, is also kept informed via his secretary.

*5 February 1975. Joint management-employee council meeting*

Malte Johansson phones Einar Ågren and the Director General of the SPK with reference to Gullfiber's production costs at Katrineholm and Älvängen. Joint consultative groups have been set up in both plants. In Katrineholm, the consultative group also contains a representative from the head office in Billesholm as well as Per Engvall in his capacity as 'landlord' for the factory space used for the manufacture of cellular plastic.

*6 February 1975. Gullfiber informs trade union representatives and the SPK*

Gullfiber's Managing Director informs Einar Ågren and Per Engvall that consultative groups have been set up following the meeting of the joint management-employee council. This information is also communicated to Åke Englund at the SPK. As a result of this latter conversation, a visit to the SPK head office in Stockholm by representatives of Gullfiber's senior management is arranged for 12 February.

*7 February 1975. SPK contacts Gullfiber*

Lars Axling (SPK) phones Einar Eriksson at Gullfiber. He requests certain information regarding the selling prices of mineral wool in different countries – information that he has previously received but mislaid. It is agreed to send him a new copy of this price data.

Axling mentions that 'events were moving at full speed at the SPK' following the critical 'comments' of Malte Johansson. A Member of Parliament had clearly got in touch with the Minister of Commerce 'who had then phoned the SPK and enquired what was going on'.

*10 February 1975. Joint management–employee council meeting in Billesholm*

Malte Johansson (Gullfiber) informs Tage Larfors, Member of Parliament, of current developments. An extra joint management–employee council meeting is held in Billesholm. A consultative group is appointed to carry out an on-the-spot analysis of company profitability, department by department. An extra joint management–employee council meeting will also be held at Söråker where production conditions are similar to those of Billesholm.

*11 February 1975. Joint management–employee council meeting in Söråker*

An extra joint management–employee council meeting is held at Söråker in order to discuss current levels of profitability in Gullfiber's various lines of production. Folke Pehrsson, representative of Industrivärden, Gullfiber's owner, visits Gullfiber in order to examine the current problems of profitability and liquidity affecting the company.

*12 February 1975. Gullfiber's senior management visits the SPK. New negotiations and further offers*

Gullfiber's Managing and Deputy Managing Directors, Malte Johansson and Bertil Lundell, visit the SPK in order to be informed of SPK's decision regarding Gullfiber's earlier requests for exemption from the price freeze. Englund, Hallman and Ohlsson represent the SPK at the meeting. According to Gullfiber's minutes of the meeting, the discussion is both lengthy and lively. The meeting starts with a short presentation by Åke Englund of SPK's principal functions.

Subsequently, Åke Englund took up the contacts that had taken place between the SPK and Gullfiber. He explained that the SPK had taken the initiative on 22 October 1974 to arrange a meeting with Gullfiber in order to investigate the possibilities for abolishing the price freeze. At that meeting, the SPK suggested verbally that Gullfiber should voluntarily agree to a period of price restraint until 1 July 1975 in exchange for the abolition of the price freeze and an agreement that allowed Gullfiber to increase the prices of cellular plastic products by the requested 4.5 per cent. At the time, Bertil Lundell stated on behalf of Gullfiber that this was a far-reaching issue which would naturally have to be examined in detail by the company and then presented to the board for their consideration. However, it had been made clear to the gentlemen from the SPK that owing to the illness of the company's Managing Director, it would not be possible for Gullfiber to arrive at a decision before the second half of November. The SPK was also reminded during the meeting that the 4.5 per cent increase in the price of cellular plastic had only come about when the meeting had finished and the participants were preparing to leave. Consequently this proposal from the SPK was not considered as a serious offer. ... Gullfiber later



made a counter-offer on 4 December 1974, regarding a voluntary commitment to price restraint. This proposal was never dealt with by the SPK....

Gullfiber presented the following points:

- Gullfiber had previously been highly restrained regarding price increases. For the most part, the company had succeeded in absorbing a large part of these increases in costs by means of rationalisation. However, these opportunities have now been entirely exhausted. Amongst experts, Gullfiber is considered to have the most highly advanced, computerised plant in the world.
- All of the company's raw materials for the production of mineral wool fibre have to be imported. Even sand from the Swedish coast is dredged using a Danish sand-pump.
- Each line of production within Gullfiber must naturally be able to justify its existence in economic terms.
- In the present situation, all planned investment by the company has been stopped including investment projects in progress provided that they have not exceeded more than 25 per cent completion.
- No new investments can be started as long as this freeze on investment remains in force and the present unfavourable situation continues to have an adverse effect on the company.
- As Managing Director, Malte Johansson considers that he is under pressure from three different directions. First, consumers need to improve insulation standards in order to lower heating and living costs. Second, Gullfiber's board demand a satisfactory return on the company's investments and the maintenance of profitability. Third, the company's employees also apply pressure, not only in the form of secure employment but also in terms of improved working conditions, better work environment and higher wages. Gullfiber has actually fallen behind average wage levels in the industry.
- The continuous increases in raw material prices and in wage costs have placed the company in a dire situation.

Gullfiber has presented a detailed documentation of all of these additional costs to the SPK. However, the only response that the company has received has taken the form of demands for further information. The SPK has failed to fulfil its promise that the company would receive a decision on this matter. Following our last meeting on 20 January, we were told that a decision would be reached in a couple of days.

The SPK apologised that they had not kept the company informed regarding the delay but that it had proved necessary to obtain some further data. Åke Englund considered that, to judge by the correspondence, contacts between Gullfiber and the SPK had been relatively limited. However, we pointed out that frequent telephone communications had taken place. Moreover Gullfiber had drawn up a five page memorandum covering the discussions that had been conducted between the SPK and the company. Gullfiber emphasised that each item in this memorandum only accounted for a few lines.

In relation to Gullfiber's request to raise the price of cellular plastic, Åke Englund stated that, following consultations with the Labour Market Board, the trade unions and the county authorities, it appeared that only a limited number of employees were

involved. He did not foresee any difficulty in finding alternative local employment in the event of lay-offs. For this reason, the employment aspects of the company's request, which are otherwise of major importance, do not have to be taken into consideration. Mr Johansson stressed that the continuous increases in raw material prices had drastically affected Gullfiber's situation. The company had always sought to maintain an open attitude and provide all of the information that the SPK required. However, the visit to Billesholm on 4 February 75 was not conducted in the constructive spirit to which the company was accustomed. It was only after Gullfiber had put pressure on their visitors that they succeeded in obtaining a table that provided the company with an overall view of the SPK's appraisal of profitability. Nor do questions such as 'Isn't there anything that could be sold off?' or 'Can't efficiency be increased?', contribute to a favourable working atmosphere.

Åke Englund then returned to Gullfiber's exemption request, pointing out that the company's profitability was satisfactory. Indeed during the period 1971-1974, it had been very good. With reference to our offer of 4 December 1974, Åke Englund stated that the SPK was now willing to accept a 7-8 per cent increase in the price of both cellular plastic and mineral wool on the condition that the company maintained these prices for the rest of 1975. Gullfiber subsequently declared that this offer could not be accepted on any basis. Mr Johansson then put forward Gullfiber's counter-proposal:

1. Prices would be immediately increased by 6 per cent. Prices would then remain unchanged until April 1st when it was assumed that the price freeze would be abolished.
2. On April 1st, the price of building insulation material would be raised by a further 14 per cent and the price of technical insulation material by 20 per cent: today's discussions could be considered as authorized notification.
3. Compensation for wage increases that result from the current negotiations would be obtained in the form of higher prices at one month's notice.

As further evidence in support of Gullfiber's request of 20 December 1974, the company informed the SPK that the budgeted figures had been recalculated on the basis of current prices for raw materials and equipment. This calculation which was given to Åke Englund showed that Gullfiber's operations were presently being run at a loss. Bilson and Gint had been excluded from this calculation since their production had no bearing on the Swedish market for building insulation material. Mr Englund admitted that this new data that they had now received put the company's financial position in a completely different light. These new facts would obviously have to be evaluated by the SPK. Englund then said that he was prepared to reassess SPK's proposal in the light of this new material and would reach a decision by Monday 17 February. During the interim period, the SPK could contact Einar Eriksson if any further information was required.

### *12 February 1975. Gullfiber meets with the National Housing Board*

Following the meeting at the SPK, Mr Johansson, in his capacity as Chairman of Swedisol, visits Mr Sännås at the National Housing Board accompanied by

Sture Christenson, Head of Marketing at Rockwool. The purpose of this visit is to inform the National Housing Board of the probable quantities of insulation material that the mineral wool industry would be able to supply in relation to the loans and grants that are currently available for the installation of additional insulation in existing buildings.

*17 February 1975. The consultative group meets. New offer from the SPK*

A meeting is held of the consultative group. Malte Johansson informs the meeting of the discussion held with the SPK's Director General on 12 February 1975.

During our visit, Mr Englund proposed that Gullfiber would be allowed to raise its prices by 7–8 per cent above the present 'frozen' levels provided that these prices then remained unchanged for the rest of the year. This price increase would also have to include the expected increases in our wage costs. This offer had not been acceptable to Mr Johansson who then put forward a counter-proposal consisting of an immediate 6 per cent increase in prices to be followed by further increases of 14 and 20 per cent respectively in the prices of building and technical insulation materials. In addition, he requested that the company would subsequently be able to take account of the additional wage costs that would result from this year's annual wage round. This counter-proposal was not acceptable to Åke Englund. The latter promised to get in touch with Mr Johansson on Monday 7 February. As Englund had not phoned by 11.00 am, Johansson phoned the SPK and spoke to him. A new offer was then put forward by the SPK whereby the company would be allowed immediately to raise its prices by 7 per cent followed by a further 5 per cent on 1 July. Prices would then be held unchanged until the end of the year. Malte Johansson said in reply that he was not able to agree to this proposal and that the company wished to stick to the offer that they put forward during their visit to the SPK on 12 February. In Mr Englund's view, the company still obtained a satisfactory return on its capital in spite of the current price situation. Johansson then offered to come to Stockholm to visit the Ministry of Commerce together with Åke Englund for a joint presentation of their respective views. However Englund did not show any interest in this proposal. Johansson informed the meeting that the consultative groups in Katrineholm and Alvängen would meet on Wednesday 19 February to give notice of the plant closures.

*19 February 1975. The SPK grants exemption*

The SPK informs Gullfiber that the company has been granted exemption from the price freeze and will be permitted to increase the price of its fibre products by 7 per cent in the case of building insulation materials and by 12 per cent for other insulation products. At the same time, Rockwool was allowed to raise its prices for equivalent products by 9 and 15 per cent respectively. Competition between the two companies prevented Rockwool from increasing its prices above those charged by Gullfiber.

*19 February 1975. A new consultative group meeting. Press release*

Gullfiber's senior management meet the consultative group at Katrineholm in order to discuss the effects of the price freeze on mineral wool and cellular plastic. Gullfiber issues a press release stating the company's point of view. Among the points raised in the press release are the following:

- Our increased costs together with the offer that we have now received from the SPK means that production at our plants is now seriously threatened.
- If the SPK persists in their present attitude towards the company, we will be forced to introduce drastic measures such as closing down the production of both mineral wool and Styrolit. At present, the factory employs 142 individuals of whom 19 are office personnel.
- The situation is equally critical at the company's plant in Älvängen near Gothenburg, which also manufactures Styrolit. This factory has a labour force of 39 of whom 9 are office personnel.

*26 February 1975. Gullfiber lodges an appeal with the government*

Gullfiber appeals to the government against the SPK's decision of 19 February 1975 that rejected Gullfiber's request for exemption from the price freeze. The appeal describes the financial problems that are at present besetting Gullfiber. It is emphasised for instance that the company is currently operating at a loss – prior to tax and reserve allocations – with regard to the manufacture of insulation materials.

This highly unfavourable development – which has accelerated throughout the past year – has also meant that our cash reserves have declined from about 50 million SEK to almost zero. As a result, we have been forced to use bank loans in order to continue production. Most of the above amount, i.e. approximately 40 million SEK, is due to the higher purchasing price of raw materials, fuel and other essential goods. The remaining 10 million SEK is accounted for by increased investment costs. In this highly unprofitable situation for the company, Gullfiber has been forced to postpone all new investment for the time being as well as cutting down or postponing existing investment contracts.... We have previously stated that there is no scope for further reductions in our costs by means of increased efficiency since the company is already working at full capacity and using the most modern production techniques....

Accordingly, with reference to the points that we have raised above, we request that the government set aside the decision made by the Price and Cartel Office and approve our request for permission to raise prices by the aforementioned amounts, i.e. by 20 per cent in the case of mineral wool for building insulation, by 26 per cent for mineral wool used in other forms of insulation and by 27.8 per cent for cellular plastic.

*27 February 1975. A trade union delegation visits the SPK and the Minister of Commerce*

A trade union delegation consisting of two ombudsmen, Messrs Lindfors and Lundgren from the Factory Workers' Union, and two members from the local branch in Katrineholm, Messrs Hellgren and Skoog, attend a meeting at the SPK. Per Engvall, the local councillor from Katrineholm is also part of the delegation. The Director General, Åke Englund, together with Mr Pontusson and Mr Saläng represent the SPK at the meeting. According to the memoranda drawn up by Gullfiber, the following discussion is held:

Mr Englund provided an account of the negotiations that had taken place with Gullfiber and informed the trade union delegation of the price increases that had affected both Gullfiber and Rockwool. He also presented the delegation with information regarding Gullfiber's profitability. During the discussion it was mentioned (probably by Mr Hellgren) that Gullfiber had introduced autonomous working groups and had also improved the working environment in the 'Minwool' factory. He also referred to the high price of Styropor and the company's justified need to compensate itself for these increased costs. The Director General made a statement along the lines that 'a further increase in the price of Styrolit was conceivable'....

Furthermore, it was stated quite emphatically that Gullfiber would be entitled to receive compensation for the additional wage costs that would arise as a result of the current wage negotiations. This was the customary practice. This statement came in reply to a remark from one of the union officials who expressed misgivings concerning the risk that a much more restrictive attitude might be adopted by the company in relation to the implementation of the new agreements.

The trade union delegation also attended a meeting with the Minister of Commerce, Kjell-Olof Feldt following its visit to the SPK.

*28 February 1975. Gullfiber meets with the County Administration Board*

A meeting with the County Administration Board in Nyköping under the chairmanship of the County Governor, Mats Lemne, is held to discuss the situation surrounding Gullfiber's factory in Katrineholm and the effects of the SPK's policy towards the company. The meeting is attended by the Director of the County Labour Board and one of his officials, the local councillor Per Engvall, and Messrs Jansson, Olsson, Skoog, Hellgren and Eriksson from Gullfiber. The meeting commences with a discussion by Per Engvall of the effects on local employment of a closure of the factory in Katrineholm. Mr Eriksson then informs the meeting of Gullfiber's present situation with regard to ownership conditions, cost and profitability trends and the effects of the price freeze. Following this introduction, the County Governor puts forward a number of questions in relation to Mr Eriksson's report:

The County Governor had studied the balance sheets I, II and III, the liquidity reports, V2 1973 and V3 1974 as well as the report to the Central Statistical Office. The decline in company liquidity seemed to him to be substantial. With reference to the balance sheets, he enquired about our profitability and our requirements.... He emphasized that he was particularly interested in the company's future development plans in the county. I replied that our plans were in principle unchanged but that the implementation of these plans was bound up with the company's profitability....

The County Governor stated that he had been in touch with the Government in Stockholm that morning and that he would be speaking to them again at 4 pm. He requested that we send him the company's balance sheets for the past three years.

### *3 March 1975. Gullfiber contacts the SPK*

Gullfiber's Managing Director, Malte Johansson, writes to Åke Englund and requests a further meeting in order to discuss what has been said at the meeting between the SPK and the trade union representatives from Katrineholm. Mr Johansson also enquires about who had taken the initiative for this meeting.

### *5 March 1975. SPK replies*

Åke Englund replies in a letter to Gullfiber that the initiative for the Meeting had been taken by Einar Ågren, Chairman of the Factory Workers' Union. The SPK's Director General also puts forward a number of alternative dates for their meeting. The SPK will be represented at the meeting by four officials.

### *7 March 1975. Gullfiber arranges a date for the meeting*

Mr Johansson suggests that the meeting should be held on 18 March and that Gullfiber will be represented by three officials. He also states that he does not expect the meeting to discuss Gullfiber's appeal to the Government.

### *18 March 1975. Negotiations between Gullfiber and the SPK. New proposals and counter proposals*

The meeting held at SPK is attended by Messrs Lundell, Aronsson and Eriksson from Gullfiber and Messrs Ohlsson, Hallman and Salång from the SPK. According to Gullfiber's memoranda from this meeting, Gullfiber's representatives attempt to reach an agreement with the SPK.

Mr Lundell stated that he hoped today's meeting would take the form of a frank discussion of what is practically feasible. He pointed out that the company was prepared to accept price restraint but that the present situation required an immediate improvement in the company's profitability. Negotiations have taken place regarding the introduction of monthly salaries which will initially cost the company around

3 million SEK. If a corresponding increase could not be introduced immediately, it would not be possible to implement our part of the agreement with the trade union.

Mr Lundell proposes the following:

1. The SPK permits Gullfiber to exceed the frozen price levels that have prevailed from 20 December 1974 by 9 per cent in the case of building insulation materials and 15 per cent for technical and other mineral wool insulation, ie, the same exemption from the price freeze as had been obtained by Rockwool.
2. In conjunction with the signing of the collective wage agreement between the Trade Union (LO) and The Employers Federation (SAF), the SPK will permit Gullfiber to increase its prices by 5–6 per cent with respect to both the increased wage costs that result from the LO/SAF agreement and the higher prices of imported raw materials.
3. The company agrees to accept the responsibility for the deficit on Styrolit and instead to intensify its efforts to reduce costs in order to try to make the product profitable.
4. The company is prepared to withdraw its appeal to the Government.
5. The price freeze should be immediately withdrawn. The company would then be prepared to maintain an unchanged level of prices during the rest of the year provided that no major increases in costs occur.

Following the presentation of these proposals, Mr Ohlsson (SPK) requests the opportunity to discuss them privately with his colleagues.

When the meeting restarted, Mr Ohlsson pointed out that the calculation of compensation for the initial costs involved in the introduction of monthly salaries should take account of the fact that 10 per cent of the company personnel affected by this change were employed by Bilsom. He also stated that the SPK was willing to grant exemption up to the same levels as applied to Rockwool (9 and 15 per cent respectively). Furthermore, although the SPK was not in a position to commit itself to a specific percentage price increase to take account of the increase in wage costs that could be expected from the LO/SAF agreement, it was nevertheless prepared to give its approval to an increase on the basis of the criteria outlined by Mr Lundell. The SPK was also willing to actively support the case for the withdrawal of the price freeze....

A private meeting then follows during which Mr Lundell speaks by telephone to Mr Johansson in Billesholm. When the meeting restarts, Mr Ohlsson confirms that the SPK maintains the position it has previously outlined.

Following the conversation between Mr Lundell and Mr Johansson, the company was prepared to accept the 9–15 per cent proposal and that a further 6 per cent would be granted once the LO-SAF agreement had been finalised. (As a result of a

subsequent telephone conversation, this figure was raised to 7 per cent.) Mr Johansson insisted that the company's representatives obtained written confirmation on these points.

Messrs Ohlsson and Hallman expressed the view that the current wage round could give rise to a 5 per cent increase in prices. However in the present situation, this remained uncertain. Moreover, the SPK was not prepared in principle to commit itself to a specific percentage figure. Mr Hallman said that he thought that it would be most unfortunate if this question should upset the progress that they had made: they were after all on speaking terms. In his words, 'We feel that we have shown flexibility on this issue and this has been accepted by Euroc, Ytong etc'.

Following these negotiations, the SPK replies to Gullfiber's request (23 December 1974) to exceed the frozen price level for mineral wool by agreeing to a 9 per cent increase in the price of building insulation material and a 15 per cent increase in the price of technical and other insulation materials.

After the meeting, Mr Lundell and Mr Englund have a discussion in the presence of Mr Hallman in order to:

Obtain confirmation of the agreement that had been reached regarding the price arrangements to be followed for Gullfiber's products in the light of SPK's acceptance of proposals for financing the introduction of monthly salaries. This exemption from the price freeze would allow Gullfiber to raise its prices by 9 and 15 per cent respectively in relation to the February 1974 price list instead of the previously proposed increases of 7 and 12 per cent respectively.

The meeting results in an agreement that is confirmed by Mr Englund:

- a) The SPK is willing to agree to compensation for the LO-SAF agreement and for the additional (international) increases in costs that Gullfiber have had to bear since 20 December 1974. In the event of the collective wage negotiations being extended for more than a further four weeks, the SPK would still be prepared to discuss the question of prices. The SPK will support the case for the abolition of the price freeze.
- b) Gullfiber would subsequently, during the rest of 1975, maintain its prices at the same level provided that no extraordinary increases in costs occur. Gullfiber would continue production at Katrineholm at the prevailing levels of costs and prices. However Gullfiber would not be able to guarantee any particular level of production.
- c) Gullfiber would withdraw its appeal once points a) and b) were finalised.

### *25 March 1975. Problems of interpretation concerning the price freeze*

Mr Eriksson has a series of telephone conversations with Messrs Andree, Starell and Axling at the SPK in order to clarify some of the regulations surrounding the price freeze. Gullfiber is experiencing considerable problems with its customers concerning prices. Mr Eriksson summarizes these numer-



ous telephone conversations in a two-page instruction sheet that is made available to the company's sales department.

*30 April 1975. Gullfiber proposes new price negotiations*

In a letter to Mr Hallman at the SPK, Gullfiber refers to the agreement of 18 March 1975. As four weeks have elapsed since this agreement and collective wage negotiations have now been finalized between LO and SAF, Gullfiber proposes that new price negotiations should take place during Week 21.

*20 May 1975. New request for exemption*

Following the completion of the central wage negotiations, Gullfiber submits a request for a 6 per cent increase in its prices. In support of this request for exemption from the price freeze, Gullfiber submits written documentation regarding the increases in costs that have taken place as a result of higher wage and non-wage costs.

*21 May 1975. Gullfiber again visits the SPK*

A new meeting is held at the SPK in Stockholm attended by Messrs Lundell, Aronsson and Eriksson from Gullfiber and Messrs Ohlsson, Hallman and Pontusson from the SPK. The discussion concentrates on the new collective wage agreement and the prices charged by Gullfiber.

Mr Lundell opened the discussion by referring to his letter of 30 April 1975. The collective wage agreement for employees at Billeholm and Söråker had now been finalized. The agreement which covers the manufacture of mineral wool products and Styrolit means that employees would now go over to a system of monthly salaries. It should be noted that wage increases have been included for office staff belonging to white-collar unions in the calculations that were submitted to the SPK. Although negotiations with these organizations have not yet resulted in a final agreement, we consider that we have made a realistic assessment of the likely outcome.... Mr Hallman hoped that the meeting would concentrate on a discussion of the scope for price increases as a result of the new wage agreements.... The detailed presentation of the new wage awards was examined line by line. Curt Ohlsson stated that he would want a breakdown of the 20.7 per cent figure. This met with our agreement. Mr Pontusson expressed the view that the price increases of 20 March 1975 were higher than could be accounted for by the expenditure of 3 million SEK on the introduction of a monthly wage system. In reply, Mr Lundell stated that the 9 and 15 per cent increases in company prices, up to a level equivalent to that already obtained by Rockwool, was not solely intended to meet the costs of the new wage system. Mr Pontusson was satisfied by this answer.

Ake Hallman expressed a wish to have details regarding the growth of productivity, expressed in terms of tons per work year, during the past five years. This point

was followed by a discussion between Mr Aronsson and the representatives from SPK on the questions of depreciation, distribution of profits, the effect of inflation on depreciation and investment, etc. We agreed to send the requisite data to the SPK. Mr Lundell then enquired whether a rapid decision could be taken by the SPK once they had received this additional information. Åke Hallman gave a positive reply to this question.

*27 May 1975. Gullfiber sends further information to the SPK*

The requested data dealing with wage and productivity movements for the period 1970–1974 are sent to the SPK. The wage increases are specified in both kronor and percentages for all categories. Productivity measured in tons per 100 hours' work for the years 1970–1974 peaked at 94.4 in 1973 and then fell to a level of 92.5 in 1974. According to Mr Lundell, these figures give support to the view that there is little scope for further rationalization in an already highly efficient production process.

*11 June 1975*

In a letter to the SPK, Gullfiber makes a minor correction to its exemption request of 20 May 1975 regarding the share of compensation attributable to wages paid retroactively.

*16 June 1975. Agreement between Gullfiber and the SPK*

SPK informs Gullfiber that according to a decision of 12 June 1975, Gullfiber is allowed to increase the price of mineral wool by 5.2 per cent. This permission is part of the following agreement:

- 1 1.46 per cent of the agreed 5.2 per cent increase represents compensation for wages paid retroactively. This special compensation will be deducted at the time of the next price revision.
- 2 The company is allowed to reintroduce normal rebates for all of its customers.
- 3 Given the compensation outlined in points 1 and 2 above, the company agrees not to raise its prices during the rest of 1975 provided that no extraordinary increases in costs occur.
- 4 The SPK will support the case for a withdrawal of the prices freeze on mineral wool and cellular plastic. Gullfiber agrees to withdraw its appeal to the Government regarding the SPK decision to reject the company's request of 20 December 1974 for exemption from the price freeze.
- 5 Gullfiber is prepared to continue its production in Katrineholm at the prevailing levels of prices and costs. However the company is unable to guarantee any specific level of production. Consultations regarding

possible compensation for this year's wage agreement may be started if continued production at Katrineholm is considered to be at risk.

*24 June 1975. Gullfiber withdraws its appeal*

In accordance with the agreement reached in June between Gullfiber and the SPK, Gullfiber withdraws its appeal to the Government of 26 February 1975.

*Developments after June 1975*

A series of negotiations and meetings take place between Gullfiber and the SPK. Price controls on mineral wool are withdrawn in December 1975. Mandatory prior notification of increases in the price of mineral wool is introduced on 25 March 1977 and withdrawn on 22 June 1982, ie five years later. During this period, mineral wool is also subject to the short-term price freezes introduced during 1977, 1980 and 1981 and to mandatory prior notification arrangements introduced on 18 March 1978 covering all goods and services. The scope of the latter arrangements is subsequently reduced on 11 October 1978. When they are in operation, these general price controls replace selective controls on mineral wool. (See Table 1.1 on this point.)

Mineral wool is again subject to a general price freeze during the period 9 October 1982 – 28 February 1983. This price freeze is replaced on 1 March 1983 by mandatory prior notification with respect to mineral wool. This arrangement is withdrawn on 23 September 1983. Mineral wool is covered by the price freeze of April–July 1984 as well as by the price freezes of 1985 and 1987.

### 3. Price controls on light-weight concrete.

#### The case of Siporex AB, 1973 – 1976

##### **Siporex AB**

Siporex AB is part of the Euroc group, one of the largest manufacturers of building materials in Sweden. The group had more than 12 000 employees in 1976 and a turnover of about 2 200 million SEK. Siporex itself is a form of light-weight concrete made largely from cement, sand and water.

Siporex AB began its operations in 1934 in Dalby near Lund. New factories were started in Södertälje (1939), Gothenburg (1940), Gävle (1945) and Skelleftehamn (1952). At present, Siporex is produced in more than twenty countries. With the exception of Belgium and France where the company has its own subsidiaries, Siporex is manufactured under licence. In 1974, Siporex AB had a turnover of 110 million SEK and approximately 750 employees in Dalby, Södertälje and Skelleftehamn. In Sweden, the sale of Siporex is carried out by a special sales company, Lättbetong AB (Light Concrete Ltd.) which Siporex AB owns jointly with another light-weight concrete manufacturer, Ytong.

In March 1974, a price freeze was imposed on building materials including light concrete. This chapter examines the contacts between Siporex AB and the SPK that occurred as a result of the year-long price freeze between March 1974 and April 1975. The primary source of information is the correspondence that took place between Siporex AB and the SPK during the price freeze. In addition, reference will also be made to internal memoranda written by company officials in conjunction with telephone conversations or visits to the SPK. Finally, this chapter will also draw on the minutes of the Joint Works Council and on interviews with two of the company's directors, Bertil Linse and Ulf Linderöth.

## Price controls 1974-75

### *Dramatis Personae*

#### Price and Cartel Office (SPK)

Åke Englund	Director General
Lars Starell	Head of section
Curt Ohlsson	Head of division

#### Siporex AB

Bertil Linse	Director
Alf Lundgren	Director
Karl-Gustav Öhrn	Director

#### Others

Kjell-Olof Feldt	Minister of Commerce
Ulf Linderöth	Director, Gyproc AB
Sten Lindh	Chief Executive, the Euroc group
Gunnar Rosenborg	Managing Director, Interoc AB

#### *8 March 1974. Price freeze imposed on building materials*

A price freeze is announced on almost all building materials. The freeze goes into effect on 15 March 1974. Prices are frozen at the levels prevailing on 7 March 1974. According to the Minister of Commerce, Kjell-Olof Feldt, the principal reason for the introduction of the price freeze is to reduce 'the impact of international inflationary pressures' on the costs of new housing. In other words, the price freeze is justified on the grounds of international price trends rather than price increases generated by Swedish companies. In a press interview, Sten Lindh, a Euroc director, states that he fears that the decision may have repercussions on employment in the Swedish building industry.

#### *12 March 1974. Siporex applies for exemption from the price freeze*

Having already planned to increase its prices, Siporex, on the introduction of the price freeze, applies to the SPK for permission to implement its planned price increases for non-reinforced materials by 11 per cent and for reinforced concrete by 7 per cent. This would mean an average rise in Siporex prices amounting to 7.65 per cent. The company considers these proposed increases justified in the light of the higher costs of raw materials following the latest price increase in December 1973. Price rises have been particularly marked in the cases of heating oil and reinforcement rods. An increase of 7.65 per cent

would compensate the company for the increases in its costs. The written request to the SPK also draws attention to Siporex's current unsatisfactory level of profitability. In 1973, Siporex's Swedish operations ran at a pre-tax loss of 5.2 million SEK prior to interest payments and contingency reserves.

*21 March 1974. SPK requests additional information*

SPK requests further information regarding the company's application for exemption from the price freeze.

*28 March 1974. Siporex replies to SPK's letter*

In reply to the SPK's letter, Siporex provides detailed calculations regarding its range of products. Once again, Siporex draws attention to its current low level of profitability. Unless the price increases are granted, Siporex anticipates that its Swedish operations will run at a loss of 9 million SEK in 1974. If the SPK did allow these price increases to go through, the company's losses would be reduced by 3.5 million SEK. Siporex concludes its letter: 'In view of the company's precarious financial situation, we urge that a rapid decision is taken by the SPK in this matter. As we need to raise our prices by April 15th at the latest, a reply should reach us by 10 April 1974.'

*8 May 1974. SPK refuses to grant exemption for reinforced products*

In reply to the request made by Siporex on 12 March 1974, the SPK agrees to an 11 per cent increase in the prices of non-reinforced products but refuses to grant exemption from the price freeze for reinforced products. The company does not receive any explanation of this decision. According to Siporex, an increase in the price of reinforced products will not conflict with the argument put forward by the Minister of Commerce in support of the price freeze. Only 20 per cent of reinforced products are used in house construction whereas the 11 per cent increase in non-reinforced products will have a much greater impact on the house building industry since the latter accounts for almost 80 per cent of the sales of non-reinforced products.

*13 May 1974. Discussions between Siporex and the SPK*

Karl-Gustav Öhrn, Bertil Linse and Alf Lindgren from Siporex visit the SPK for a meeting with Curt Ohlsson and Lars Starell in order to discuss the refusal of the SPK to grant exemption from the price freeze for reinforced products. The memoranda from the meeting were taken by Alf Lindgren.

We stressed that the company was now placed in an untenable position by the decision to only allow exemption for non-reinforced products. If we are unable to

secure higher prices for reinforced products, the company will be forced to wind down its operations in order to make savings in both variable and fixed costs. Closure of the plant at Skelleftehamn would be the measure most likely to be taken by the company. However, this would inevitably raise the price of light concrete throughout Norrland due to the high transport costs from central Sweden. From a broader social point of view, this would be an unfortunate development. In reply to a question from the SPK, regarding the likely savings in costs to be made from a closure of the Skelleftehamn factory, we have given an estimate of around 2 million SEK. We emphasised that these measures had not been taken earlier since prior to the introduction of the price freeze, a recovery in the company's profits had seemed likely. Moreover, the company has a social responsibility for its employees.

The SPK raised the question as to whether the company's foreign operations could offset the losses that had occurred in Sweden. In reply, we emphasised that these two spheres of operation had to be examined separately. Moreover it seemed strange to expect that the company could charge higher prices abroad in order to compensate for increased costs in Sweden. In addition, the German market presents us with a number of difficulties not least in relation to prices.

The SPK considered that although the company's results for 1974 would, in the absence of higher prices, be worse than in the previous year, the company had nevertheless incurred greater losses in the past. In the SPK's opinion, Euroc would be able to withstand another year of losses for Siporex.

Later in the memorandum, it is noted that:

As a result of today's meeting and following further internal discussions, the SPK stated that they accepted that the price freeze had serious implications for employment. However, notices of redundancies must first be issued by Siporex before the SPK could re-examine the question. We were advised to appeal to the King-in-Council.

*16 May 1974. Siporex informs the Joint Works Council and the County Labour Board*

Information on the prospective cut-back in the company's operations is provided by Siporex's management to the executive committee of the Works Council and to the County Labour Boards in those counties where Siporex has its operations. Following a brief survey of events since the introduction of the price freeze in March, the company statement continues in the following manner:

The decision taken by the SPK has led to a drastic deterioration in the company's financial situation. Consequently, we have to inform the executive committees of all of our Joint Works Councils in Sweden that the company is now forced to rapidly reduce its operations in Sweden unless the King-in-Council upholds the appeal that the company is to make against the SPK decision. Consultations within the executive committee on the measures to be taken will start immediately. Measures

will also have to be taken to reduce costs within the company's central organization. It is likely that all development projects will have to cease. This will inevitably have repercussions on employment within the company's central organization. Consultations on this issue will also start immediately. The County Labour Boards in the counties concerned have also been informed of these matters. An appeal against the SPK decision will now be made to the Government. In this appeal, we will emphasize the serious threat to employment in our factories in Sweden. The company's decisions regarding a cut-back in operations in Sweden are wholly dependent on the outcome of this appeal.

*17 May 1974. Siporex appeals to the Government.*

Siporex appeals to the Government against the decision taken by the SPK on 8 May 1974. Due to further increases in the price of iron that have taken place after the company made its request for exemption on 12 March 1974, Siporex requests permission to raise the price of reinforced concrete by the 7 per cent that SPK had rejected and by an additional 3 per cent to cover the new higher price of iron.

*13 June 1974. The SPK partially approves Siporex's appeal*

The SPK submits a written statement to the Ministry of Commerce concerning Siporex's appeal of 17 May 1974. Following contacts with the relevant County Labour Boards and trade unions on the employment situation, the SPK proposes that the company's appeal should be partially approved. Accordingly, Siporex is granted permission to exceed the statutorily frozen price levels by 5 per cent.

*19 June 1974. Siporex replies to the SPK statement*

In a written statement to the Ministry of Commerce, Siporex contends that the increase of 5 per cent in the price of reinforced Siporex granted by the SPK, fails to provide adequate compensation to the company for its increased costs. Siporex estimates that the shortfall in revenue amounts to 3.4 million SEK and will make an already difficult situation untenable. The company also draws attention to the fact that it has had to announce a substantial cut-back in its operations as a result of the SPK's decision of 8 May 1974. It is also emphasized that this cut-back will have to be implemented unless the company receives permission to raise its prices.

*28 June 1974. Ministry of Commerce agrees to a limited price increase*

The Ministry of Commerce informs Siporex that it has accepted the SPK's proposed 5 per cent increase of the prices of the company's reinforced



products. This increase, which is half of the amount requested by Siporex, has been granted in the light of the employment situation that has arisen. Siporex does not receive any explanation for the rejection of its request to raise prices by 10 per cent.

*15 August 1974. Siporex requests exemption from the price freeze for load-bearing beams*

The Siporex factory in Södertälje has introduced a new method of production for load-bearing beams. This innovation, which is intended to contribute to an improvement in the employees' working environment, has increased the company's costs of production. In order to compensate for these additional costs, Siporex requests exemption from the price freeze for load-bearing beams.

*26 August 1974. Siporex requests exemption for reinforced Siporex*

Siporex AB applies to the SPK for permission to exceed the current frozen price for reinforced Siporex by 3 per cent from 1 October 1974. The company considers that this increase is warranted on the grounds of higher raw material costs.

*26 September 1974. The SPK withdraws a promised price increase*

Following a telephone conversation with the SPK, Bertil Linse of Siporex AB receives a verbal assurance that the company will be allowed to increase the prices of reinforced materials by 3 per cent from 1 October 1974. Several days later, the company is informed that the Director General of the SPK, Åke Englund, has not given his approval to this increase.

*9 October 1974. SPK visits Siporex*

Representatives from the SPK visit Siporex AB in order to discuss the company's request of 26 August for exemption from the price freeze.

*11 October 1974. Joint Works Council meets in Malmö in order to discuss the closure of the Södertälje factory*

A special meeting of the Joint Works Council takes place at the company's head office in Malmö in order to discuss the closure of the Södertälje factory. At the same time, the executive committee of the Joint Works Council in Södertälje is informed that the company wishes to have consultations on the possible closure of the plant. The major reason for this discussion is the decline

in construction activity in the Stockholm area. Between 1972 and 1974, the number of completed flats declined from 20 000 to 14 500 while the estimate for 1980 is only 8 000. The deterioration in the company's financial situation as a result of the price freeze has also contributed to the likelihood of a plant closure in Södertälje. During 1974 so far, the increases in the costs of production of the company's two major beam products are 34 and 41 per cent, respectively. The corresponding price increases for these products are 5.5 and 14.5 per cent, respectively.

*14 October 1974. Joint Works Council in Södertälje meets to discuss possible plant closure*

The Joint Works Council in Södertälje discusses the possibility of plant closure. Information on the risks of closure is given to all of the employees at the plant. In conjunction with the meeting, the following press release is issued.

As a result of the price freeze on light concrete and the decline in housing construction, the senior management of the Siporex plant at Södertälje – a company belonging to Euroc's Interoc division – have informed the Joint Works Council that it wishes to have consultations on the probable closure of the plant. It is estimated that about 200 employees – 165 skilled and unskilled workers and 40 staff – would be affected by a closure. Substantial increases have taken place in the costs of raw materials used in the manufacture of light concrete since the introduction of the price freeze on the majority of building materials in March 1974. At the same time, Siporex has been unable to increase its prices sufficiently to compensate for these higher costs.

The decline in housing construction – which is expected to continue during the next few years – has added to the company's present difficulties. There are few export opportunities available due to the high freight costs involved....

According to Interoc's Managing Director, Gunnar Rosenborg, the exemptions that the company has obtained have been either too late or too insubstantial to offset the negative effects of the price freeze. The factory at Södertälje accounts for almost 25 per cent of Swedish Siporex production. The company's other two Siporex plants in Sweden, at Dalby near Lund and at Skelleftehamn, account for 55 and 20 per cent respectively. At present, the volume of deliveries from the latter two factories is substantially higher than the budgeted figures. In Södertälje on the other hand, deliveries are far below expected levels, largely due to the marked decline in housing construction in the Stockholm region. Enquiries have been made with other industrial employers in the Södertälje region regarding the possibilities of alternative employment for redundant personnel.

*16 October 1974. Siporex supplements its request for exemption*

Siporex sends additional information to the SPK in support of its request for exemption from the price freeze of 26 August 1974.

*25 October 1974. Meeting of consultative group in Södertälje*

The consultative group meets in Södertälje. The following agreed statement is released: 'The group considers that production can be continued at the Södertälje factory on an acceptable financial basis provided that the price freeze is abolished or is modified in such a manner that it ceases to affect the company's financial position.'

*6 November 1974. Proposed closure of Södertälje factory*

The consultative group at Södertälje meets again to discuss the factory's future prospects. The company's senior management proposes that the plant should be closed down.

*10 November 1974. Closure of Södertälje factory*

A decision is taken on the closure of the Södertälje factory. The Board of Interroc AB issues the following press statement: 'The Board of Interroc AB does not consider it feasible to continue production at the Siporex factory in Södertälje. Consequently the plant will be closed at the end of June 1975.'

*19 November 1974. The Chief Executive of the Euroc group writes to the SPK*

The Chief Executive of the Euroc group, Sten Lindh, writes to the Director General of the SPK, Åke Englund, to inform him of the consequences of the price freeze for the Euroc group. Mr Lindh writes, *inter alia*:

During the autumn, there have been several instances of factory closure and production cut-backs within the Euroc group that have to varying but substantial degrees been caused by the price freeze. The likelihood of similar disruptions to production threatens future developments.

The effects of the price freeze have been particularly difficult to bear since the Swedish construction industry, including the building materials sector, has been in continuous decline for the past three years. During 1974, the severe recession has also seriously affected the market for building materials in neighbouring countries. Hence it is not only a question of being unable to reduce costs by means of an expansion of volume. The decline in sales has actually led to higher costs and further intensified the pressure exerted by the price freeze on the company's profitability.

*26 November 1974. Interroc AB submits a proposal to the SPK*

Gunnar Rosenborg proposes during a visit to the SPK that the Interroc group, which includes Siporex, should be allowed to raise its prices by 12 per cent on condition that no further increases take place before 1 March 1975. Curt

Ohlsson of SPK promises to get in touch with Mr Rosenberg once he has presented the proposal to the SPK's Director General.

*20 December 1974. Siporex demands a decision on its request for exemption*

As Siporex has not received any notification regarding its request of 26 August 1974 to raise the price of reinforced Siporex, the following letter is sent to the SPK:

On August 26 we requested permission to raise the price of reinforced Siporex by 3 per cent from October 1st 1974. Frequent contacts between the SPK and Siporex AB have taken place since that date both in the form of telephone conversations and personal visits. In addition you examined our cost calculations, annual accounts etc at our Malmö office on October 9th. Although four months have now elapsed since the submission of our application, Siporex AB has still not received a reply....

As indicated by the enclosed calculations, our profitability is highly unsatisfactory. The maintenance of an unchanged level of prices during 1975 will therefore have serious, far-reaching repercussions for the company's financial situation. The cut-back in production that has taken place has led to the proposed closure of our plant in Södertälje and to the dismissal of office personnel in our sales and technical departments. The costs involved in this closure are not included in our calculations.

A further deterioration in the company's profitability as a result of a refusal to grant price rises will unfortunately lead to further dismissals of white collar staff.

A refusal to grant the company the requested price increases would inevitably give rise to a further loss of profitability and to the dismissal of office personnel. This would, in turn, lead to the suspension of the company's investment programme, the cancellation of development projects and the postponement of marketing projects. It is quite evident that these measures are seriously detrimental to the company's development. For instance, the continuous loss of personnel represents a fundamental weakening of the company's capacity. Similarly, the deterioration in the company's liquidity position creates an insolvency that cannot be covered by grants from the parent company.

Accordingly we request that the SPK deals with our application for exemption at the earliest possible date in order that the company can implement these price adjustments by, at the latest, February 1st 1975.

*3 February 1975. SPK proposes structural rationalizations*

Mr Linderoth of Gyproc AB, a company which belongs to the Euroc group, visits the SPK. In a memo, he notes:

During the discussions which took place on February 3rd, Curt Ohlsson (SPK) made a remarkable statement. In his view, the refusal of the SPK to grant the company's requested price increases for light concrete was a positive development. The industry was in need of structural rationalization. The introduction of such measures would have inevitably been delayed if approval had been given to the requested price increases.

#### *4 February 1975. SPK grants approval*

The SPK informs Siporex that the company is allowed to increase the price of reinforced products by 3 per cent as requested on 26 August 1974.

#### *20 March 1975. Price freeze is replaced by mandatory prior notification*

The Government abolishes the price freeze on building materials from 1 April 1975. It is to be replaced by a system of mandatory prior notification of price increases.

#### *Developments after March 1975*

Correspondence and contacts between Siporex and the SPK continued after the abolition of the price freeze. Two representatives from Siporex visited the SPK at the beginning of April 1975 to discuss requested price increases for reinforced and non-reinforced products of 11.5 and 10 per cent, respectively. The price increase was introduced on 1 May 1975. Mandatory prior notification of increases in the prices of building materials was abolished on 21 December 1975.

Siporex products were made subject to the mandatory prior notification that was introduced on 18 March 1978. This obligation to notify planned price increases was withdrawn for Siporex products on 22 June 1982. Furthermore, Siporex products were also subject to general price freezes that were introduced on seven separate occasions between 1977 and 1985. Following the price freeze that was in force between October 1982 and February 1983, building materials were subject to prior notification procedures until the end of September 1983. Siporex products were subject to price freezes during April – June 1984, March – September 1985 and during 1987.

## 4. Price controls on paper tissue products.

### The case of MoDo consumer products 1974–75 and 1978–79

#### **MoDo Consumer Products**

MoDo Consumer Products (MoDo-K), which has its head office in Solna, is one of six subsidiary companies that are wholly owned by Mo-Domsjö Ltd. MoDo-K was founded in 1972 and produces and sells household and toilet paper, disposable napkins, sanitary towels and tampons. The company's operations are divided into three main regions: Scandinavia, Central Europe and Great Britain. In early 1977, the company had about 1700 employees of whom roughly 1000 were located in Scandinavia. Company turnover in 1977 was 414 million SEK of which the Scandinavian market accounted for 255 million SEK.

For most of the 1970s, MoDo-K was subject to either a price freeze or was obliged to provide prior notification of planned price increases for its paper tissue products, that is, household and toilet paper and disposable napkins. This chapter deals with two price freezes. The first was introduced in March 1974 and continued for 19 months. The second freeze covered the three months from October to December 1978. The account of the course of events during these periods of price freezes is based principally on the correspondence that took place between MoDo-K and the SPK both during and after the periods of price control, and on interviews with John Nordlund, the company's Managing Director, Rolf Erlandsson, Marketing Director, and Olle Sten, Finance Director.

## Price controls 1974–75

### *Dramatis Personae*

#### Price and Cartel Office (SPK)

Kerstin Björkholm	Assistant
Åke Englund	Director General
Åke Hallman	Head of division
Olof Pontusson	Head of department
Stefan Saläng	Head of section

#### MoDo Consumer Products

Rolf Erlandsson	Marketing Director
Werner Magnusson	Finance Director
John Nordlund	Managing Director
Nils Sjögren	Marketing Director
Olle Sten	Finance Director

#### MoDo AB

Matts Carlgren	Managing Director
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### *22 February 1974. MoDo–K notifies SPK about planned price increase*

MoDo Consumer Products (MoDo–K), which has been subject to mandatory prior notification since September 1973, notifies the SPK of planned price increases for plastic tie pants and household and toilet paper. The company has decided to raise the price of its household and toilet paper products by 9–10 per cent and its *Rustibuss* plastic tie pants by 20–25 per cent. The company states that these price increases have been brought about by increased costs for transport, insurance, raw materials, wages and fuel.

### *8 March 1974. Introduction of price freeze*

A price freeze is introduced covering household, sanitary and toilet paper products as well as disposable napkins and serviettes. Prices are frozen at the levels prevailing on 7 March 1974. The price freeze is due to come into force on 15 March 1974.

### *26 March 1974. MoDo–K requests exemption from the price freeze*

MoDo–K, which had announced planned price increases for both household

and toilet paper and plastic tie pants, applies to the SPK for exemption from the price freeze. The company submits a request to raise the price of its disposable napkins, household and toilet paper by an average of 13–25 per cent. In the company's judgement, these price increases are primarily justified on the grounds of the increases in costs that have taken place since the last price rise in January 1973. However, increases in costs that occurred during the latter part of 1973 for which the company has not received full compensation are included in the requested price increase. Due to the recent marked deterioration in company profits, MoDo-K urges the SPK to deal with its request for exemption from the price freeze as quickly as possible.

#### *4 April 1974. SPK requests further information*

In order to assess MoDo-K's application for exemption from the price freeze, the SPK requests the following additional information:

- 1 Value of sales per ton for various paper tissue products, at 1 March 1973.
- 2 Purchase prices of those inputs whose prices have changed and whose costs are significant enough to exert an influence on product prices. Price data is required for the following dates: 1 March 1973, 15 January 1974 and 1 April 1974. This information should be verified by means of photostat copies of invoices.
- 3 According to the directives laid down by the King-in-Council, an exemption from the existing frozen price levels could only be granted in special circumstances. Consequently, a detailed and *specific* (italics by SPK) account of the company's profitability is required. This analysis, which should also be supplemented by the annual reports of the past three years, must clearly indicate the company's reasons for increases in prices during the present price freeze.

#### *3 May 1974. Additional information provided by MoDo-K*

MoDo-K submits the additional information requested by the SPK in its letter of 4 April 1974. This material consists of photostat copies of 55 invoices together with eight typed pages of information dealing with the company's profitability. John Nordlund, MoDo-K's managing director, concludes:

In the light of this additional information and against the background of the unacceptably low level of profits that has resulted from the extraordinary increases in the company's costs, as shown in Appendix 3, we would once again urge the SPK to give our request for exemption prompt consideration in order to ensure continued production.



*29 May 1974. SPK rejects request for exemption*

The SPK sends the following letter with regard to MoDo-K's request for exemption from the price freeze:

In a written submission to the SPK of March 26th 1974, you have requested permission to exceed the present frozen price levels for household and toilet paper as well as for disposable napkins, on the grounds of increases in your costs. After due consideration, the SPK has decided to reject your request.

The grounds for this decision are not disclosed by the SPK.

*31 May 1974. MoDo-K requests a reappraisal of the SPK decision*

As a result of the proposed new increases in the price of pulp to come into force on 1 July 1974, MoDo-K asks the SPK to review its decision of 29 May 1974.

*12 July 1974. Price freeze is modified but remains in force for disposable napkins*

The price freeze on household, toilet and sanitary paper is withdrawn and replaced by a system of mandatory prior notification of planned price increases. However, the price freeze on nappies is retained.

*18 July 1974. SPK grants exemption*

Against the background of the proposed increase in the price of pulp, the SPK reviews its previous rejection of MoDo-K's request of 26 March 1974 for exemption from the price freeze. The SPK is now prepared to accept a 12 per cent increase in MoDo-K's prices. The latter had requested price rises of between 13 and 25 per cent.

*26 July 1974. MoDo-K appeals to the Government*

An appeal is lodged by MoDo-K against the SPK ruling of 18 July. The company concludes its appeal to the Government in the following manner:

We request that the King-in-Council reviews the decision taken by the SPK and grants us permission to raise the net price of a 100 package of *Nalle* and *Princess* nappies to 13.22 and 12.26 SEK respectively.

If this request were not to be approved, our products would inevitably have to be withdrawn from the market. Consequently, the production of nappies at Hallsberg would have to be discontinued.

As a result of the higher price increases that have been granted by the SPK to other low price manufacturers, the current price level for 100 nappies is between 12 and 14 SEK: in other words, at a level equivalent to that we have requested.

It would seem doubtful on economic grounds whether these companies would be able to retain their present volume of sales if we decide to adopt the prices proposed by the SPK for *Nalle* and *Princess* napkins, namely 9.57 and 10.46 SEK, respectively. As these companies lack the financial resources to sell their products at below their costs of production, this alternative would thereby endanger their very existence and pose a threat to employment at their factories.

As this matter is of the greatest importance for the security of employment in a number of Swedish industries as well as for the future availability of a relatively large number of low price products, we would request that it receives your earliest attention. We would also wish to appeal against the decision by the SPK to restrict price increases of our other napkin products to 12 per cent. However, due to the holidays, we will submit a detailed case in support of our appeal at a later date.

### *12 August 1974. SPK reports to the Ministry of Commerce*

The SPK reports to the Ministry of Commerce on the appeal made by MoDo-K on 26 July 1974. Following a summary of the course of events, the SPK continues:

MoDo manufactures both disposable napkins of a standard quality called *Rustibuss* and a lower quality, low price product called *Nalle*. The latter was first sold in January 1974 at a price lower than its variable costs of production.

The price of the *Nalle* napkins is lower than the price of other disposable pads. The SPK is prepared to accept a further 5 per cent increase in the price of *Nalle*, above the present 'frozen' level, since there is a considerable risk that the product would have to be withdrawn from the market unless a price increase is forthcoming.

As no new circumstances have arisen regarding the other qualities of napkins, the SPK proposes that the King-in-Council rejects the company's appeal concerning these products.

### *16 August 1974. MoDo-K replies*

MoDo-K submits a reply to the Ministry of Commerce regarding SPK's statement of 12 August 1974. In its reply, the company refers to a number of errors that appeared in the SPK statement: 'On several previous occasions, we have pointed out to the SPK that the company has not used pulp from its sister company, MoDo Cell AB, in the manufacture of *Nalle* and *Princess*.'

The pricing policy of MoDo-K products at the end of 1973 has, in the view of the company, also been dealt with in summary fashion. In particular, scant attention is paid to the reason why the price of *Nalle* was lower than its variable costs of production as early as January 1974. (This product had just been introduced on to the market on 1 January 1974. In order to achieve quickly a market share, the company priced the product below its variable costs. The introductory price was still in operation when the price freeze was introduced on 7 March 1974.) MoDo-K's reply to the Ministry of Commerce concludes:

‘The company has now decided not to take any further orders for *Nalle* nappies. Production will be limited to the completion of existing orders. The question as to whether the company will continue with its production of *Princess* napkins will depend on the outcome of our appeal.’

*23 August 1974. The Ministry of Commerce grants exemption*

In reply to MoDo-K’s appeal of 26 July 1974, the Ministry of Commerce grants a 15 per cent increase in the price of *Nalle* napkins which was substantially higher than the 5 per cent rise recommended by the SPK in its report of 12 August 1974. As regards *Princess* napkins, the Ministry of Commerce follows the line adopted by the SPK and rejects any price increase.

*2 December 1974. MoDo-K visits the SPK*

MoDo-K visits the main office of SPK in Stockholm in order to discuss increases in the prices of household and toilet paper. The company’s representatives draw attention to the ‘very serious losses’ that are at present affecting the company.

*11 December 1974. MoDo-K reports an increase in the price of household paper*

MoDo-K notifies the SPK that the company plans to raise the price of household and toilet paper by approximately 10 per cent. John Nordlund concludes the letter to the SPK in the following manner:

We would wish to emphasize that the prime reason for the notified price increases is not so much the increases in costs that have occurred since the last price increase but rather that the company has been generally unable to secure compensation for previous increases in its costs. As a result, profits are not only unsatisfactory: the company finds itself incurring actual losses.

*18 December 1974. SPK requests additional information*

The SPK requests additional information from MoDo-K in support of its planned price increases for household and toilet paper since it does not consider that the company has adequately specified its costs and other factors that would warrant a rise in the company’s prices. Consequently, the SPK rules that the 30 day period of respite will not come into effect on 11 December 1974 but from the day on which the company submits to the SPK an acceptable case for the planned price increases.

*27 December 1974. Reply from MoDo-K*

MoDo-K replies to the letter from the SPK, dated 18 December 1974. John Nordlund repeats the arguments that were presented in the company's prior notification on 11 December 1974 of the planned price increases.

*31 January 1975. Discussions between MoDo-K and the SPK*

A meeting is held between MoDo-K and the SPK. The company is represented by John Nordlund, Managing Director, Werner Magnusson, Director of Finance and Nils Sjögren, Director of Marketing. The SPK is represented by Kerstin Björkholm and Stefan Saläng. The latter keeps minutes of the meeting. The principal point of discussion is the planned 10 per cent rise in the price of household and toilet paper. In a summary of the meeting, Stefan Saläng of the SPK writes:

According to the company's internal analysis of profitability for the period January–November 1974, a relatively marked decline in profits occurred in the Scandinavian region. To a certain extent, this deterioration in profits was offset by improved profitability in the British market. The Central European region was not expected to show any significant change in profits during this period.

John Nordlund takes strong exception to this view. In his opinion, a profitable British market is no argument for producing at a loss in Sweden.

*3 March 1975. MoDo-K increases the price of household paper*

MoDo-K increases its prices of household and toilet paper products by 10 per cent.

*1 July 1975. MoDo-K notifies the SPK of new planned price increases*

MoDo-K reports to the SPK that the company has raised the price of household and toilet paper. After discussing the general background, John Nordlund continues in his letter to the SPK:

The serious deterioration in company profits during 1974 and 1975, which has now resulted in continuing losses for the company, has occurred in spite of the major efforts made by the company to rationalise its operations. Moreover, this situation has come about at a time when the company has experienced significant growth in its markets.

Hence, there is no doubt that the main reason for this deterioration in the company's profitability is, as you well know, related to the company's inability to secure adequate compensation for the very substantial increase in its costs.

The company realises that the problem of declining profitability has also affected

other companies in the industry. Consequently, it is our firm belief that the SPK is well aware of the serious implications of the present situation and of the impossibility of continuing to produce at a loss. Confronted with this extremely serious situation, the company is compelled to increase its prices in order to compensate not only for the increases in costs that have taken place this year (5.1 per cent) but also to take account of earlier price rises that were not actually implemented (4.0 per cent). In other words, a total increase in costs of 9.1 per cent.

Most of these increases in costs have already had a serious impact on company profitability. Consequently, we urge the SPK to grant, without delay, the price increases requested by the company.

*2 July 1975. MoDo-K requests permission to raise the price of its napkins*

MoDo-K applies to the SPK for permission to raise the price of its disposable nappies by between 9 and 19 per cent. According to the company's managing director, the price freeze on napkins must now be considered as a permanent feature since it has been in operation for seventeen months. As a result, the company has been forced to reappraise its production of napkins. In particular, it is now uncertain whether the company will be able to continue to manufacture the products most affected by the price controls, ie *Nalle* and *Princess*.

*16 July 1975. SPK requests additional information*

SPK requests additional information regarding the company's application to raise the prices of its paper tissue products. The SPK does not consider that it has received sufficient information to be able to carry out an assessment of the company's request. The one month period of respite will, according to the SPK, come into force on the date on which the SPK receives the requested material.

*18 July 1975. Reply from MoDo-K*

The following letter from MoDo-K is sent in reply to the SPK's written request of 16 July 1975:

Thank you for your letter of July 16th, 1975. In our view, the company's prior notification was completely in accordance with existing regulations as the planned size of the increase, the date on which the increase was to come into force and the reasons for the increase were all specified in our notification request.

Hence the respite period ought to cover the period of one month from the date on which the SPK received our notification request.

We will naturally provide the additional information that you have requested.

*25 July 1975. MoDo-K visits the Ministry of Commerce*

MoDo-K visits the Ministry of Commerce in order to hand over a written report providing details of the background to the company's proposed increases in the prices of household and toilet paper. This report also deals with the company's exemption request of 2 July 1975 concerning an increase in the price of napkins.

*29 July 1975. SPK requests further information*

The SPK requests additional information concerning MoDo-K's application for exemption from the price freeze on napkins.

*30 July 1975. MoDo-K sends additional material*

In reply to SPK's request of 16 July 1975 MoDo-K sends the additional information concerning the prior notification of increases in the prices of household and toilet paper.

*5 August 1975*

MoDo-K sends further material to the SPK concerning the prior notification of 1 July 1975.

*20 August 1975*

MoDo-K sends additional information to the SPK related to its exemption request for an increase in the price of napkins.

*1 September 1975*

Following a telephone conversation with the SPK, MoDo-K sends detailed calculations showing the increases in prices and costs that have affected the company's *Vita Lamm* household paper. According to these figures, the increase in the company's costs is equivalent to a price increase of 13.3 per cent. An equivalent estimate by the SPK indicates a price increase of 4 per cent.

*2 September 1975*

A forecast of company profits in the British market is sent to the SPK.

*8 September 1975. Negotiations between MoDo's management and the SPK*

Matts Carlgren, Managing Director of Mo Domsjö AB, and John Nordlund,

Managing Director of MoDo-K, meet with Åke Englund, Director General of the SPK. Carlgren and Nordlund describe the impact that the price freeze has had on the company since its introduction in March 1974. In the report submitted to the SPK's Director General, the following statement is made:

During 1974, when MoDo's overall profitability was satisfactory, the company was able to accept 'short-term interventions', as they were called by the Ministry of Commerce. Today the situation is quite different. The timber trade is stagnant and operates at a loss. The pulp market is weak and deliveries have been markedly reduced. Prices are tending to fall. The fine paper market has also been seriously affected by the severe recession. This branch is now operating at a loss. The growing volume of inventories has tied up large amounts of capital. Combined with a heavy investment programme, this has imposed a severe strain on MoDo's liquidity with the result that planned investments have had to be curtailed.

In certain acute situations, price controls can be considered to be necessary. However, when companies and in this case, an entire industry is placed under severe pressure over a long period of time, the situation becomes quite untenable with a whole range of undesirable consequences making themselves felt....

In order to achieve the best possible results for us all, employers, employees and government authorities should endeavour to live in harmony with each other. Government authorities must be able to provide companies with clear and fairly long-term rules of conduct for their operations. Companies must to a much greater extent than now be able to rely on the information that they receive from the authorities. Moreover in their assessment of the grounds for price increases, the SPK must not only take account of increases in short-run variable costs, as is presently the case, but also give due consideration to increases in the company's fixed costs. Against this background of rising costs and declining profitability, the increases in prices requested for household and toilet paper together with the requested exemption for napkins are, in our opinion, extremely reasonable. A failure to approve these requests would inflict serious and irreparable damage on the company.

#### *10 September 1975. SPK agrees to higher prices for disposable napkins*

The SPK informs MoDo-K that it is prepared to grant an exemption to raise the price of disposable napkins above the present frozen level of prices. Increases of 5 and 7 per cent respectively are permitted for *Rustibuss* and *Nalle* and *Princess* (MoDo-K had requested a 19 per cent increase in the price of the *Nalle* and *Princess* products and an increase of between 9 and 15 per cent for *Rustibuss*, dependent on the size of the package).

#### *16 October 1975. Agreement between SPK and MoDo-K. SPK supports the abolition of the price freeze*

The SPK agrees to a 5 per cent increase in the price of household and toilet paper. This decision applies not only to MoDo-K but to the entire industry. MoDo-K confirms that the company has accepted this 5 per cent increase

rather than the previously requested 9 per cent rise. At the same time, MoDo-K is prepared to accept SPK's proposal that the price of disposable nappy pads should not be increased prior to 1 February 1976. In return, the SPK agrees to support the abolition of the price freeze.

#### *22 October 1975. Abolition of price freeze on disposable napkins*

The price freeze on napkins is abolished and replaced by mandatory prior notification of planned price increases. The price freeze was thus in force for a period of 19 months.

### **Price controls 1978-1979**

#### *2 August 1978. MoDo-K notifies the SPK of planned increases in the prices of napkins and household paper*

In accordance with the company's obligations under the system of mandatory prior notification, MoDo-K notifies the SPK of a planned increase of 4.9 per cent in the prices of napkins, toilet and household paper. A number of reasons are put forward for these increases of which the most important is the higher price of pulp. This price rise will take effect from 4 September 1978.

#### *1 September 1978. MoDo-K visits the SPK*

As a result of a further increase in the price of pulp, representatives of MoDo-K visit the SPK in Stockholm in order to discuss the company's desire to include these increased costs in the prior notification that it made on 2 August.

The company withdraws the price increases to be introduced on 4 September in order to submit a new prior notification.

#### *8 September 1978. New price increases announced by MoDo-K*

MoDo-K notifies the SPK that it intends to increase the prices of its napkins, toilet and household paper products by approximately 8 per cent on 16 October 1978 to compensate for higher costs. MoDo-K delays raising the price of its paper tissue products until 23 October 1978 and its napkins until 30 October 1978.

#### *20 September 1978. Negotiations between MoDo-K and SPK*

Representatives from MoDo-K and SPK discuss the price increases reported by the company on 8 September 1978.



*4 October 1978. MoDo-K writes to the SPK*

In a letter to the SPK, Rolf Erlandsson, Marketing Director at MoDo-K, discusses the company's present lack of profitability.

*12 October 1978. MoDo-K makes an offer*

The SPK does not consider MoDo-K's proposed 8 per cent price increase to be justified. During a telephone conversation, the company proposes to the SPK that it should be allowed to raise its prices by between 7 and 7.3 per cent. However, the SPK considers that the price increase should be limited to 5.5 per cent. No agreement is reached between the parties.

*13 October 1978. Criticism of the SPK*

As a result of the telephone conversation of 12 October 1978, Rolf Erlandsson criticizes, in a letter to the SPK, the methods used by the SPK to assess profitability.

*19 October 1978. SPK replies to the criticism*

Åke Hallman of the SPK replies to MoDo-K's criticism of the SPK's methods of calculation.

*20 October 1978. New meeting between MoDo-K and the SPK*

A further meeting is held between representatives of the SPK and MoDo-K to discuss the company's planned price increases. Both parties remain committed to their standpoints, ie MoDo-K insists on price rises of between 7 and 7.3 per cent while the SPK refuses to accept increases above 5.5 per cent. The negotiations are concluded at 3.15 pm without any agreement being reached.

*Price freeze on napkins and paper tissue products*

At 3.50 pm, Olof Pontusson of the SPK phones to inform MoDo-K that a price freeze has been imposed on disposable napkins and paper tissue products, to take effect from the previous day, ie 19 October 1978.

As a result of this price freeze, MoDo-K has now to apply to the SPK for exemption in order to be able to raise its prices by the 5.5 per cent to which the SPK had already agreed when negotiating with the MoDo-K earlier the same day.

*23 October 1978. MoDo-K writes to the SPK*

Rolf Erlandsson writes to Åke Hallman at the SPK in order to try to clear up the misunderstanding that has arisen in relation to the company's letter of 13 October 1978.

*24 October 1978. MoDo-K applies for exemption from the price freeze*

MoDo-K applies to the SPK for permission to raise the price of its napkins and paper tissue products by an average of between 7 and 7.3 per cent. MoDo-K suggests that the motives for this increase have been previously presented in the written evidence already submitted to the SPK as well as during the negotiations with the SPK that have taken place during the autumn.

*SPK commences negotiations*

MoDo-K's application for exemption from the price freeze is not dealt with by the SPK. Instead negotiations take place during November and early December, at the request of the SPK, to discuss the abolition of the price freeze. On condition that the company maintains an unchanged level of prices during 1979, excluding exceptional increases in costs, the SPK is prepared to agree to a 5-6 per cent increase in the company's prices. According to the SPK, this rise will compensate MoDo-K for its increased costs during 1978 and for the 'normal' increases in costs that took place during 1979.

This offer is clearly inferior to that proposed by the SPK during October, prior to the introduction of the price freeze. On that occasion, the SPK offered 5.5 per cent as compensation for the increases that occurred during 1978. The SPK considers that this more restrictive offer is justified on the grounds of the changed circumstances now in operation following the introduction of the price freeze.

*13 December 1978. SPK improves its offer. MoDo-K accepts*

Following a series of discussions and negotiations between MoDo-K and the SPK, the latter raises its offer to 7 per cent. A rejection of this offer by MoDo-K would force the SPK to deal with the company's exemption request. It is made clear to MoDo-K that this request would most probably be rejected since in the short run, employment is not under threat and there is no risk that the company would withdraw a 'budget price' commodity from the market. Under these circumstances, MoDo-K accepts SPK's offer and raises its prices by 7 per cent from 2 January 1979 in the case of household and toilet paper and from 15 January 1979 in the case of nappies.

*8 January 1979. MoDo-K raises the price of household paper*

MoDo-K raises the price of household and toilet paper by 7 per cent.

*15 January 1979. MoDo-K raises the price of nappies*

MoDo raises the price of baby napkins by 7 per cent.

*26 January 1979. Price freeze abolished*

The price freeze on household and toilet paper and on disposable napkins is abolished and replaced by mandatory prior notification of planned price increases.

*Developments after January 1979*

Disposable napkins, sanitary towels and paper tissue products are subject to mandatory prior notification until 22 June 1982 as well as to the general price freeze that is in operation between 1980 and 1981. Mandatory prior notification is reintroduced following the general price freeze that is in operation between October 1982 and February 1983. These notification procedures are withdrawn on 24 September 1983. A price freeze covers MoDo-K's products from April to July 1984. A new price freeze is instituted in March 1985 and terminated in mid-September 1985, January 1987 and December 1987, respectively.

## 5. Price controls on bricks.

### The case of AB Tegelcentralen 1978

#### **AB Tegelcentralen**

AB Tegelcentralen is a sales company for six brickworks in the southern Swedish province of Skåne. The company which has its head office in Malmö is jointly owned on the basis of equal shareholdings by Bara, Kaniks, Klippans, Minnesbergs, Slottsmöllans and Östra Grevie brickworks. Prior to its bankruptcy in 1978, Högs New Brickworks/Helsingborgs Brick Steamworks was also a part-owner of AB Tegelcentralen. In 1979, AB Tegelcentralen sold bricks to the value of 54 million SEK. In the event of losses, the company charges the brickworks a commission sufficient to eliminate these losses. AB Tegelcentralen, which has a 35 per cent share of the Swedish brick market, is considered by its competitors to be the market leader. Instead of conducting negotiations with the individual brickworks, the SPK carries on negotiations with AB Tegelcentralen.

In January 1978, a special price freeze was introduced for both facing and building bricks. This price freeze, which was of relatively short duration, was withdrawn in May 1978. The present chapter examines this short price freeze with the help of the correspondence that took place between the parties and internal memoranda written by the company's directors Tommy Harneman, Ingvar Persson and Karl-Olov Fentorp. Reference is also made to interviews with the above company representatives.

## Price controls 1978

### *Dramatis Personae (in order of appearance)*

#### Price and Cartel Office (SPK)

Per Åke Eriksson

Gun Schulte

Åke Hallman

Head of Division

Olof Pontusson

Head of Department

#### AB Tegelcentralen

Tommy Harneman

Director

Ingvar Persson

Director

Karl-Olov Fentorp

Director

Sven Bauer

Chairman of the Board

Mr Ohlsson

Mr Ekström

#### Ministry of Commerce

Per Borg

Head of Department

### *14 December 1977. Tegelcentralen raises its prices*

The board of AB Tegelcentralen announces an average increase of 11.5 per cent in the price of bricks to take effect from 1 January 1978. This increase is justified by reference to higher labour and energy costs, both of which are of particular importance to the brick industry. (Prices had remained unchanged since January 1st 1977).

### *20 December 1977. Notification of price increase to the SPK*

In accordance with the company's obligations to give prior notification of planned price increases, Tegelcentralen informs the SPK of its decision of 14 December 1977.

### *23 December 1977. Customers receive new price lists*

Tegelcentralen sends new price lists to its customers informing them of the price increases to take effect from 1 January 1978.

*30 December 1977. SPK requests negotiations. Meeting held between Tegelcentralen and the SPK*

As a result of the company's notified price increases, the SPK requests negotiations with Tegelcentralen. Representatives from the company meet Per-Åke Eriksson and Gun Schulte of the SPK to discuss the planned price increases. The meeting fails to reach any agreement. New negotiations are arranged for 5 January. Tegelcentralen promises to postpone the price increases until after this meeting.

*Postponement of the price increase*

Following these discussions with the SPK, Tegelcentralen sends a letter to its customers in order to inform them of the postponement of the previously announced price rises planned to take effect on 1 January 1978. Negotiations are to continue with the SPK in order to try to settle the disagreement regarding the company's justification of these increases.

*5 January 1978. Tegelcentralen fails to reach an agreement with the SPK*

Representatives from Tegelcentralen – Messrs Baur, Harneman, Persson and Ohlsson – visit the SPK for a meeting with Gun Schulte, Åke Hallman and Olof Pontusson. During the meeting, the representatives from Tegelcentralen attempt to describe the present situation in the company and the industry: almost 70 per cent of the country's brickworks have been forced to close down during the last ten years. The industry's gloomy prospects are largely due to a decline in housing construction and increasing competition from rival products such as light reinforced concrete.

The representatives of the SPK refuse to accept the inclusion of an estimated return on capital and a profit figure in the calculations of Tegelcentralen. Tegelcentralen's representatives reject the argument put forward by the SPK arguing that 'profit' represents a cost as much as any other cost and that, moreover, profit is essential to the company's long-term survival. The meeting fails to arrive at any agreement.

*9 January 1978. Tegelcentralen decides to increase its prices*

The present situation is discussed internally at Tegelcentralen. As a result of these discussions, it is concluded that the main objective of mandatory prior notification is to enable the SPK to monitor price movements rather than as a device to create an artificially low level of prices, as in the case of a price freeze. Although Tegelcentralen has not reached an agreement with the SPK about an acceptable level of price increases, the company should nevertheless implement the previously announced price rises.

### *The SPK and Tegelcentralen's customers receive notification of higher prices*

In a letter, Tommy Harneman (Tegelcentralen) notifies the SPK that the company has decided to raise its prices from 16 January 1978. The tense situation that has arisen between Tegelcentralen and the SPK is evident from the letter's opening sentences: 'As a result of the delicate atmosphere in which our communications are at present being conducted, I have decided to write rather than phone as had been previously agreed.' Tegelcentralen informs their customers by letter of the new prices due to come into force on 16 January 1978.

### *16 January 1978. The Ministry of Commerce writes to Tegelcentralen*

Following the company's announcement of higher prices, the SPK discusses the matter with the Ministry of Commerce. Tegelcentralen subsequently receives a letter from the Ministry of Commerce in which the company is invited to comment on the following report that the Ministry has received from the SPK:

#### **Increases in the prices of bricks**

- 1 The SPK has notified the Ministry of Commerce that AB Tegelcentralen plans to raise the prices of bricks. The Ministry has received the following information from the SPK.
- 2 AB Tegelcentralen, which is the largest seller of bricks in the country accounts for approximately one third of total domestic sales. Tegelcentralen is a sales company that represents the seven brick works operating in southern Sweden. The agreement between Tegelcentralen and the seven brickworks is registered in SPK's list of cartel agreements. According to the SPK, Tegelcentralen is the price leader on the Swedish market. Other brickworks in Sweden usually raise their prices by the same amount as Tegelcentralen.
- 3 On 1.1.1977, Tegelcentralen raised its prices by an average of 12 per cent. The SPK tried to persuade the company to reduce these price increases. It was suggested that the company ought to base its calculations on the situation confronting individual brickworks rather than on a general estimate for the group as a whole. The company admitted that there were weaknesses in its calculations but had not altered the scale of its price increases.
- 4 In a letter received by the SPK on 22.12.1977, Tegelcentralen informed the SPK of its decision to raise its prices by an average of 11.4 per cent from January 1 1978. During a visit to the SPK on December 30 Tegelcentralen presented the material on which the company's decision to increase prices had been based.... The company was also informed that according to the government's supplementary instructions to the SPK, price increases that sought to compensate for anticipated

increases in costs were incompatible with stable prices. Consequently, against this background, the company decided to reconsider the calculations on which its price increases were based. As a result of this reappraisal, Tegelcentralen decided to postpone its proposed price increases.

- 5 During a meeting held at the SPK on January 5 Tegelcentralen presented new arguments to justify its price increases. However, the SPK pointed out to the company that its estimates were still based on average calculations for the group as a whole. For instance, the company cited increases in profit margins and non-compensated increases in costs since 1973 as part of its evidence. These factors – according to the company – accounted for a cost increase of 13.1 per cent. The SPK and Tegelcentralen were finally able to agree that 4.4 per cent, ie approximately a third of the above figure, was attributable to non-compensated increases in costs that had occurred since the company's last price increase in January 1977. In the view of the SPK, the non-compensated increases in costs that had taken place during earlier periods were largely a result of a reduction in volume. On January 12th 1978, Tegelcentralen notified the SPK that it intended to implement the previously announced price increases on January 16 1978.

#### *17 January 1978. Reply from Tegelcentralen*

The Ministry of Commerce receives the following reply from Tegelcentralen:

Following today's telephone conversation, we have the following comments to make with regards to the points raised in 'Increases in the price of bricks'.

Points 1 and 2: None.

Point 3: The copy of the letter dated 9. 1. 1978 indicates that we do not accept that the data is subject to fundamental weaknesses. However, its reliability could almost certainly be improved.

Point 4: The data provided for the SPK showed the result for 1977, increases in costs and revenues for 1978 and the company budget for 1978.... At the meeting that took place on 30.12.1977, the company was told that according to the directives laid down by the SPK, no consideration could be given to estimates of calculated depreciation. In our view this was a quite extraordinary statement and we expressed a wish to adjourn the discussions. However, before this could be brought about, the SPK put forward a request for changes to be made in the data that we had presented in support of our case. Instead of the estimates for costs and revenues, 'pure' cost data was now required. This type of data could then be linked to the older data that had been previously supplied to the SPK.

The chairman of our board, Sven Baur, was then asked to discuss the above SPK directives with your representative, Per Borg. At the same time, our data was to be modified to meet your requests. We were fully aware of the SPK's directives since we had been informed of them by letter on 2.11.1977. Consequently, as suggested after the meeting on 30.12.1977, there was no need to revise our data.

Point 5: During the visit to the SPK on 5.1.1978, Tegelcentralen did not present any



new justification for the proposed price increases. The arguments presented were in fact points of discussion that had been previously raised by Tegelcentralen but were now repackaged to meet the SPK's wishes.... Although an increase in our profit margins would be desirable, our case is actually based on the maintenance of existing margins. There has never been any agreement between the SPK and Tegelcentralen that 4.4 per cent is an accurate reflection of the extent of non-compensated increases in costs since 1.1.1977. The hypothesis presented by the SPK regarding the possible effect of a decline in the volume of production on our figures has not previously been a subject for discussion. Consequently, there has not been an opportunity to present the data shown below....

### *19 January 1978. Price freeze on bricks*

The government introduces a price freeze on facing and building bricks to take effect from 27 January 1978. Prices are frozen at the levels prevailing on 30 December 1977. As a result of this measure, Tegelcentralen's new price list that came into force on 16 January 1978 is replaced by the old price list of 1 January 1977. Tegelcentralen is told verbally by Per Borg, Head of Department at the Ministry of Commerce, that a reduction of the brick industry's losses during 1978 compared to the losses of 1977 must be considered as an unacceptable improvement in the light of the prevailing economic situation.

### *23 January 1978. Tegelcentralen reintroduces the old price lists*

Tegelcentralen informs its customers that it is reintroducing the old price list. The company encloses a newly printed version of this price list.

### *27 January 1978. The brick industry discusses the price freeze*

Representatives from the brick industry discuss the price freeze at the Swedish Brick and Tile Manufacturers' Association in Stockholm. Tommy Harneman from Tegelcentralen is present at the meeting. It is decided to send a delegation to the Ministry of Commerce in order to clarify the industry's present situation.

### *3 February 1978. Delegation from the brick industry visits the Ministry of Commerce*

A delegation from the Swedish Brick and Tile Manufacturers' Association attends a meeting at the Ministry of Commerce. The brick industry is described by the delegation as characterized by small-scale firms 'with an average labour force of around 30 employees and a turnover that does not generally exceed 10 million SEK'. During recent years, a large number of brickworks have been forced to close down. The brick industry is generally regarded to be labour intensive: wage costs account for 38 per cent of the value of sales. The equivalent proportion for energy costs is 20 per cent. Both of these types of

costs have been subject to drastic increases during recent years. With reference to these factors, the delegation urges the withdrawal of the price freeze.

*11 February 1978. Tegelcentralen applies for exemption from the price freeze*

Tegelcentralen applies to the SPK for exemption from the price freeze. The company wishes to raise its prices by 11.4 per cent above present frozen levels to take effect on 20 February 1978.

*17 February 1978. Tegelcentralen discusses its exemption request with the SPK*

Ingvar Persson from Tegelcentralen visits the SPK in order to discuss the company's exemption request. The SPK points out that exemption requests are only granted under 'exceptional circumstances'.

*20 February 1978. Tegelcentralen provides additional data in support of its exemption request*

Tegelcentralen supplements its request for exemption from the price freeze made on 11 February 1978 with the following information:

*Supplementary information to the exemption request of 11.2.1978*

With reference to our visit of 17.2.1978, we would wish to cite the following exceptional circumstances that have arisen as a result of our inability to secure adequate price rises for our products.

*AB Bara Brickworks* A decision on planned investment in machinery and buildings amounting to 1.8 million SEK to take place during the autumn of 1978 is postponed until the company is able to increase its prices.

*Högs New Brickworks AB/AB Helsingborgs Brickworks* An order for a purchase of a new brick machine amounting to 1.1 million SEK due to be delivered in August 1978 will be cancelled unless the company secures an immediate increase in its prices. The company is at present experiencing severe liquidity problems.

Moreover as a result of the strain on liquidity, there is a considerable risk that the company will be forced into liquidation. This would mean the loss of 36.5 whole-year jobs. It should also be noted that with regard to the risk of products being withdrawn from the market, the above company is the sole manufacturer in Sweden of certain types of paving bricks.

*AB Kaniks Brickworks* Planned investment during 1978 of 400 000 SEK is postponed.

*Klippans Brickworks AB* A packaging machine valued at 1.4 million SEK has been ordered for delivery in August 1978. This investment will take place regardless of the outcome of the negotiations on price increases.

*Minnesberg Brickworks AB* A decision on planned investments worth 350 000 SEK to be undertaken during 1978 will be postponed until an adequate price increase can be secured. Freeze on new employment.

*Slottsmöllans Brickworks* Postponement of a 3.6 million SEK investment in new machinery and ancillary buildings planned to take place at the end of 1978.

*Östra Grevie Brickworks AB* Postponement of a 1.5 million SEK investment in new machinery planned to be delivered in the autumn of 1978. The general reason underlying the dependence of investments on your decisions regarding price increases is that companies wish to avoid liquidity problems.

We assume that 'exceptional circumstances' must indicate that a price adjustment has to be made immediately. The question then arises – by how much? As regards this latter question, we would refer you to the data that has been sent to you and to our meeting of 17 February 1978.

#### *29 March 1978. Negotiations between the brick industry and the SPK*

A meeting is held between representatives of the brick industry and the SPK. The brick industry hopes that the parties will be able to reach an agreement that covers all of the companies that have applied for exemption from the price freeze. However, the meeting fails to produce an agreement.

#### *31 March 1978. New negotiations lead to an agreement*

A new meeting is held between representatives from the brick industry and the SPK. Negotiations are conducted by Hallman and Pontusson from the SPK and Ekström and Harneman from the brick industry. An agreement is reached whereby the SPK agrees to a price increase of 6.5 per cent for yellow and red bricks and an increase of 7 per cent for other types of bricks. On the condition that these increases can be implemented immediately, the companies are prepared to hold the new prices for the rest of 1978. In the event of further increases in wages or exceptional increases in costs during 1978 the companies will then discuss possible additional price increases with the SPK.

*4 April 1978. Tegelcentralen is allowed to raise its prices*

The SPK informs Tegelcentralen that it may implement the price increases agreed upon at the meeting held between representatives of the SPK and the brick industry on 31 March 1978.

*5 April 1978. Customers receive information on new price levels*

Tegelcentralen informs its customers that negotiations held with the SPK have resulted in price increases of between 6.5 and 7.0 per cent. The new prices will come into force on 10 April 1978.

*3 May 1978. The price freeze on facing and building bricks is withdrawn*

*Developments after May 1978*

Facing and building bricks were subject to mandatory prior notification between 5 May 1978 and 22 June 1982 and to a price freeze as part of the general freeze on prices in operation during 1980 and 1981. Mandatory prior notification procedures were reintroduced following the general price freeze of October 1982 – February 1983. They were withdrawn in September 1983. Bricks were subject to further price controls under the Price Control Act during 1984, 1985 and 1987.

## 6. Price controls on farm machinery.

### The case of Lilla Harrie Verkstads AB 1974–76

#### **Lilla Harrie Verkstads AB**

Lilla Harrie Verkstads AB was founded in 1890 in an old blacksmith's in Lilla Harrie, a small village north of the town of Lund in southern Sweden. The business was converted into a limited company in 1911. Throughout its existence, the company mainly specialized in the manufacture of agricultural machinery. In the late 1960s, the company was granted a licence by the Swedish Sugar Company for the manufacture of the Hilleshög beet harvester. As a result, turnover doubled in the space of two years. During the latter part of the 1970s, about 90 per cent of the Swedish beet acreage was harvested using Hilleshög machinery. In 1974, the company had 120 employees and a turnover of 24 million SEK. Lilla Harrie Verkstads AB went into liquidation in 1981.

This chapter is based on the correspondence that took place between Lilla Harrie Verkstads AB, the SPK and the Ministry of Commerce and on interviews with Nils Holmqvist, manager of Lilla Harrie Verkstads AB.

#### **Price controls 1974–76**

*11 March 1974. Lilla Harrie raises its prices in anticipation of a future price freeze*

Normally, Lilla Harrie introduces a new price list in October. However, in the spring of 1974, the company raises the prices of its agricultural machinery

since it fears the introduction of a price freeze. However, the price of beet harvesters is not increased since the company considers that the market situation does not permit a higher level of prices.

### *11 September 1974. Introduction of price freeze on agricultural machinery*

A price freeze is introduced covering 'major' agricultural equipment and fertilizers. Prices are frozen at the level prevailing on 2 September 1974. The Ministry of Commerce's press release explains the price freeze in the following manner:

The introduction of a price freeze covering agricultural machinery and fertilisers should be viewed against the background of the substantial increases that have taken place in the prices of these products during recent years. Farmers have thus been confronted with higher costs which have inevitably led to higher food prices for consumers. As a result of the agreement between the government and the farmers which comes into force on July 1st this year, agricultural food prices are directly linked to changes in the most important production costs. It is therefore a matter of national importance that increases in the costs of machinery and other agricultural inputs should, as far as possible, be kept to a minimum.

### *12 November 1974. Lilla Harrie requests exemption from the price freeze*

Lilla Harrie submits a request to the SPK for permission to raise its prices above present frozen levels:

#### *Exemption request*

Due to the increases in costs that have occurred since our prices were last raised on March 11th 1974, the company requests permission to increase its prices as follows:

<i>Type of machine</i>	<i>Percentage increase</i>
Horticultural harrow	11
Long tine harrow	11
Spike tooth harrow	11
Disc harrow	11
Disc implement	11
Tractor-mounted hoe	11
Beet harvester	7.5

We enclose verification of the increases in input costs, applying to 75 per cent of our total purchases of inputs. Approximately 80 per cent of our production in 1975 is subject to the price freeze.

### *Motives for price increase*

Problems of liquidity. We enclose details of our liquidity position and business results as of 5.11.1974. It is evident from these figures that if the company is not allowed to raise its prices, it will be faced with an additional loan requirement, assuming unchanged levels of production, of 2 278 000 SEK at the end of the year. In the company's view, it is not possible to borrow this sum of money through normal channels. A loan could perhaps be arranged on the black market at 100–200 per cent rates of interest but this would inevitably lead to the company's bankruptcy. Another effect of our inability to raise prices would be that our suppliers would consider us to be no longer creditworthy with the result that we would be unable to secure our customary level of credit. As a result we would be unable to meet our liabilities and would be forced into liquidation.

In our view, the company provides a useful service to Swedish farmers and indeed to Swedish society as a whole. Our aim is to produce and develop agricultural machinery that is adapted to Swedish conditions.... Furthermore, we would wish to emphasise that if the company is able to expand its operations, this would have a beneficial effect on productivity and on the working environment. The company would thereby become more competitive and would be able to keep price increases to a minimum. However in order to bring this about, a normal level of profitability must be ensured.

### *Consequences of a possible rejection of this exemption request*

A rejection of the company's exemption request would have the following consequences:

- 1 We would be unable to implement our production plans for 1975.... Accordingly, Swedish sugar beet producers would not be able to obtain the machinery required for the sugar beet harvest.
- 2 A cut-back in production would also have other consequences:
  - lay-off of workers (minutes of the meeting of the Joint Works Council on 8.11.1974 are enclosed)
  - stagnation of the company and an increase in imports
  - sub-contractors who are highly dependent on the company would be badly affected
  - a marked deterioration in security of employment and job satisfaction.

### *A rapid decision is required*

Our products are sold by distributors who are awaiting the outcome of our request for higher prices. Deliveries of machinery to distributors have also been made subject to an increase in our prices. Distributors naturally find it impossible to sell under such conditions. Many farmers wish to purchase equipment before the end of the year. Consequently, if trade is not to be disrupted, it is essential that the company receives a prompt reply to its exemption request.

## Summary

The company was founded in 1890. It is a well-established company with a good reputation. The company accepts responsibility for its employees. The imposition of a price freeze on manufacturers is, in the company's opinion, quite unjustified since the intense competition between manufacturers restricts the scope for price increases.

It is vital to the company's future existence that its request for exemption from the price freeze is met in its entirety. However, the company is prepared to accept immediate increases of 9 and 6.5 per cent respectively in its net prices with the remaining increase to come into effect on April 1st 1975. This arrangement would be implemented even though a wage agreement had not been finalised. A new wage agreement always involves retroactive wage increases. It would not be possible for the company to demand extra payment from our distributors for goods that had already been supplied and invoiced.

Once again, we would wish to emphasise that if the company does not secure an increase in its prices, it would be faced with a borrowing requirement of 2.3 million SEK plus an additional 2.5 to 3.5 million SEK which the company is in danger of being unable to borrow due to the unavailability of extended trade credit. Consequently, the company would find itself in a position where it was obliged to borrow between 5 and 6 million SEK. This is quite impossible. We would hope that you would take account of your heavy responsibility in this matter.

The following 19 appendices are submitted along with the request for exemption: Cost of materials as at 3 November 1974 and 20 September 1974 (13 agricultural implements). Cost of materials as at 1 October 1973 and 1 September 1974 (4 beet harvesters). Documentation verifying costs of materials. Annual reports, 1971, 1972 and 1973. Sales statistics, 1972-1974. Sales budget, 1975. Analysis of balance sheets, 1967-73. Liquidity budget, 1975 of 28 October 1974. Profit and loss budget, 1975 of 5 November 1974. Liquidity budget, 1975 of 5 November 1974. Profit and loss budget, 1975 of 5 November 1974. Long-term planning of 11 June 1974. Long-term planning of 25 June 1974. Letter from the Central Association of Swedish Beet Growers, Ltd. Letter from the Swedish Sugar Co., Ltd. Minutes from a meeting of Lilla Harrie Verkstads works council held on 8 November 1974. Photocopy of a page in *Veckans Affärer* (a Swedish business weekly) dated 6 June 1974. Net price list, machinery 1974-1, dated 11 March 1974. Net price list, machinery dated 11 March 1974. Net price list, Hilleshög harvester, applying from 11 March 1974.

A joint letter from the Central Association of Swedish Beet Growers, Ltd. and the Swedish Sugar Co. Ltd. is also submitted. This letter which praises the qualities of the Hilleshög harvester is concluded in the following manner:

Consequently we would wish to stress the crucial role played by the Hilleshög harvester in the mechanisation of the beet harvest. This machine which has been



specially adapted to meet Swedish conditions is therefore a vital requirement for a successful Swedish beet harvest. We would also wish to emphasize the importance of providing adequate economic support to research and development. In this context, it is essential that the impact of such a programme on the cost of machinery must be viewed in relation to the sizeable benefits that accrue to the industry and to society in general from even a modest improvement in machinery performance.

Malmö, November 11th. 1974  
Central Association of Swedish  
Beet Growers, Ltd.

Swedish Sugar Co., Ltd.

*8 November 1974. SPK requests further information*

SPK requests Lilla Harrie Verkstads AB to submit further information regarding the company's dealer network for harrows and ploughs together with data on the volume of company sales to each of the dealers.

*14 November 1974. Reply from Lilla Harrie*

Lilla Harrie Verkstads AB replies to the SPK's letter of 8 November 1974 by sending more information.

*6 December 1974. SPK requests further information.*

SPK informs Lilla Harrie Verkstads AB that its exemption request is incomplete and asks for additional information regarding the estimated cost-prices of the company's products.

*13 December 1974. Reply from Lilla Harrie*

Lilla Harrie Verkstads AB submits the additional information requested by the SPK. This information comprises three typed pages and 16 pages of cost estimates.

*15 January 1975. SPK grants limited exemption*

SPK informs Lilla Harrie Verkstads AB that it will be allowed to raise the price of its agricultural machinery by 3 to 8 per cent rather than by the 11 per cent which the company had requested. However, the company is not allowed to increase the price of its beet harvesters. No explanation is offered by the SPK for this decision.

According to the estimates made by Lilla Harrie Verkstads AB, the price increases requested by the company would have raised revenue by nearly 2.3 million SEK. On the basis of the price rises granted by the SPK, the company can anticipate additional revenue of around 650 000 SEK.

*4 February 1975. Lilla Harrie appeals to the government against the SPK decision*

Lilla Harrie Verkstads AB appeals to the government against the SPK decision. The joint letter from the Central Association of Swedish Beet Growers and the Swedish Sugar Co. Ltd., dated 11 November 1974, is submitted along with the appeal. Following a description of the background to the appeal, Nils Holmqvist, Lilla Harrie's managing director, states:

The company will be unable to increase its production of beet harvesters without the improvement in profitability that would have been guaranteed by our requested price increase of 7.5 per cent. Consequently, we would be unable to supply Swedish beet producers with harvesters in sufficient numbers to meet the demands of an increased beet acreage. Moreover there will be an inevitable increase in imported beet harvesters which are not wholly suited to Swedish conditions. The rejection by the SPK of our requested price increases will also lead to a delay in planned factory investment. This planned expansion would have enabled the company to increase productive capacity, raise efficiency and improve the working environment. With reference to the above, we thereby submit an appeal against the decision taken by the SPK on 15.1.1975. It is our hope that the Ministry of Commerce will be prepared to reassess this decision and accept the price increases put forward in our exemption request of November 11th 1974, namely an increase of 11 per cent in the price of agricultural implements and 7.5 per cent in the price of beet harvesters.

*3 April 1975. Government rejects appeal*

The Ministry of Commerce ratifies SPK's decision and thereby rejects Lilla Harrie's appeal.

*21 May 1975. Lilla Harrie applies for new exemption from the price freeze*

Lilla Harrie Verkstads AB applies again for permission to raise the price of beet harvesters, disc harrows, disc implements and spike tooth harrows. The company requests a 3.8 per cent increase in its prices to take effect from 1 July 1975.

*17 June 1975. Lilla Harrie provides additional information in support of its exemption request*

Lilla Harrie Verkstads AB provides additional information in support of the exemption request of 21 May 1975. As a new agreement has been reached between the Metal Trades Employers' Association and the Industrial Salaried Employees' Association, the company requests permission to raise its prices by a further 1.7 per cent from 1 July 1975. This price increase will cover those products for which the company has previously requested exemption on 21

May 1975. Together, the two exemption requests comprise a total requested increase of 5.5 per cent.

*11 July 1975. SPK grants modified price increases*

SPK gives partial approval to Lilla Harrie's requested price increases. The company is allowed to raise its prices by 4 per cent rather than by the 5.5 per cent requested by the company. The SPK does not offer any explanation for its decision.

*3 November 1975. Lilla Harrie applies for further exemption*

Lilla Harrie requests the permission of the SPK to exceed current frozen price levels. The company presents the following justification:

As a result of the increases that have taken place in our costs since the last approved price rise (11.7.1975) and taking account of the increases in wage costs, employers' contributions and costs of materials, we request exemption from the current price freeze in order to raise our prices as follows:

<i>Type</i>	<i>Percentage increase</i>	<i>of which changes in construction, per cent</i>
Horticultural harrow	8	2
Spike tooth harrow	7	
Disc harrow	10	1.5
Disc implement	7	0.7
Disc implement TRL 18x2	11	5
Beet harvesters		
B-700	10	3.2
B-700 S	10	3.4
B-701	10	2
B-701 S	10	1.7

Changes in construction have been made in order to improve both the function and the durability of the machines. We enclose a profitability study carried out by the Metal Trades Employers' Association.... Regarding the motive for the price increases: see our exemption request of 12.11.1974. n.b.A prompt decision is essential in order that our dealers can be informed of the prices to be charged.

The following appendices are submitted with the exemption request: annual report of 1974, profitability study of 1974, profit and loss budget of 1975, profit

and loss budget of 1976 including and excluding price increases, as well as preliminary calculations for 1976 including and excluding price increases.

*16 December 1975. SPK grants limited exemption*

The SPK grants limited exemption from current frozen prices not offering any explanation for these percentage increases.

*19 February 1976. Cessation of price freeze*

The price freeze is withdrawn. The following press notice is released by the Ministry of Commerce:

The government decided today to withdraw the price freeze on agricultural machinery from Wednesday, February 25th. The price freeze has been in force since September 2nd, 1974. Commenting on the decision, Kjell-Olof Feldt, Minister of Commerce, emphasized the need for price restraint by producers of agricultural machinery. In taking this decision, the government has assumed that the new prices will be maintained at these levels during 1976. The Minister pointed out that the Price and Cartel Office will be keeping a close watch on price movements in this area.

*Developments after February 1976*

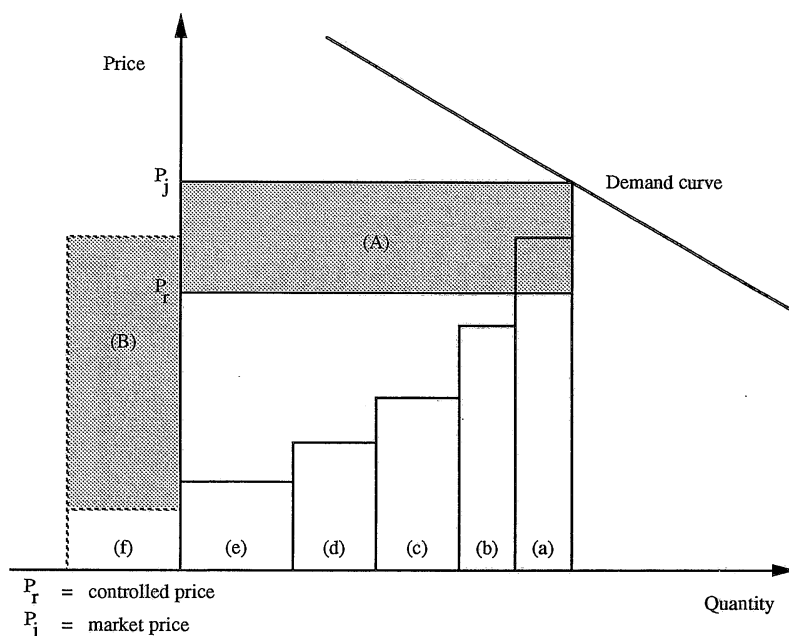
Lilla Harrie's products were subject to the general price freezes that were introduced during 1977 and 1980. Their products were also subject to mandatory prior notification from March 1978. The company was declared bankrupt in 1981. The senior management of Lilla Harrie Verkstads AB stated that the 1974–1976 price freeze was one of the major factors that contributed to the company's bankruptcy.

## 7. Microeconomic effects of price control policy

According to the arguments presented by the companies in the case studies in Chapters 2–6, price controls had far-reaching consequences for companies subject to controls. The aim of this chapter is to try to estimate the actual costs incurred by companies as a result of price controls. These estimates, which are expressed in current prices, have been made with the help of the companies concerned. The microeconomic effects of price control policy are discussed under three separate headings: loss of sales revenue due to price controls, effects on investments and the administrative costs of price control policy.

Figure 7.1 is a convenient point of departure for the analysis of the experiences of the five companies. The figure illustrates the effects of price controls on the revenues and investments of a given industry. The demand for the industry's products is represented by a demand curve while a Salter curve is used to depict the industry's supply side. The different levels of the individual columns along the Salter curve represent the variable costs of each plant (Plants (a)–(e) may be owned by one or several companies). The curve is based on the assumption that the older plants have higher operating costs and less productive capacity than modern plants. Compare the oldest plant, (a), with the most modern plant, (e). It is assumed that planned investment in plant (f), which uses new technology, would lead to lower operating costs than any existing plant.

The area between the current market price,  $p_i$ , and a particular column indicates each individual plant's contribution to capital costs. The more modern the plant, the greater its contribution to fixed costs. At the outset, with the price level at  $p_i$ , all of the plants operate at 'normal' returns. Following the



*Comment:* The levels of the individual columns (forming the Salter curve) represent the operating costs of plants (a) – (e). The area between the price line and each individual column indicates each plant's contributions to capital costs.

**Figure 7.1 Effect of price controls on sales revenues and on investments of an industry**

introduction of a price freeze and the establishment of a new, controlled, price level,  $p_r$ , (lower than the previous market price), the revenues and profitability of all the plants decline. The reduction in sales revenue for the entire industry at the controlled price,  $p_r$ , is indicated by the hatched area (A). As seen from the figure, the oldest plant, (a), is unable to cover even its operating costs. This will lead to its closure and a reduction of the industry's output.

Price controls will also have an impact on the profitability of planned investments. Plant (f) represents a planned new investment using new technology. The hatched area B comprises the plant's capital costs, that is, interest payments, a 'normal' investment return and depreciation. The imposition of price controls makes it impossible for this planned investment to cover its total costs (capital plus operating costs). Accordingly, the investment in the new plant will not materialize. Resources which would have been invested in the price-controlled industry will be reallocated to other branches of industry.

Figure 7.1 offers only a static view – the longer the duration of price control, the greater these effects are likely to be. Compare the above discussion with the analysis related to Figure 9.2, p. 145.

### **Loss of revenue due to price controls**

All of the companies included in the case studies indicated that loss of revenue was the major economic consequence of price controls. This loss of revenue arose as a result of the company charging a lower price (the controlled price) than it would otherwise have done in the absence of price control (the market price). See Figure 7.1. The companies have attempted to estimate this loss of income as the difference between expected revenues from sales in the absence of price controls and actual revenues during the period of price controls<sup>1</sup>. The following picture emerges.

#### *Loss of revenue incurred by Gullfiber AB*

Gullfiber AB estimates that during the price freeze from March 1974–December 1976, the loss of revenue was at least 50 million SEK. This loss of revenue led to a decline in profitability. Indeed this loss of profitability is a recurrent theme in Gullfiber's requests for higher product prices. The longer the duration of the price freeze, the greater the loss of sales revenue. In turn this created a problem of liquidity for the company. On one occasion when Gullfiber found itself confronted with a liquidity crisis, the SPK's representatives suggested that the company ought to sell off some of its assets. Gullfiber's concern regarding the company's financial situation was further increased by the view held by Åke Englund, the SPK's Director General, that loss-making prices did not constitute the 'special circumstances' required for exemption from the price freeze.

#### *Loss of revenue incurred by Siporex AB*

The price freeze on light concrete was kept in force for approximately a year – from March 1974 until April 1975. According to Table 7.1, the loss of revenue suffered by Siporex AB as a result of the price freeze on light concrete amounted to approximately 7 million SEK. The imposition of the price freeze meant that prices were lower than they would have been in the absence of the price freeze. The estimates in Table 7.1 do not take account of the closure of the Södertälje factory on 30 June 1975 with the loss of 200 jobs. The attitude of the SPK to this closure is evident from the memoranda kept by Ulf Linderöth, director of Gyproc, following a meeting held at the SPK.

Attention should be particularly drawn to a remarkable statement made by Mr

Ohlsson (SPK) during the meeting on February 3rd. In his view, the restrictive stance adopted by the SPK on the question of increases in the prices of light concrete had been beneficial. The industry was in need of structural rationalisation. If companies had been allowed to raise their prices as they had intended, rationalisation would have inevitably been delayed.

**Table 7.1 Siporex AB. Loss of revenue (SEK) due to the price freeze on light concrete 1974–75**

Period	Sales (SEK)	Difference between requested and frozen price level (Per cent)	Loss of revenue (SEK)
<i>Non-reinforced products</i>			
15.3.75–8.5.74	2 422 000	11	266 000
1.2.75–30.4.75	3 642 000	12	437 000
		Total	703 000
<i>Reinforced products</i>			
15.3.74–17.5.74	11 607 000	7	812 000
18.5.74–30.6.74	8 341 000	10	834 000
1.7.74–30.9.74	14 458 000	5	723 000
1.10.74–31.1.75	26 355 000	8	2 108 000
1.2.75–30.4.75	20 199 000	9	1 818 000
		Total	6 295 000
Total loss of revenue			6 998 000

*Note:* Table compiled by Siporex AB.

It is difficult to assess whether or not the Södertälje factory would have been able to continue its operations if the price freeze had not been introduced. The primary reason for the closure of the factory appears to have been the decline in the construction industry. However, the price freeze aggravated these pressures and destroyed any chance that the factory may have had to continue its operations.



### *Loss of revenue incurred by MoDo Consumer Products*

The price freeze in 1974 imposed on the household, toilet and sanitary paper products of MoDo-K lasted for approximately four months. However, the company's profitability was affected by price controls over a much longer period, from February 1974 – October 1975, since the price freeze was replaced by mandatory prior notification. The price freeze on baby disposable nappies remained in force for 19 months. According to MoDo-K, this price freeze had a particularly serious impact on company profitability since it came into operation at a time when MoDo-K's economy baby napkins, *Nalle* and *Princess*, were on special offer. However, the SPK rejected the company's application for exemption from the price freeze stating that it did not consider that a temporarily low price level (the special offer) was an adequate reason for a price increase. A limited increase was subsequently approved by the SPK following an appeal by MoDo-K to the Ministry of Commerce. In its written submission, MoDo-K stressed that there was a substantial risk that the company's economy baby napkins could be withdrawn from the market.

The estimates in Table 7.2, which have been made in cooperation with

**Table 7.2 MoDo-K. Loss of revenue (SEK) due to price freezes and mandatory prior notification during 1974-75 and October 1978-January 1979, by product group**

Product group	Loss of revenue (SEK)
1974	
Disposable napkins	2 000 000
Toilet and household paper	1 250 000
Plastic nappy liners	340 000
Other products	100 000
1975	
Disposable napkins	700 000
Toilet and household paper	2 100 000
Total 1974-75	6 490 000
October 1978-January 1979	
Disposable napkins and paper rolls	1 730 000

*Note:* Table compiled by MoDo-K.

MoDo-K's Director of Finance, Olle Sten, indicate that the company lost 6.5 million SEK in sales revenue as a result of the price freeze during 1974–1975. However, in the view of the managing director of MoDo Consumer Products, John Nordlund, the figures presented in Table 7.2 represent a substantial underestimate of the impact of the price freeze on the company's financial position.

During the period 1974–1976, the Scandinavian operation of MoDo Consumer Products suffered a severe setback. In 1977, company profits improved to the extent that the company's return on working assets reached the still unsatisfactory level of 12 per cent (after planned depreciation but prior to the allocation of central costs within MoDo Consumer Products AB and Mo Domsjö AB). The same results were also achieved during 1973. Following the company's expansion programme in the early 1970s, company profitability could normally have been expected to improve during 1974, 1975 and 1976. If company profitability had been maintained at the 1973 level during the years 1974–76, the figures would have been 29 million SEK higher. Price controls accounted for the major share of this difference in company profits. During the period 1974–75, the shortfall in profits exceeded 10 million SEK. Moreover there have been substantial repercussions from price controls. In addition to the actual estimated losses of 6.7 million SEK shown above, account has also to be taken of the following factors:

Informal commitments given to the SPK not to submit further price increases before a certain date.

Due to the decline in profitability, the company has been reluctant to commit itself to product development. This has undoubtedly led to lower profits in subsequent years, particularly in the case of baby napkins and sanitary towels.

Postponement of rational investment opportunities due to uncertainty regarding future profitability.

Requests to increase prices based solely on grounds of costs. It would have been both possible and desirable to have improved profit margins as well.

The failure of MoDo-K and the SPK to reach an agreement on the level of price increases to take effect from October 1978 led to the introduction of a new price freeze on 19 October 1978.

Following negotiations between the SPK and MoDo-K, an 'agreement' was reached in December 1978. According to Table 7.2, the price freeze accounted for a loss of revenue amounting to 1.7 million SEK during the period 22 October 1978 to 14 January 1979. This loss of revenue would have been reduced to 400 000 SEK if MoDo-K had been granted permission to raise their prices by 5.5 per cent. In the company's view, the introduction of a price freeze was a 'punishment', amounting to 1.4 million SEK, imposed by the SPK as a result of MoDo-K's refusal to accept its offer in October 1978.

### *Loss of revenue incurred by AB Tegelcentralen*

A price freeze on facing and building bricks was introduced in January 1978 since Tegelcentralen had raised its prices without having reached an agreement with the SPK. Although the price freeze only lasted for four months, the agreement reached with the SPK at the end of March which abolished the price freeze did not permit Tegelcentralen to charge what the company considered to be the requisite level of prices. Table 7.3 indicates that the estimated costs of the price freeze in the form of a loss of revenue amounted to 2.8 million SEK.

**Table 7.3** Loss of revenue (SEK) incurred by AB Tegelcentralen as a result of the price freeze on facing and building bricks 1978

Period	Sales (SEK)	Difference between requested and frozen price level (Per cent)	Loss of revenue (SEK)
1.1.1978–10.4.1978	11 200 000	11.5	1 288 000
10.4.1978–31.12.1978	34 000 000	4.5	1 530 000
Total loss of revenue			2 818 000

*Note:* The table is based on estimates made by AB Tegelcentralen.

### *Loss of revenue incurred by Lilla Harrie Verstds AB*

In September 1974, a price freeze was introduced covering agricultural machinery. Although this freeze was withdrawn in early 1976, it had a substantial impact on the sales revenue and profits of Lilla Harrie Verkstds AB during 1975 and 1976. This is explained by the fact that the company's production during 1976 resulted from orders received during the final quarter of 1975 and the first quarter of 1976. These orders were undertaken at frozen price levels. On the other hand, 1974 profits were by and large unaffected by the price freeze since that year's production had already been sold at unregulated prices when the price freeze was introduced in September of that year.

It is difficult to make an exact estimate of the lost revenue incurred by Lilla Harrie Verkstds AB as a result of the price freeze. There was frequently a substantial gap between the date on which the order was accepted and the date

of the actual sale. Prices were set at the time of the order but the transaction was recorded at the time of sale. Consequently, different prices could be charged for the same type of machine sold during the same period of time. Moreover the company also made use of a bonus and rebate system for its largest customers.

According to the estimates made in Table 7.4, the loss of revenue due to the price freeze incurred by Lilla Harrie Verkstads AB amounted to 3.7 million SEK during 1975 and 1976 of which 1.6 million SEK was in the beet harvester category, while 2.1 million SEK of lost revenue was in other categories of agricultural machinery. Price controls undoubtedly undermined the company's financial position and thereby paved the way for the company's liquidation in 1981.

The estimates contained in Tables 7.1–7.4 must be treated with considerable caution. They do not provide exact figures of the level of sales revenues in the

**Table 7.4 Loss of revenue (SEK) incurred by Lilla Harrie Verkstads AB as a result of the price freeze on agricultural machinery**

Product	1975	1976	Total
Beet harvester	700 000	900 000	1 600 000
Other machinery	1 200 000	900 000	2 100 000
Total	1 900 000	1 800 000	3 700 000

*Note:* The table is based on estimates made by Lilla Harrie Verkstads AB.

absence of price controls. The tables offer the best assessments that the companies were able to provide.<sup>3</sup> However, the tables do clearly indicate that an immediate effect of price controls was to reduce the revenues of companies subject to the price freeze below levels that would have been achieved if the companies had been able to implement planned price increases. This effect is illustrated by the area (A) in Figure 7.1.

### **Effects on investment**

The above discussion clearly indicates that companies subject to price controls experienced a fall in sales revenues and profits. A decline in profitability tends

to reduce investments too. The five companies covered by this study have attempted to assess the effects of price controls on their investments.

Prior to the introduction of the price freeze on mineral wool in March 1974, Gullfiber AB had planned to invest in its 'T6' line of production at Billesholm. According to the company's original plans, this investment programme would have been completed in time to allow production to get under way at the beginning of 1977. However, due to the introduction of price controls, there was a drastic fall in profitability and the company decided to postpone its investments in 'T6' by 15 months. This postponement of investment in 'T6' led to a 12 month delay in investment in another line of production, 'T9', at the Söråker plant near Sundsvall. The company needed to generate capital for investment in 'T9'. In the light of the personnel available to the company, Gullfiber was only able to expand one line of production at a time.<sup>4</sup>

With regards to Siporex, the price freeze imposed on light concrete led to an accelerated run-down of existing investments resulting in the closure of the factory at Södertälje.

In the case of MoDo-K – see the comments made on the profitability estimates in the previous section – the managing director noted that 'rational investments' had been delayed as a result of uncertainty surrounding the company's future level of profits. However, MoDo-K have not made any specific estimates regarding the effects of the price freeze on investments.

As regards the brick industry, the price freeze which only lasted three months did not lead to company closure or cuts in planned investments. In a letter to the SPK, dated 11 February 1978, Tegelcentralen stated that planned investments would be postponed as a result of the price freeze. However, due to the short duration of the price freeze, the investments were carried out. Any delay in investment programmes must therefore be explained by factors other than the price freeze.<sup>5</sup>

Before the price freeze, the management of Lilla Harrie Verkstads AB intended to carry out a substantial modernization and improvement in the company's working environment. During the price freeze, these investments were postponed owing to a deterioration in company profits and an increase in liquidity problems. These investments were never actually undertaken owing to the decline in the market for the company's products, a factor which substantially contributed to the company's liquidation in 1981.

The price control policy of the 1970s introduced increasing uncertainty into company planning. Companies became uncertain as to whether they were to be subject to price controls and what the 'rules of the game' would be once a price freeze was finally withdrawn. It is reasonable to assume that increased uncertainty regarding future developments exerted negative pressures on company investments.

## **Administrative costs of price controls**

The case studies indicated that companies subjected to price controls incurred substantial administrative costs in the form of meetings with SPK representatives, telephone conversations, letters, preparatory work for meetings, internal discussions regarding price controls and meetings and contacts with branch organizations, competitors, customers, representatives from the Employment service, trade unions, Ministry of Commerce and other authorities. It is inherently difficult to provide exact estimates of these administrative costs of price controls. However, the five companies have attempted to calculate their costs and their estimates are presented in Tables 7.5–7.8. These estimates – as well as the assessment of the impact on profitability – must be interpreted as rough approximations which should be treated with considerable caution.

### *Administrative costs incurred by Gullfiber AB*

The estimated administrative costs of price controls for Gullfiber during 1974–75 are presented in Table 7.5. The costs are distributed between eight items. The first five items comprise the salaries, including payroll taxes, of personnel engaged in administrative work connected with the price freeze. The other three items cover the costs of meetings of the joint works council held during working hours, as well as telephone charges and travel expenditures for meetings held outside Billesholm. The estimated total administrative costs of the price freeze for Gullfiber AB during the period March 1974 – June 1975 were of the order of 600 000 SEK.

### *Administrative costs incurred by Siporex AB*

The administrative costs for Siporex AB of price controls on light concrete during 1974–1975 cover the same items of cost as presented above in the case of Gullfiber AB: salaries for personnel engaged on administrative work associated with the price freeze, telephone charges and travel expenses. According to Table 7.6, the estimated administrative costs of the price freeze for Siporex AB were about 166 000 SEK.

### *Administrative costs incurred by MoDo–K*

The estimated expenditure on price control administration by MoDo–K in 1974–75 was around 250 000 SEK which was equivalent to the cost of  $1\frac{1}{2}$  full-time employees during the period April 1974 – October 1975. Between October 1978 and January 1979, the cost of price controls for the company amounted to 42 000 SEK. Salaries paid to the finance, marketing and managing directors totalled 15 000 SEK while a further 25 000 SEK represented personnel costs in the finance department. The remaining 2 000 SEK was attributable

**Table 7.5. Gullfiber AB's administrative costs (SEK) associated with the price freeze on mineral wool, 1974-75**

Item	Cost breakdown	Cost (SEK)
Salary	Deputy head of marketing (18 months work, part-time (50%) on price freeze)	94 000
Salary	Managing director (3 months work, full-time, on price freeze, 1974-1975)	100 000
Salary	Deputy managing director (9 months work, part-time (33%), on price freeze, March-December 1974. 4 months work, full-time, 1975)	148 000
Salary	Finance director (18 months work, part-time, 1974-75)	100 000
Salaries	Secretary and other office personnel 1974-75	125 000
Meetings of the joint works council	Held during working hours, to discuss price controls	3 750
Telephone charges	At least 500 conversations of, on average, 20 minutes in length	10 000
Travel expenses	Meetings held in Stockholm and Katrineholm. Approx. 40 journeys at 800 SEK per person/journey (air ticket, hotel accommodation, subsistence allowance and taxi)	32 000
Total administrative costs		612 750

*Note:* Figures estimated by Gullfiber AB.

**Table 7.6 Siporex AB's administrative costs (SEK) associated with the price freeze on light concrete, 1974-75**

Item	Cost breakdown	Cost (SEK)
Salary costs	Senior management personnel (800 hours work on price freeze)	75 000
Salary costs	Department personnel plus secretary (1600 hours work on price freeze)	80 000
Telephone and postal charges		3 000
Travel expenses	Meetings with the SPK in Stockholm. Approx. 10 journeys at 800 SEK	8 000
Total administrative costs		166 000

*Note:* Estimates by Siporex AB.

to expenditure on the revision of price lists on 15 and 25 September 1978. In the view of the head of marketing, Rolf Erlandsson, the major problem associated with the price lists was not the actual cost of printing and distribution but the bad public relations involved in charging different prices over a relatively short period of time.

#### *Administrative costs incurred by AB Tegelcentralen*

According to Tegelcentralen, the estimated administrative cost associated with the brief freeze on the price of bricks in 1978 was approximately 38 000 SEK. As seen in Table 7.7, the largest single item of expenditure was on the provision of new customer price lists.

#### *Administrative costs incurred by Lilla Harrie Verkstads AB*

As a result of the price freeze on agricultural machinery, Lilla Harrie Verkstads AB needed to employ one additional member of staff for six months, full-time. The work involved the collection of data and the preparation of written reports to be sent to the SPK. Moreover Nils Holmqvist, director at Lilla Harrie,



estimated that about 30 per cent of his working hours during the period September 1974–February 1976 were concerned with various aspects of price control. In October 1975, Nils Holmqvist estimated that up to that time the

**Table 7.7 AB Tegelcentralen's administrative costs (SEK) associated with the price freeze on bricks, 1978**

Item	Cost breakdown	Cost (SEK)
Salary costs	Senior management personnel (100 hours work on price freeze)	8 000
Printing and postal charges	Information to customers and new customer price lists	18 000
Travel expenses	Meetings with the SPK, Swedish Brick and Tile Manufacturers' Association and participation in a delegation to the Ministry of Commerce (Approx. 10 journeys at 1200 SEK)	12 000
Total		38 000

*Note:* Estimates by AB Tegelcentralen.

company had sent 2.5 kilos of paper to the SPK. In addition, a large number of telephone calls had taken place between Lilla Harrie and the SPK. According to Table 7.8, the total administrative costs were estimated to be around 120 000 SEK.

Tables 7.5–7.8 indicate the estimated additional expenditure that the companies had to bear in conjunction with the administration of price control measures, that is the costs of negotiations and contacts with the SPK and other authorities and organizations, together with expenditure on internal administrative work that arose as a result of price controls. The figures presented in the tables would appear to underestimate rather than overestimate the actual costs of administration. As a result of price controls, senior management had less time for their normal management functions. This qualitative deterioration in the role of management is naturally much more difficult to assess than the figures presented above for the numbers of hours that senior management devoted to the SPK and questions of price control.

**Table 7.8 Lilla Harrie Verkstads AB's administrative costs (SEK) associated with the price freeze of 1974-76**

Item	Cost breakdown	Cost (SEK)
Salary	Managing director (800 hours work on price freeze)	75 000
Salary	Secretary (800 hours work on price freeze)	40 000
Telephone and postal charges		1 500
Travel expenses	Meetings with the SPK in Stockholm (Approx. 5 journeys at 800 SEK)	4 000
Total		120 500

*Note:* Estimates by Lilla Harrie Verkstads AB.

### **The representative nature of the case studies**

The microeconomic effects of price control policy have been illustrated with reference to data from five companies. The question naturally arises regarding the extent to which their experiences are representative of other companies. The five companies have not been selected on a random basis. The choice has been governed by the availability of comprehensive documentation of companies' dealings with the SPK. An additional requirement was that the company in question has been willing to provide access to its records.<sup>6</sup>

Companies subject to price controls can be divided into two principal categories. The first category comprises companies whose prices would, in the absence of price controls, have exceeded the frozen price level. The impact of price controls on revenues, investments etc. would thus depend on the difference between the frozen price level and the higher market price, the duration of the price freeze, the opportunities available to the company to adjust to the price controls, etc. It ought to be evident that the five companies dealt with in Chapters 2 – 6 belong to this first category.

The second category consists of companies whose prices would in the absence of price control have been lower than the maximum or frozen price

levels stipulated by the SPK. Price controls do not thereby represent a direct limitation on the pricing policy of companies within this second category. The two cases may be illustrated with the aid of Figure 7.1, page 107. Companies that fall within the first category are confronted with a controlled price,  $p_c$ , which is lower than the equilibrium or market price,  $p_j$ . In the second case the opposite prevails, i.e. the controlled price exceeds the equilibrium price. In this instance, the price set by the SPK does not act as a restriction on company pricing policy.

Several companies with which the author has been in contact have put forward various reasons in support of the argument that price controls do not present companies with any noticeable difficulties. Company pricing policy has been unaffected since each company has developed methods by which it avoids price controls. In a similar vein, companies have stated that they have had a 'cooperative' relationship with the SPK which has shown 'understanding' of their views. Companies have also stated that, for various reasons, their prices have been lower than the controlled prices set by the SPK. Moreover, the latter has been willing to accept generous price increases. These companies have not been willing to publish – and thereby reveal – their experiences, contacts and techniques. An examination of these experiences would be of interest in this study of price control policy since these companies have successfully avoided the controls.

Following the presentation of the original report on the impact of price controls on Gullfiber to the Price Control Committee, a discussion took place regarding the extent to which Gullfiber could be considered as a representative case. The SPK members of the committee argued that Gullfiber could not be considered to be representative of company experience of price controls. As a result of this discussion, the Government Consultant Organization (Stat-skonsult) was requested by the Price Control Committee to study the effect of price freezes on individual companies in five particular industries: door carpentry, light concrete, fertilizers, electrical household appliances and passenger cars. Selective price controls were imposed on these industries in the mid-1970s, for slightly more than one year.

The study of the Government Consultant Organization, which is summarized in SOU 1982:42, Supplement 12, shows that:

each of the five industries has encountered far-reaching negative effects from the imposition of a price freeze. A decline in profitability was indicated to be the major effect. In several cases, company trading figures indicate severe adverse effects both during and after a period of price freeze. For example, car manufacturers were unable to increase production sufficiently to compensate for the substantial decline in revenue as a result of the price freeze on passenger cars and spare parts. One of the firms studied in this industry estimated that its loss of revenue in 1976 was about 35 million SEK. The experience of individual firms in other industries provides further evidence that price controls have had a negative impact on company profitability.

Regarding the effects on investment, the Government Consultant Organization concluded that:

Our investigations have also indicated that price controls have a negative impact on a company's propensity to invest. The imposition of a price freeze has also increased uncertainty regarding future planning. This will in turn tend to influence the company's willingness to commit itself to particular investment decisions. ...

The report of the Government Consultant Organization also deals with several specific effects of price controls. In at least one instance, the price freeze contributed to a merger. Husqvarna AB suffered a significant decrease in profitability during a price freeze on electrical appliances. Owing to the company's limited export share, it was unable to compensate for domestic losses on foreign markets. Electrolux, a competitor to Husqvarna that occupied a relatively strong position in export markets, was able to take over Husqvarna because of the price freeze.

The report of the Government Consultant Organization provides further support for the conclusion presented on pp 106–111 regarding the negative effects of price controls on the sales revenue of individual companies. However, the Government Consultant Organization did not attempt to assess the administrative costs for individual companies associated with price controls. Nor does the report deal with the bargaining process that evolved between the SPK and the company subject to the price freeze. This bargaining process will form the subject of the next chapter. Several arguments can be put forward in support of the view that the analysis of the microeconomic effects of price controls presented in this chapter is representative for companies whose pricing policy has undoubtedly been restricted by the imposition of price controls.<sup>7</sup>

First, the negative effects of price controls on company profitability that have been discussed in our analysis are also borne out by the Government Consultant Organization's report. Moreover the latter report covers the same period of time and forms of price control as were discussed in the case studies presented in Chapters 2–6. Second, the effects of price control summarized in this chapter can easily be recognized in the numerous empirical studies that have dealt with price controls in a wide range of markets in different countries over different periods of time.<sup>8</sup> Thus the negative effects on profitability and investment can be seen as typical for companies and markets where the price set by the authorities is lower than otherwise would have prevailed. Third, the consequences of price controls discussed here are completely in accordance with the predictions of traditional economic theory with regard to price controls. Finally, the case studies showed that the question of price controls became a matter of concern for the management of the individual companies. The decision of a managing director and his closest associates to devote a substantial part of their time to negotiations and contacts with the SPK must

be seen as an indication that price controls had far-reaching effects on the economic position of individual companies. If this had not been the case, measures of price control would not have received the considerable attention that was devoted to these issues by senior management.

To sum up, this chapter has demonstrated that price controls had substantial effects on the economic positions of individual companies. Their primary effect was to reduce sales revenues since companies were obliged to charge lower prices than they would have done in the absence of price controls. The loss of revenue gave rise to negative effects on investment. In addition, the administrative costs of price controls were not inconsiderable.

## Notes

- 1 None of the companies indicated that costs of production could have been lowered during periods when a price freeze was in operation. On the other hand, the loss of revenue did contribute to a decline in profitability.
- 2 This figure includes MoDo-K's administrative costs with respect to both the price freeze and the mandatory prior notification.
- 3 An alternative method which could be used to estimate the effects of price controls on company revenues is discussed in Chapter 9, namely econometric estimates. However this approach, applied to each individual company, would require a substantial quantitative effort, too large to encompass within the framework of this book.
- 4 It may be thought that Gullfiber would be able to utilize more modern technology and machinery as a result of the postponement of investment. In other words, investment would eventually be more productive than it would otherwise have been in the absence of the delay. However, a number of factors would suggest that this hypothesis is not valid. First, technology remained almost entirely unchanged during this period. Both 'T6' and 'T9' used the same type of equipment that would have been installed prior to the postponement. It is possible that some improvements were made to ancillary plant. However, these improvements would have been introduced in any case as a result of the company's continuous rationalization programme. Furthermore, the investments in 'T6' and 'T9' were carried out under a much tighter time schedule than had originally been planned.
- 5 One of Tegelcentralen's owners, Högs New Brickworks/Helsingborgs Steam Brickworks, closed down during the autumn of 1978. However, the company was in difficulties prior to the price freeze. Its closure was consequently not brought about by the introduction of a price freeze.
- 6 During work on this book, companies have been generally willing to provide access to their records. They have considered that the 'release' of this material would be valuable and allow it to receive a wider distribution. On several occasions, however, companies have been concerned that the publication of company records would lay them open to the charge that they were 'antagonistic towards the SPK'. These companies were worried that this might have repercussions with regard to their future dealings with the SPK. The author allayed these worries by means of four separate arguments. First, the willingness to provide access to company records has not been limited to odd isolated cases. A number of companies have been prepared to 'open up their books' regarding their relations with the SPK. Second, the SPK can hardly intervene retrospectively against a company simply because the latter has published some of its internal records. Third, the publication of a company's experiences would contribute to the discussion of price control issues and to a possible reassessment of this kind of policy. Finally, the very fact that companies have

expressed concern regarding possible 'counter-measures' from the SPK is a clear indication of the need for publication.

- 7 A study by Näslund (1978) is of some relevance in this context. With the aid of a number of interviews, Näslund examined the impact of inflation on companies in England and Sweden. In March 1978, a questionnaire was sent to 71 Swedish companies listed on the Stock Exchange. One of the questionnaire's twenty questions dealt with price controls: 'What are the most important effects of price control?' According to Näslund (1978, p. 143):

Only about ten companies dealt with the effects of price controls. Three companies considered that the controls were rigid, bureaucratic and time-consuming. Two companies stated that the imposition of price controls merely led to a postponement of price increases. As a result, subsequent price increases were introduced in excessively large stages. A further three companies maintained that price controls led to a decline in profitability and to a bias in planning and production.

These comments should be assessed in the light of the fact that only about 20 per cent of companies replied to the question. Näslund does not provide any further, detailed analysis of the effects of price control. However, his conclusions regarding profitability are in line with the above discussion.

- 8) See Schuettinger and Butler (1979).

## 8. Price controls as a bargaining process

A striking feature that emerges from the five case studies analysed above is that price control policy frequently developed into a protracted bargaining process between two parties: the SPK and the companies subject to price controls. The primary objective of the SPK is to hold down price increases. At the same time, the authority does not wish to force companies to lay off personnel or discontinue production. It is also the intention of the SPK to try to avoid an excessive number of appeals to the government being made by companies dissatisfied with the controls. On the other hand, companies that wish to implement price increases are prepared to threaten the SPK with lay-offs of employees and production cut-backs. The negotiations that take place to consider these proposed price increases may be described as:

a process in which two or more parties explore the necessary conditions for the establishment of an agreement. This process is characterised by a series of offers, counter-proposals and subsequent modifications of previously held positions. Another typical feature of this process is that although all parties have an interest in reaching an agreement, there is not the same unanimity with regard to the contents of such an agreement. The bargaining process may either result in an agreement being reached or in an understanding that the necessary conditions for such an agreement do not exist.

In comparison with the market and political decision-making processes, bargaining procedures are less standardized and less strictly governed by pre-set rules and conventions. In a highly developed market economy, buyers and sellers are able to reach an agreement on the basis of a market price. The element of bargaining in this decision-making process is both limited and of an almost trivial nature. Similarly,

standardized procedures for political decisions are feasible within the framework of well-established voting arrangements. Negotiations are more indeterminate and provide a greater opportunity to take account of the various elements encompassed by the bargaining process as well as the interrelationships between these elements and the protraction of the bargaining process over time.<sup>1</sup>

The purpose of this chapter is to examine, in the light of the case studies, some of the central aspects of price control policy viewed as a bargaining process.<sup>2</sup> We start with an account of the behaviour of the Price and Cartel Office. This section is followed by a discussion of company behaviour in the bargaining process. The arguments are summarized in a final section concluding that price control policy led to an extension of the bargaining economy in Sweden.

## **Behaviour of the Price and Cartel Office**

The case studies reveal a number of recurrent features in both the behaviour and arguments presented by the SPK. These features are discussed under the following headings: bargaining tactics, price analyses, and access to information.

### *Bargaining tactics*

Following the imposition of price controls, the first step taken by companies is to apply to the SPK for exemption from the price freeze. On receiving an application for exemption from controls, the SPK frequently requests detailed documentary evidence from the company.<sup>3</sup> The submission of written information to the SPK regarding the company's financial situation may in turn give rise to a request for further documentation. At one stage (12 February 1975), Gullfiber complained that 'the only response that the company has received to its detailed documentation of costs has taken the form of demands for further information'. Demands for written information – and the subsequent delay in dealing with the company's request for exemption from the price freeze – can be viewed as an element in the bargaining process. The aim of the SPK is to postpone a final decision and at the same time utilize the information submitted by the company to justify its own arguments and decisions. Moreover during this period of negotiation, the company's prices remain at the lower controlled level. This is one reason that would explain the SPK's lack of urgency in dealing with company requests for exemption from the price freeze.

Once the SPK has completed its collection of information, a period of time usually elapses before the SPK makes its decision. After a while, companies may demand that their requests for exemption from the price freeze should be treated with greater urgency. During this phase, the company and/or the SPK may initiate direct contacts and arrange meetings. Representatives from the



SPK visit the company in question or vice versa. This part of the bargaining process was shared by all of the companies dealt with in the case studies, with the exception of the smallest company, Lilla Harrie Verkstads AB.

The bargaining process consists of an offer being made by either the company or the SPK which gives rise to a counter-offer being put forward, followed in turn by a new offer and so forth. These negotiations, which also comprise an exchange of information, various promises, compromises and threats, requests for exemption from price controls and appeals against decisions made by the SPK generally become fairly prolonged. On occasions, negotiations break down only to be resumed subsequently by means of new offers or counter-proposals presented directly at a meeting or communicated in the form of a letter or phone call.

A commitment by the SPK to support the abolition of price controls in exchange for an agreement by the company to maintain an unchanged level of prices for some time *after* the removal of the price freeze is a vital part of the bargaining process. These bargaining tactics are illustrated by the case of Gullfiber AB. During the autumn of 1974, the SPK raised the question as to whether Gullfiber would be prepared to agree to an unchanged level of prices during the spring of 1975 if, for its part, the SPK supported 'the abolition of the current price freeze'. It should be noted that the initiative for this proposal was taken by the SPK. Gullfiber made a counter-proposal which was rejected by the SPK. Negotiations between Gullfiber and the SPK continued throughout the spring of 1975 with various 'offers' and 'proposals' being put forward by both sides. In February 1975 the Director General of the SPK, Åke Englund, put forward an offer to Gullfiber in which the company was offered certain price increases in exchange for a commitment by Gullfiber 'to maintain its prices at the same level throughout 1975'. Gullfiber rejected the proposal. Five days later, a new offer was made by Åke Englund which was also turned down by Gullfiber. A new offer was presented by Gullfiber in March 1975 in which the company agreed to withdraw an appeal to the government in exchange for a commitment by the SPK to support the abolition of the price freeze. In June 1975, a new round of negotiations led to an agreement whereby Gullfiber withdrew its appeal and the SPK declared that 'the SPK will support the case for a withdrawal of the price freeze on mineral wool and cellular plastic'.<sup>4</sup>

Similar bargaining tactics were employed by the SPK in their dealings with MoDo-K. The latter accepted a proposal put forward by the SPK regarding the maintenance of an unchanged level of prices for disposable baby napkins until 1 February 1976. In exchange, the SPK committed itself to the abolition of the price freeze on disposable baby napkins. As a result of this agreement, the price freeze was brought to an end.<sup>5</sup>

In October 1978, in response to a request from MoDo-K for exemption from the price freeze, the SPK approached the company in order to discuss the conditions for the abolition of the price freeze. Following a series of negotiations during November – December 1978, the SPK accepted certain price

increases in exchange for a commitment by MoDo-K not to introduce any further price increases during 1979.<sup>6</sup>

In November 1974, Siporex proposed that the SPK should grant exemption from the price freeze by accepting a price increase of 12 per cent in exchange for a commitment by Siporex not to raise its prices before 1 March 1975. In this instance, it was a company that took the initiative with regard to the maintenance of a certain price level. A round of negotiations also lay behind the price rises introduced by Tegelcentralen on 10 April 1978 and the withdrawal of the price freeze on bricks in May 1978. At the end of March 1978, the brick industry and the SPK reached an agreement on the level of price increases to be introduced during the rest of the year. The price freeze on bricks was abolished at the beginning of May 1978.<sup>7</sup>

The SPK frequently adopted the tactic of first reaching an 'agreement' with the company, subject to price controls. This 'agreement' was followed subsequently by the removal or a relaxation of the price controls. In this context, note should be taken of the following quotation concerning the price freeze on bread and flour:

During December 1974, the representatives of the bakery industry and the SPK agreed to propose to the government that price controls in the form of a price freeze should be replaced by a one month period of mandatory prior notification. In exchange thirty of the country's leading bakers agreed, in accordance with section 3 of the Price Control Act, to maintain an unchanged level of prices for the three most popular types of household bread for a period of six months from December 21st 1974. From the same date, the government agreed to replace the statutory price freeze by a period of mandatory prior notification of planned price increases.<sup>8</sup>

The tactic employed by the SPK, whereby agreements were reached on the basis of commitments made by companies for a period of price restraint immediately following the withdrawal of a statutory price freeze, makes it difficult to assess the scale and consequences of price controls. Official statistics on the scale of price control policy underestimate the period of time during which price control measures were in operation. Consequently, the actual scope of price controls tends to be concealed. This type of approach to negotiations employed by the SPK also tends to delay the increases in prices that frequently accompany the removal of price controls. Finally, this tactic indicates that the SPK plays a very active role in the formulation of price control policy. It offers openly, in letters and conversations, to work for the withdrawal of a statutory price freeze. In effect this is also what takes place, that is the SPK as a government agency exerts a substantial influence on the price control policy officially designed by the government.

The 'active' role played by the SPK is also illustrated by several of the case studies. In the cases of Gullfiber, MoDo-K and Tegelcentralen, a compulsory price freeze was actually initiated by the SPK in response to the notification of

planned price increases by these companies.<sup>9</sup> In the view of MoDo-K, the price freeze introduced in 1978 was a result of the company's refusal to accept the proposed price agreement put forward by the SPK. Similarly, the price increases announced by Tegelcentralen, in spite of the lack of any price agreement with the SPK, also led to the imposition of a mandatory price freeze. Consequently, it is difficult for companies to avoid the conclusion that the SPK is responsible for both the introduction and removal of compulsory price controls. As a result, the distinction between price monitoring and legally enforceable price controls is nullified.<sup>10</sup> Furthermore, the bargaining position of the SPK *vis-à-vis* individual companies is reinforced by the impression that the SPK exerts an influence over government policy.

Several other features of the SPK's bargaining position are also of interest in the present context. Enquiries from the SPK in order to establish whether or not a company is prepared to accept an offer are frequently conducted by telephone. Accordingly, the actual extent of the SPK's authority is not fully documented.

The centralization of decision making within the SPK is another feature that emerges from the bargaining process.<sup>11</sup> During their negotiations with companies, officials of the SPK have frequently expressed a need to consult their superiors on various questions. In several cases, consultations involved the Director General, Åke Englund or his closest associate (and successor), Åke Hallman.<sup>12</sup> The need for uniform decisions concerning price controls is probably the principal reason for the centralization of decision making within the SPK. A delegation of authority to the departmental level would tend to increase the risk that a marked divergence would occur between departments regarding the appropriate level for the approval of price increases. This would, in turn, tend to weaken the bargaining position of the SPK. It is in this light that one should view the participation of Englund and/or Hallman in all central decisions regarding exemptions from controls.

In their dealings with the SPK, companies seek to clarify the principles and motives underlying the SPK's assessment of a company's pricing policy and request for exemption from price controls. Generally speaking, the SPK does not provide companies with clear-cut answers on these points. The reluctance of the SPK to reveal the basis on which its policy decisions are made should not be viewed in terms of the impossibility of assessing the 'correct' price but also as an indication of a desire to prevent access to the SPK's deliberations on price policy, thereby possibly undermining the SPK's bargaining position. By withholding information on the rules and guidelines governing price control policy, the SPK is able to strengthen its bargaining position. Companies find themselves unable to cite previous decisions as a precedent or as principles that ought to be applied in a consistent manner.<sup>13</sup>

Officially the SPK wishes to appear as a 'passive' government agency that merely administers in a 'neutral' fashion the decisions taken by government and parliament. According to the terminology used by the SPK, the board

'consults' companies with regard to their pricing policy. However, the evidence of the case studies indicates that the SPK behaves in quite different fashion: the SPK is an extremely active agency. It bargains rather than consults with companies and initiates both the introduction and removal of price controls.<sup>14</sup>

### *The SPK's analysis of price determination*

The SPK employs a historical analysis of price determination in its assessment of the arguments put forward by companies in support of their requests for exemption from price freezes. The SPK's representatives usually concentrate solely on historical costs, profits and rates of return rather than on expected future trends. During our case studies, a long list of demands emerged from the SPK urging companies to provide written evidence on past rather than expected levels of prices and costs. The SPK only accepts 'documented price increases'.<sup>15</sup> The Director General, Åke Englund, pointed out that Gullfiber's profits had been satisfactory during the period 1971-4 and used this argument to counter the company's requested price increase.<sup>16</sup>

In contrast to the 'historical' backward-looking perspective adopted by the SPK, companies are forward-looking. Company planning and price decisions are intimately bound up with future (expected) levels of costs, revenues and profits. In the cases of Gullfiber and MoDo-K, these companies initially maintained a low level of prices in order to introduce new products ('Styrolit' and 'Nalle' disposable baby napkins) on the market. Once price controls had been imposed on these products, the SPK rejected the companies' requests for exemption on the grounds that it did not accept a pricing strategy that was based on product cycle considerations.

Companies wanted to maintain profitability for each of their products in all of their markets. The SPK usually adopted a different approach. Losses on a product subject to price control ought to be compensated by means of profits from the sale of products in markets not subject to price controls, for example foreign markets. A considerable proportion of the time spent on discussions and negotiations with the SPK was due to these fundamental differences in approach to pricing policy.

The commitment of the SPK to historical prices, costs and profits limits the opportunities available to a company to take account of inflation. These effects will be particularly marked when a company wishes to undertake investment. Consequently, the company may need to generate capital by means of borrowing and/or maintaining or improving profitability. At the same time, the general price level is rising. Given these circumstances, price control represents a serious threat to company expansion. (Cf. the discussion on pages 111-112.)

### *The SPK's access to information*

The SPK does not possess as good information as that available to the management of a particular company with regards to its markets, competitive position, productive potential, costs, suppliers etc. The SPK, which has its headquarters in Stockholm, has no opportunity to obtain or maintain the detailed knowledge and information that is available to local management. It is forced to rely on second-hand sources, particularly on information that it receives from the company subject to price control.

It is only natural that companies wish to present their written documentation to the SPK in as favourable a light as possible. The frequent and often-repeated demands made by the SPK for further information should be viewed from this perspective. The Gullfiber case study illustrates that the SPK was placed in an inferior position with regard to access to information. On a number of occasions during negotiations with Gullfiber, the SPK presented incorrect data on costs and production. In the view of Gullfiber's senior management, many of the questions or requests for information raised by the SPK were misleading or irrelevant.<sup>17</sup> As a result of the difficulties involved in monitoring the activities of individual companies, the SPK developed an interest in negotiating with trade associations and other branch organizations.

### **Company behaviour**

A company that becomes the subject of price control endeavours in various ways to strengthen its bargaining position. In negotiations with the SPK, in requests for exemption from price controls and in appeals against decisions taken by the SPK, the company continually stresses that price controls constitute a threat to the company's financial viability, its profitability, employment and investments. The company also emphasizes the risk that particular products subject to price control may be withdrawn from production.

In its assessment of individual companies, employment considerations are of major importance to the SPK.<sup>18</sup> Consequently, in their dealings with the SPK, companies pay particular attention to the negative effects of price controls on employment. In one particular instance, the case of Siporex, the concern of the SPK for the maintenance of employment was reflected in a recommendation to the company to issue notices of redundancy. Against the background of this serious employment position, the company would then be in a strong position to appeal to the government to raise its prices. It was implicit in this strategy that the SPK would support the company's appeal to the Ministry of Commerce.<sup>19</sup> In the case of Gullfiber, the threat of closure, redundancies and limited increases in wages enabled the company to mobilize trade union support in its negotiations with the SPK.

Another method used by companies in order to strengthen their bargaining position *vis-à-vis* the SPK is the recruitment of support from other companies in the industry. This is also illustrated by the case of Gullfiber. In its discussions with the company, the SPK referred to the behaviour of Gullfiber's competitors. In its dealings with Rockwool, for example, the same level of price increases would apply as in the case of Gullfiber. On one occasion, Gullfiber was informed by the SPK that its exemption request would be dealt with once additional information had been received from Rockwool.<sup>20</sup>

The approach adopted by the SPK made it more attractive for Gullfiber to try to get involved in closer cooperation with its competitors than otherwise would have been the case in the absence of price controls. Contacts were actually established between Gullfiber and Rockwool.<sup>21</sup> Together with Rockwool's head of marketing, Gullfiber's managing director had a meeting with the Director General of the National Housing Board. In association with other companies in the building materials industry, arrangements were made for the coordination of negotiations with the SPK and a joint meeting with representatives for the SPK, the National Housing Board and the Ministry of Commerce. Thus, price controls tended to strengthen the incentive for cooperation and coordination within the building materials industry.

A similar picture of cooperation and coordination between companies emerges from some of our other case studies. Siporex got in touch with the trade association of the building materials industry. Representatives from the brick industry met in Stockholm at the Swedish Brick and Tile Manufacturers' Association. During a hearing of the Price Control Committee, the Anti-Trust Ombudsman pointed out that price controls induce 'increased cooperation between companies, eg. the industry-wide coordination of reported price increases to the SPK and a greater degree of certainty regarding the plans of competitors through discussions with the SPK'. Product groups such as radiators, wallpaper, household goods, road haulage, paint, fine paper, sanitary porcelain and chipboard were all examples where the Anti-Trust Ombudsman had found this type of cooperation. (On this point see Appendix 2.)

Companies such as Siporex and Gullfiber that had been the subject of a long-term price freeze also extended their contacts to cover institutions and organisations other than just fellow competitors and branch organizations. Joint works councils and local trade union organizations were also kept informed, meetings were held at the County Labour Board. Politicians and civil servants were also consulted. In the case of Lilla Harrie Verkstads AB, the company's customers represented by the Central Association of Swedish Beet-Growers Ltd. and the Swedish Sugar Co. Ltd. took the apparently surprising step of writing to the SPK in support of a request by Lilla Harrie for higher prices. The letter praised the performance of the Hilleshög beet harvester and emphasized its importance for Swedish sugar beet production.<sup>22</sup>

The case studies presented in Chapters 2–6 point to the conclusion that price controls gave rise to a bargaining process characterized by offers and counter-

offers, threats and promises. This conclusion is also supported by a study by the political scientist Roger Henning regarding the contacts that took place between the senior managers of approximately twenty large Swedish companies and the Swedish government in the mid-1970s. He briefly discusses the contacts between these companies and the SPK:

Price questions were mentioned by ten of the firms interviewed. The contacts were mainly concerned with the SPK's monitoring and administration of price controls. During interviews with senior management, a bargaining type of situation frequently emerged. The price negotiations held between Fortia and Kabi on the one hand and the Pharmaceutical Company AB were special cases. In contacts with the SPK, two particular types of bargaining or quasi-bargaining situations occurred.

Firstly, there is the situation that arose in relation to the price monitoring laid down by the Mandatory Notification Act. Under the directives of this act, the SPK was required to 'consult with companies, organisations and other bodies that have a price-setting function in order to influence pricing decisions in a manner that would benefit consumer interests'. The SPK was also obliged to notify the government immediately if it considered that the Price Control Act should be brought into operation. During 1975 many of the companies in the study negotiated – or to use the terminology of the act, consulted – with the SPK regarding price control policy. These consultations usually originated with the Director General of the SPK who got in touch with company senior management in order to put across the board's point of view. Contacts between companies and the SPK were then delegated to the specialists.

Secondly, bargaining or quasi-bargaining also emerged when a price freeze or a price ceiling on a particular product was withdrawn. This type of decision was frequently preceded by informal consultations which resulted in a commitment by the company to a period of stable prices in exchange for the removal of the price freeze. Quasi-bargaining situations did not, however, usually occur in relation to requests made by companies for exemption from a price freeze. The SPK has the powers to grant price increases that are in excess of the statutory limits in cases where 'exceptional circumstances prevail'. However, the contacts do contain a marked element of attempted persuasion.

In all of these instances, companies frequently make open or concealed threats in order to try to persuade the SPK of the validity of their case. The employment argument would appear once again to be the one most frequently used. On occasions, companies also state that they may be compelled to withdraw their product from production unless their point of view is accepted. However, it would seem to be fairly unusual for a company to state that it would raise the price of another product unless it is allowed to increase the price of the product in question. On the other hand, the SPK is also able to exert various forms of pressure. According to its directives with regard to price monitoring, it is obliged to notify the government if it considers that a price freeze should be introduced. Companies are naturally kept informed on these matters.<sup>23</sup>

Roger Henning interviewed 18 large private companies, none of which is covered by the case studies in Chapters 2–6. His findings, thus based on the

experiences of companies other than those examined here, support the view that the implementation of price controls led to an extended bargaining process.

## Summary

Before 1970, price determination in the Swedish economy was 'free' in the sense that companies were neither compelled to notify price increases to a government authority nor to seek permission in order to alter their prices. The price control policy introduced in the early 1970s gave rise to a prolonged bargaining process whereby the SPK, and private companies, together with a whole range of organizations and authorities, sought to establish a 'correct' price. As previously discussed (see Chapter 1) there is no clear distinction between legally binding price control measures introduced under the Price Control Act and the obligation of companies to notify the SPK about price increases. On numerous occasions, mandatory prior notification gave rise to a bargaining process which in reality constituted an attempt on the part of the SPK to influence company pricing decisions.

The purpose of price control policy is to establish lower prices than would have prevailed in the absence of price controls. A contributory reason for the development of price controls into a bargaining process is that there is no single unambiguous measure of calculation for a 'reasonable' lower price. Similarly, there is no clear straightforward means by which 'justified' price increases can be distinguished from 'unjustified' increases. Hence there is substantial scope for arbitrary decisions on the part of the SPK. When companies apply to the SPK for exemption from price controls or appeal to the government against a decision made by the SPK, the very absence of clear guidelines regarding the 'correct' price allows the various parties sufficient scope to bargain about prices.

The outcome of the price control process depends on the bargaining strength of the parties involved. The greater the resources at its disposal and the more parties that can be mobilized – trade unions, employees, local authorities, industry associations, interest groups, politicians etc. – the greater the likelihood that the company will succeed in pushing through its demands. A large company with substantial bargaining resources and a considerable labour force has a much better opportunity of asserting its interests *vis-à-vis* the SPK than a small company with only a few employees and little influence over groups outside the company.<sup>24</sup>

It might be expected that the measures undertaken by the SPK are solely a question of pricing policy. However, the case studies demonstrate that it is not possible to distinguish questions of pricing policy from issues concerning profitability, employment and growth in these particular companies. Price decisions are directly related to the company's employment position and



investment activity. Consequently, price controls have implications for industrial, regional and employment policy.<sup>25</sup> This makes it easier for individual companies to mobilize an interest in the bargaining process on the part of trade unions, political organizations and other authorities.

A system of centrally-determined and controlled prices is often considered to be a feature of a planned economy. The introduction of price controls in Sweden during the 1970s could be viewed as a step towards a centralized system of price determination in which the SPK acts as both the price-setting and controlling authority. However, as we have seen above, the marked element of bargaining in the Swedish system of price control suggests that Sweden instead moved towards a 'bargaining economy'. According to some economists, this is a type of hybrid that adopts neither the 'free' price determination of the market economy, nor the centrally determined prices of the planned economy.<sup>26</sup> In the opinion of many researchers, the bargaining economy exists, on a substantial scale in Sweden. Wages, rents, farm prices, taxes etc. are largely determined by means of bargaining processes. As a result of the establishment of price controls, the bargaining economy was extended to include price determination in product markets as well.

The argument presented above applies primarily to large companies. The operation of price controls in relation to smaller companies has probably had a stronger element of 'central planning' since their limited bargaining resources have prevented them from exerting much influence over the SPK. It should also be noted that, as a result of the bargaining system, price control policy became more flexible than it would otherwise have been in a system that did not provide opportunities for bargaining. The bargaining processes most likely introduced a greater degree of market adjustment to the system of price controls than would otherwise have been the case.

## Notes

- 1 Höglund and Wadensjö (1983, pp. 187-8).
- 2 This again raises the question of the representativeness of the case studies. A more detailed discussion of this problem is presented in the introduction to Part II and on pp. 117-20. Through contacts with other companies subject to price controls, the author has been able to confirm that the SPK has conducted its operations in a manner similar to that described in this chapter. The central role played by 'consultations', i.e. bargaining, in the implementation of price control policy is clearly shown in SOU 1981:42, Appendix 9. This appendix provides additional support for the arguments and conclusions presented in this chapter.
- 3 For example, Gullfiber 21.3.1974, Siporex 21.3.1974 and 16.10.1974, MoDo-K 4.4.1974, 18.12.1974, 16.7.1975, 29.7.1975 and 1.9.1975, Lilla Harrie 8.11.1974 and 6.12.1974.
- 4 Gullfiber 16.6.1975.
- 5 MoDo-K 16.10.1975 and 22.10.1975.
- 6 MoDo-K 13.12.1978.
- 7 Tegelcentralen 17.2.1978, 29.3.1978 and 31.3.1978.

- 8 SOU 1981:42, p. 343. See also the withdrawal of price controls on building materials (pp. 383-88), fertilizers (p. 424), electrical household appliances (p. 449), road haulage services (p. 504), potatoes (p. 532), canned and frozen foods (p. 550) and on passenger cars and spare parts (p. 579). The page references refer to SOU 1981:42, Appendix 9.
- 9 See Gullfiber 10.1.1974, 5.2.1974 and 8.2.1974, MoDo-K 22.2.1974, 8.3.1974, 2.8.1978, 8.9.1978 and 20.10.1978 and Tegelcentralen 20.12.1977, 16.1.1978 and 19.1.1978.
- 10 Cf. the discussion in Chapter 1 on the relationship between price monitoring and price controls.
- 11 See e.g. Gullfiber 22.10.1974 where Lars Axling (SPK) informs Gullfiber that 'the final decision is always taken by the Director General, Åke Englund'.
- 12 On one occasion, this type of contact had clearly not occurred. On 26 September 1974, Siporex received a verbal assurance that it would be able to raise the price of its reinforced material. The company was informed several days later by the SPK that the Director General had not approved the price increase.
- 13 This feature of bureaucratic behaviour is emphasized by, for instance, Mueller (1980).
- 14 Cf. the discussion on the SPK's role in the framing of price control policy in Chapter 10.
- 15 See e.g. Gullfiber 20.1.1975.
- 16 See e.g. Gullfiber 12.2.1975.
- 17 Gullfiber 22.4.1974, 22.10.1974, 4.12.1974, 9.12.1974 and 18.3.1975.
- 18 See Siporex 13.5.1974 and 13.6.1974.
- 19 See e.g. Gullfiber 22.10.1974, 20.1.1975 and 29.1.1975.
- 20 See Gullfiber 11.9.1974 and 28.11.1974.
- 21 See Gullfiber 29.5.1974 and 11.6.1974.
- 22 Heikensten (1981, p.54) arrives at a similar conclusion.
- 23 Henning (1977, pp.147-8)
- 24 In certain cases, price controls become a question of trade policy. See Chapter 9 regarding the operation of price controls in an open economy.
- 25 The efficiency losses that result from the operation of a bargaining economy are illustrated by Johansen (1979) and Höglund and Wadensjö (1983).
- 26 There is a growing literature on the Swedish bargaining economy, e.g. Henning (1977), Skogh (1982) and Höglund and Wadensjö (1983). Skogh (1982) points to a general trend in the Swedish economy whereby an increasing number of decisions have become negotiable and interest group coalitions easily arise between companies, trade unions and local interests. The bargaining solutions that emerge will depend on 'the relative bargaining strength of the parties involved and on considerations of strategy'. See also Olson (1982) on the role of interest groups.



## PART III

# THE MACROECONOMICS OF PRICE CONTROLS



## 9. Macroeconomic effects of price controls

The purpose of this chapter is to analyse the effects of price controls on the rate of inflation, inflationary expectations, the allocation of resources and the distribution of income in the Swedish economy. An account of the effects in these areas is an essential part of a total assessment of the costs and benefits of price controls. The impact on inflation and inflationary expectations will be dealt with first, followed by a discussion of the effects on the allocation of resources and briefly, on the distribution of income. Subsequently, we will examine foreign experience of price and wage controls during the 1970s. The chapter is concluded with a summary of the principal macroeconomic effects of price control.

### **Effects on the inflation rate**

The literature on price control policy during the 1970s is primarily concerned with stabilization policy issues, that is the effects of controls on the rate of inflation and inflationary expectations. This is a reflection of the standard argument presented in support of price controls, namely that they have both an effect on the rate of inflation and on existing inflationary expectations. By lowering the latter, price controls will thereby exert an influence on the future rate of inflation.

How have price controls affected the inflation rate in Sweden in the 1970s? Firstly, the inflation rate and the degree of price controls tended to rise throughout the decade.<sup>1</sup> (See Appendix 1 and Figure 1.2.) This does not imply

that price controls failed to reduce the rate of inflation. The latter might well have been even higher in the absence of price controls. In order to answer this question, use must be made of econometric models that estimate the rate of inflation that would have arisen if price controls had not been introduced.

The literature on price control policy deals with a number of techniques used to estimate the rate of inflation that would have occurred in the absence of price controls. The technique of simulation offers considerable advantages. The first step is to estimate the central relationships of the inflationary process by means of an equation that describes the determinants of the rate of inflation (the price equation) using data for periods when no controls were in effect. The price equation for the period without price controls is then used to estimate the rate of inflation that would have occurred in the absence of controls. Finally this hypothetical rate of inflation is compared with the actual rate. The difference between the two rates of inflation is taken to provide a measure of the impact of price controls.

Simulations also enable us to examine if and how the effects of price control policy have varied during the period of price control. This is an advantage since there have been marked variations in the extent of price controls during the period 1970–87. Appendix 1 indicates that there were substantial monthly variations in the share of private consumption subject to price controls under the Price Control Act.

A quarterly simulation model of the rate of inflation was presented in a report to the Price Control Committee.<sup>2</sup> It took the form of a quarterly model designed to simulate price movements in Sweden during the period in which price controls were in operation. The model takes account of the impact on inflation during the 1960s and 1970s of a number of factors: the level of and change in capacity utilization, changes in the wage level and in the money supply, the international rate of inflation, changes in sales taxation, inflationary expectations and various seasonal factors.

This model of inflation was first estimated during periods when price controls had not been in force, mainly in the 1960s. According to the estimates, inflationary expectations and the international inflation rate exerted a strong influence on inflation in Sweden.<sup>3</sup> The simulation model was then used to estimate the rate of inflation that would have occurred if price controls had not been introduced during the 1970s. The results indicated that for most quarters there were only small divergences between the actual and the simulated rate of inflation. The price controls implemented during the first half of the 1970s may have had a slight anti-inflationary effect. During the latter part of the decade, price controls were more extensively used. However, during this period, price controls do not seem to have had any clear-cut effect on the rate of inflation.

According to these results, price control policy, that is controls under the Price Control Act and the price monitoring system, did not have any significant long-run effects, in either direction, on the rate of inflation.<sup>4</sup> This result is hardly surprising since wage increases covered by collective wage agreements

were allowed to be fully reflected in price increases. Wage costs represent the largest single item in the overall costs of the industrial sector in Sweden.

As mentioned above, it cannot be ruled out that price controls had a slight anti-inflationary effect when they were first introduced in 1970–71.<sup>5</sup> This result is consistent with the recent stabilization policy theory which suggests that an economic policy instrument has its strongest effect when it is used for the first time, that is when its use is most likely not fully expected. However, firms, organizations and the general public tend to adapt to a continuous application of the same instrument. Hence, in the long run, i.e. after the first price freeze in 1970–71, when firms and the general public had adjusted their expectations and behaviour to price controls, the control system should not be expected to have had any appreciable effect on the rate of inflation.<sup>6,7</sup>

The simulation model described above constitutes the most ambitious attempt hitherto to estimate the effects of price control policy on the rate of inflation.<sup>8</sup> The results are based on the assumption that the econometric model provides a realistic description of the factors that determined the rate of inflation. However, during the 1970s, a series of institutional changes took place, especially on the labour market. This raises doubts about the reliability of a model that was largely estimated using data from the 1960s. The question of the effects of price controls on the rate of inflation in Sweden ought to receive a more definitive answer once further econometric studies have been carried out.<sup>9</sup>

Empirical studies provide scant support for the use of price controls as an instrument of inflation restraint.<sup>10</sup> This is in accordance with traditional theories of stabilization policy where the rate of inflation is treated as an endogenous variable, that is a variable that is determined by the operation of other economic factors. The price level is not an entity that can be controlled directly by the policy makers as for example in the case of tax rates. Hence, the view that price controls should be used to influence the general level of prices finds little support in the main body of economic theory.

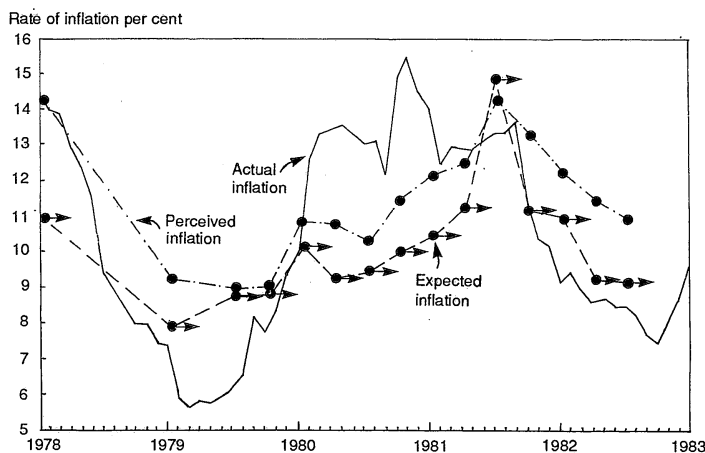
### **Effects on inflationary expectations**

Considerable importance is attributed to inflationary expectations in current research on stabilization policy. Numerous empirical studies have concluded that inflationary expectations exert a major influence on the inflation rate, nominal wage formation, exchange rates and nominal interest rates. The relationship between price controls and inflationary expectations has played a key role in the debate during the 1970s concerning the effects of price controls. In fact, price controls have been proposed as a method of reducing inflationary expectations 'directly', which would in turn lead to a lowering of the rate of inflation.



What have been the effects of the Swedish price controls on inflationary expectations? A comprehensive answer to this question would require access to time series data on the inflationary expectations of the public, covering periods with and without price controls. However, such data was not available towards the end of the 1970s when the Price Control Committee was examining this issue. Consequently, at the request of the Price Control Committee, the Central Bureau of Statistics conducted a public opinion poll in January 1978 of a representative sample of Swedish households comprising approximately 10 000 individuals. The main purpose of this poll was to identify the views held by these individuals with regard to both perceived (historical) and expected (future) rates of inflation. First, the respondents were asked about the rate of inflation they believed to have prevailed during the immediate past twelve months to get a measure of the perceived rate. Next, they were asked about the rate of inflation they expected during the coming twelve months to obtain an estimate of the expected rate.

The poll provided several interesting results. Swedish households held



*Note:* Continuous line denotes actual inflation, the dotted-dashed line, perceived inflation and the broken line, expected inflation. Horizontal arrows indicate future expectations over a period of 12 months. The dates of the interviews are represented by circles.

**Figure 9.1** Actual, perceived and expected rate of inflation 1978–82, annual percentage change

definite views on perceived and expected rates of inflation which they were able to express in quantitative terms. Swedish households firmly believed that an inflationary process was in operation and that it would continue in the future. Econometric estimates indicated a significant relationship between perceived and expected inflation rates. Individuals who considered that the current rate of inflation was relatively high also expected that a relatively high rate of inflation would prevail in the future.<sup>11</sup>

Similar surveys were conducted on a quarterly basis starting in July 1979 under the auspices of the National Institute of Economic Research. The results of these polls are summarized in Figure 9.1 which shows the perceived, expected and actual (observed) rates of inflation expressed as annual percentage changes during the period 1978–82.<sup>12</sup> The expected rate of inflation is calculated as an average of individual estimates.

It is evident from Figure 9.1 that perceived and expected inflation rates adjust relatively sluggishly to fluctuations in the actual rate of inflation as registered by the consumer price index. Perceived and expected rates of inflation appear to have followed the actual rate although the fluctuations are much less pronounced for the perceived and expected rates. Figure 9.1 also illustrates the almost parallel movements in perceived and expected rates of inflation. The figure suggests that the perceived rate of inflation has been the major determinant of the expected rate of inflation. This conclusion is enforced by studies of expectations data covering the period 1979–83, see Jonung (1984).

It is not possible to carry out an entirely satisfactory test of the effects of price control policy on inflationary expectations solely on the basis of the results of the surveys presented in Figure 9.1 as these surveys emanate from a period when price controls were in operation. Data is also needed for periods of no price controls. Nevertheless, Figure 9.1 represents a useful point of departure for a discussion of the effects of price controls on inflationary expectations. By and large, such controls may influence expectations in at least three separate ways.<sup>13</sup>

- 1 Through an influence on the actual (historical) rate of inflation, and then indirectly, via the perceived rate of inflation, on inflationary expectations.
- 2 Through a direct influence on the perceived rate of inflation which will in turn exert an influence on the expected rate.
- 3 Through a direct credibility or information effect on the expected rate of inflation.<sup>14</sup>

The discussion below concerning the first two factors is based on the following line of argument: the actual (historical or observed) rate of inflation affects the

perceived rate, which in turn influences expected and accordingly, future inflation.

### *Influence on the actual rate of inflation*

As discussed on pp. 138–9, the econometric tests of the effects of price control policy on the actual rate of inflation during the late 1970s indicate that price controls did not have any significant long-term influence on the rate of inflation during these years. Hence it seems reasonable to exclude any substantial influence from the first effect.

### *Influence on perceived rate of inflation*

Is it possible that price control policy exerted an independent or direct influence on perceived and thus on expected inflation rates by making the public believe that the rate of inflation was lower than it actually was as registered by the official consumer price index? The numerical values which the respondents assigned to perceived and expected rates (Figure 9.1) do not differ markedly from the actual rate of inflation. Perceived and expected rates of inflation of between 6 and 15 per cent during the period 1978–85 (Figure 9.1) should in fact be regarded as reasonable and realistic viewed against the background of the trend of Swedish and worldwide inflation in the early 1970s and an actual annual rate of inflation in Sweden of between 6 and 15 per cent during the period 1978–85.

Moreover, the difference between actual and perceived rates of inflation is very small when measured as an average for all of the surveys covered by Figure 9.1. In fact, the average difference between the actual rate of inflation and the perceived rate is 1.5 percentage points for the quarterly surveys July 1979 – January 1985, the perceived rate being higher than the actual rate.

A test concerning the rationality of perceptions reported by Jonung and Laidler (1988) actually shows inflationary perceptions to be unbiased predictors of actual inflation. It therefore seems reasonable to conclude that price control policy has not significantly lowered the perceived rate of inflation above or below the level that would have otherwise prevailed in the absence of price controls. Consequently, it is reasonable also to exclude any direct influence.

### *Credibility effects*

In the 1980s, the concept of credibility has gained increasing prominence in American research on stabilization policy. (See for example Schelling (1982) and Taylor (1982).) Both authors contend that a successful government stabilization policy, particularly one which attempts to lower the rate of inflation without any significant increase in unemployment is crucially de-

pendent upon the credibility that the government is able to create for its macroeconomic policy. If a government succeeds in establishing a substantial degree of credibility, the costs of an anti-inflationary policy will be limited. The problem for the authorities becomes one of finding methods that help to establish the credibility of new policies.

This argument concerning the role of credibility may also be applied to price control policy. The actual imposition of price controls could exert a direct influence on inflationary expectations by means of a credibility or information effect that led people to believe that the future rate of inflation would be lower than would have been the case in the absence of price controls. An immediate downward adjustment of expectations would contribute to a lowering of the actual rate of inflation. Accordingly, the introduction or removal of price controls, that is a marked change in the degree of price controls during the period 1977–87, would be expected to have an immediate and ‘significant’ effect on the expected rates of inflation recorded by the various surveys.<sup>15</sup>

The information on inflationary expectations from the surveys carried out between July 1979 and July 1982 is interesting since it provides a continuous time series for this period. The expected rate of inflation varied between 8 and 11 per cent during the three years with the exception of the 15 per cent in July 1981, a level that was substantially above the 11 per cent of the previous quarter. The expected rate of inflation subsequently fell back to 11 per cent in October 1981. This marked jump in inflationary expectations in an otherwise relatively ‘even’ time series was probably attributable to the lively discussion in the media regarding the cuts in food subsidies and subsequent price increases during the summer of 1981.

The relatively small quarterly fluctuations in expectations shown in Figure 9.1 hardly suggest that price controls or indeed any other form of economic policy measures gave rise to sudden, drastic revisions in inflationary expectations – with the exception of the survey conducted in July 1981. However, the latter was not associated with any change in the degree of price control which remained unchanged during the period January 1981 – August 1981, see Appendix 1. Consequently a comparison between the degree of price control in Appendix 1 and inflationary expectations in Figure 9.1 does not indicate any systematic short-run relationship between changes in the degree of price control and changes in inflationary expectations.<sup>16</sup>

Price control policy in Sweden does not appear to have had any direct effect on inflationary expectations.<sup>17</sup> This may be partly attributable to the fact that price controls became a permanent feature of Swedish economic policy during the 1970s and early 1980s without the general public having discerned any reduction in the rate of inflation in comparison with the 1950s and 1960s. In so far as price control policy received any consistent public attention, it would therefore appear to have lost a great deal of its credibility as an instrument of anti-inflationary policy during the 1970s and 1980s.

The relationship between price controls and inflationary expectations can be summarized in the following manner. Price controls have not exerted any long-run influence on either the actual or the perceived rate of inflation. As the actual rate has determined the perceived rate, and the perceived rate has been the main determinant of inflationary expectations, price controls have not exerted an influence on expectations through perceived rates. Similarly, price controls have not had any notable short-run direct impact on inflationary expectations via a credibility effect.

## **Effects on the allocation of resources and the distribution of income**

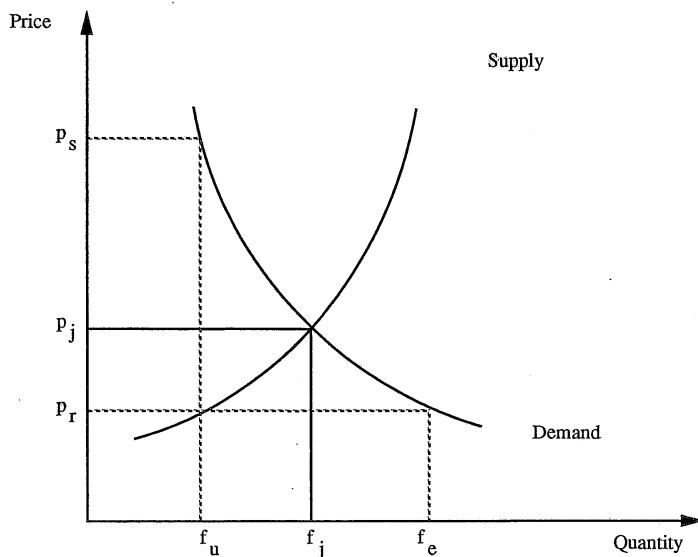
### *The allocation of resources*

The traditional analysis of the effects of price controls on a particular good usually assumes the existence of a competitive market and the establishment of an equilibrium price at the intersection of standard demand and supply curves (see Figure 9.2). At the equilibrium price,  $p_e$ , the quantity,  $q_e$ , is supplied and demanded. The introduction of a price control, in the form of a controlled maximum price at  $p_c$ , lower than the equilibrium price,  $p_e$ , creates a surplus demand ( $q_d - q_s$ ) which is the difference between the quantity demanded at the controlled price,  $q_d$ , and the quantity supplied at the controlled price,  $q_s$ .<sup>18</sup> This excess demand is often described as a 'shortage' of the price-controlled commodity. Hence, a shortage of goods and subsequent queues are consequences of price controls according to Figure 9.2.

There are now purchasers who are willing to pay more than the controlled price. Therefore price controls provide an incentive for the creation of a black market where part of or even the entire output may be sold at prices above  $p_c$ . In the latter case, the black market price will be  $p_s$ .

The prices and quantities of goods produced will depend on the actual form of the price control: the monitoring system, the sanctions imposed on breaches of price controls, the risks of being discovered and so on. Some purchasers may pay more than the initial market price while others may be able to obtain the product at a lower price. However, the latter group will either have to queue or in some other way obtain the product. In the long run, moreover, firms will tend to avoid markets subject to price control, which will inevitably lead to a decline in investment and production in these markets. (See also in this context the discussion related to Figure 7.1.)<sup>19</sup>

Figure 9.2 has been drawn on the assumption that 'other things are unchanged' (*ceteris paribus*). However, each good has specific characteristics in terms of price, after-sales service, guarantees, price discounts, quality, and rights of disposal as well as in terms of the general availability of the good. Price controls will affect these characteristics in different ways dependent on the legal and institutional conditions that apply to the market(s) subject to price



$p_j$  = equilibrium price  
 $p_r$  = controlled price  
 $p_s$  = possible black market price under a system of price controls when the entire output is sold on the black market

*Note:* The figure is based on the assumption that 'other things remain unchanged'. However, price controls give rise to various adjustment processes once they are introduced.

### Figure 9.2 Price control in a single market

control. These dynamic problems of adjustment created by price controls, which have been much discussed in the empirical literature dealing with the operation of price controls in individual markets, necessitate a modification of the *ceteris paribus* assumption underlying Figure 9.2. The latter serves, however, as a suitable starting point for a discussion of the effects of price controls on resource allocation in the Swedish economy.

*Cuts in production and 'shortages'.* Figure 9.2 illustrates that price control on individual goods and services will lead to cuts in production, shortages and

queues. A study of press archive material for the period from the end of World War II up to 1956 provides a series of more or less anecdotal examples of 'shortages' that appeared as a result of Swedish price control policy.<sup>20</sup> Among the newspaper headlines from this period, one finds the following: 'Clothing shortage – childrens' clothes disappear, price control to blame' (*Göteborgs Handels Tidning*, 4 February 1948); 'Paper shortage to continue: Stoppage threatens paper bag factory despite 18 month order book' (*Svenska Dagbladet*, 28 January 1951); 'Paper shortage threatens to delay schoolbooks. Serious blow to printing industry' (*Svenska Dagbladet*, 29 January 1951); 'Serious shortage of nails in their country of origin' (*Sydsvenska Dagbladet*, 21 May 1947). The latter newspaper article continues in the following manner: 'Although there is a general, widespread shortage of Swedish ironware which has been only partially covered by imports, manufacturers are still very reluctant, due to the price freeze, to increase production above minimum levels. In view of the present high levels of import prices and wages, production is just not profitable'. Under the headline 'shortage of iron wire, shortage of chain' (*Sydsvenska Dagbladet*, 2 June 1947), the article reports that

in many places, ironmongers weren't able to supply farmers with a single coil of iron wire for bailing hay. How will our farmers manage if the present long dry period is followed by a wet hay harvest? The shortage of chain will have a catastrophic effect on forestry, one of our most important industries.

'Chocolate cakes disappear, an absurd price policy brings quality manufacture to a halt' (*Sydsvenska Dagbladet*, 9 March 1948). 'Cellulose is in danger again. Production is no longer profitable' (*Sydsvenska Dagbladet*, 7 September 1950). The article continues: 'There has been a shortage of cellulose for several months particularly for baby nappies. The situation may well become reminiscent of the shortages of a few years ago when mothers were forced to queue for a single packet of baby nappies.'

The price controls introduced during the Second World War and up to the mid-1950s were undoubtedly 'stricter' than the controls that came into operation in the early 1970s. However, the effects on output described above apply in varying degrees to all forms of price control that seek to fix a price below the prevailing market price.<sup>21</sup> This is also evident from the examples below which are drawn from the Swedish experience of price control policy during the 1970s and 1980s.

Price controls that endeavour to maintain a domestic price that is lower than the world market price will make it profitable for Swedish producers to sell their entire production on international markets. As a result, the Swedish domestic market will be subject to 'shortages' of the product in question. This may be illustrated with reference to the price freeze imposed on timber products, following the devaluation of the Swedish krona in the autumn of 1982. Production for export became particularly profitable. Following nego-

tiations held between the SPK and the Swedish Sawmills and Timber Exporters Association, the price freeze was relaxed in order, according to a letter sent by the SPK to the Association, dated 18 November 1982, to avoid shortages of timber products on the domestic market:

Price freeze on timber products.

As a result of the negotiations held between the parties and in order to facilitate the operation of the domestic market, the SPK had decided that sawmills... may apply the following maximum prices...

...signed: Olof Pontusson

The SPK states openly that the price freeze imposed on timber products contributed to the 'disruption' of the domestic market.

The price freeze on timber products introduced in September 1973 caused similar problems. Sawmills exported their entire output at the higher world market prices and refused to supply domestic customers at the lower controlled prices. The government was compelled to intervene and authorize supplies to the domestic market. This course of events is described in the report presented by the Price Control Committee (SOU 1981:42, p. 290):

The price freeze on sawn and planed timber was combined with a request to the Ministry of Commerce to monitor the availability of these products on the Swedish market. Any signs of an emerging shortage had to be immediately notified to the Government.

The question of availability of these products on the Swedish market was touched upon in the discussions that representatives of the Swedish sawmills held with the Government during the first half and summer of 1973. Following consultations with the Minister of Commerce in October 1973, the sawmills agreed to supply the Swedish market with adequate quantities of timber for as long as the price freeze was in operation.

The Ministry of Commerce and the SPK devised a special information system in order to monitor the industry's supplies of timber to both the foreign and the domestic market.

Price controls on potatoes that were introduced in 1975–76 gave rise to a domestic price of potatoes that was *lower* than the world market price. Imports of potatoes were subsidized by an amount equivalent to the difference between the world market price and the lower controlled domestic price. Special import allowances were proposed by the Government.<sup>22</sup> However, Swedish potato producers had no opportunity to export their products and obtain the higher world market price. As a result, according to some press reports, a domestic black market in potatoes emerged.<sup>23</sup> /



*Changes in the methods of rationing.* The working of the price system is hampered by price controls. The price mechanism tends to be replaced by or combined with various forms of less efficient rationing. In Chapter 8, as well as in the case studies, it was shown that price control policies tended to develop into prolonged bargaining processes. Negotiations between the SPK and individual companies thus replaced the normal process of price formation that arises when companies change their prices without reference to the orders or wishes of government authorities.<sup>24</sup>

Queueing and black market prices are the 'traditional' forms of rationing that apply to price control regimes. However, the relatively 'moderate' nature of Swedish price controls during the 1970s prevented the creation of permanent queues. A number of markets in the Swedish economy are characterized by queues that have arisen as a result of other forms of price controls than those administered by the SPK, for example the markets for housing, land, day nursery places and higher education. The queues that exist in these markets are the result of price controls that have sought to establish prices below equilibrium prices. They have also created the basis on which both black and grey markets for goods and services may flourish.

The system of price controls imposed on books during the early part of the 1950s provides us with another example of how price controls produce a different form of rationing than that of the price mechanism. The Price Control Board (PKN), the SPK's predecessor, and the Swedish Publishers' Association developed a system whereby book prices were largely determined by the number of words in a book rather than by demand. 'Most novels were treated according to a given norm although exceptions were made in the case of particularly well known authors or new writers' (*Stockholms Tidning*, 4 October 1949). According to Mr Hellman, head of department at the PKN, 'the name of the author should not influence the price of the book'. However, the same spokesman also pointed out that

certain exceptions could be made. One example was the case of the popular author Olle Hedberg whose long books were published at a somewhat higher price than normal. This divergence from the general agreement was naturally due to the higher royalty that the author could be expected to receive. Several other authors were also able to benefit from this exception to the general agreement.<sup>25</sup>

The prolonged price controls on meat products during the 1970s gave rise to a number of 'campaigns' required to sell off meat products that had received too 'high' a price as a result of price controls. Against this background, the campaigns can be viewed as a method of lowering the price of 'non-attractive cuts of meat' below the level specified by the price controls:

One problem in the area of meat products is that a market must be found for all parts of the meat carcass. Changes in the pattern of consumption can therefore present

difficulties and indeed may even lead to a surplus of less attractive parts of the meat carcass. During recent years, consumers have increasingly tended to demand a leaner type of meat product. As a result, it has become increasingly difficult to sell, for example, the fatter types of pork ...

During the price freeze, the SPK has allowed a certain amount of price adjustment to take account of market conditions. According to branch representatives, a much greater degree of price flexibility is required than is available under the present system of control. In their opinion, this lack of flexibility in pricing arrangements is the greatest single problem associated with the price freeze.

According to the meat products industry, this lack of price flexibility has affected the profitability of individual companies. In certain market situations, companies have been unable to charge customers at regulated price levels for the less attractive meat products, while at the same time they have found themselves unable to charge market prices for products that were in high demand. Consequently, the average price of all meat products has, during certain periods, been lower than anticipated by the Government.<sup>26</sup>

As pointed out in Chapter 8, price controls provide an incentive for cooperation between companies that are subject to controls. Thus the operation of cartels or cartel-type organizations is facilitated by a system of price controls. As reported in Appendix 2, the Anti-Trust Ombudsman suggests that a number of companies, in areas of production such as radiators, wallpaper, chipboard, foodstuffs and road haulage services provide evidence of this type of development during the 1970s. The findings of the Anti-Trust Ombudsman can be interpreted in the following way: either prices are regulated which leads to the elimination of traditional competition or free competition is permitted whereby price control would have to be abolished.

*'New' Products.* Another effect of price controls on the supply side is that they make it more profitable for companies to introduce 'new' products whose prices can be determined more 'freely' than is the case with established products subject to price control. This phenomenon is illustrated by Table 9.1 showing how the SPK replied to a question from the cooked meats department of the Swedish Cooperative Union and Wholesale Society regarding the price of a new type of veal brawn. It is evident from this reply that the SPK does not consider the new pork brawn 'to be a new product from the point of view of price controls'.

The same phenomenon is illustrated by the following press cuttings from the early 1950s, which discuss the way in which new producers exploit price controls at the expense of existing producers:

New producers frequently charged prices that were 70-100 per cent above the prices of existing products subject to price controls. A German manufacturer setting up operations in Sweden sold embroidery scissors at 55 SEK per dozen while the PKN refused to allow a Swedish manufacturer to raise the controlled price of 28.84 SEK...

**Table 9.1. Price controls and a new product. The example of veal brawn produced by the Swedish Cooperative and Wholesale Society. (Letter from the SPK to the Cooperative and Wholesale Society)**

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SPK, April 7th, 1976

Cooperative and Wholesale Society, Cooked meats department/Administrative section, Fack 104 65 Stockholm

*Veal brawn, produced in Gothenburg*

On January 11th, 1974, you informed the SPK that you intended to market a new veal brawn product. According to the product's ingredients and the packaging, this product is said to be of a higher quality than other types of veal brawn. Due to new methods of production, this type of brawn will keep much longer. Production of the new product is centralised in Gothenburg.

After due consideration of your written submission, the SPK does not find that this centrally produced veal brawn can be considered to be a new product from the point of view of price control.

Regarding your letter of 28th January 1974, the SPK partially accepts your request that a nationwide price of 18 SEK per kilo (incl. VAT) should be charged for this veal brawn manufactured in Gothenburg. This decision means that a maximum gross price of 19.85 SEK per kilo (incl. VAT) and a net price of 12.25 SEK per kilo may be charged for the above mentioned veal brawn.

Approval by the SPK of the above request does not extend to the regional manufacture of veal brawn.

This decision by the SPK also assumes that it is possible to distinguish veal brawn manufactured centrally in Gothenburg from veal brawn produced elsewhere in Sweden.

An appeal against this decision may be submitted to the Ministry of Commerce within a period of three weeks from your having received this decision.

(signed)

Ulf Dahlsten, SPK

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There is no reason to blame the large number of small manufacturers that flourished in this sellers' market. They simply made use of the opportunity that had been generously and probably unwittingly provided by the PKN. However, from an economic point of view, the result was far from fortunate. Prices were much higher

than would have been the case if the PKN had followed a more sensible policy' (*Göteborgs Handelstidning*, 21 February 1953).

Another serious problem that confronted the price control authority was that of products which varied markedly in quality and type. By altering the character of the product, the manufacturer might well be able to avoid price controls. In this case, price controls would become illusory. The system of price controls imposed on saffron buns (a vital ingredient in the *Lucia* celebrations held in early December) during the 1950s serves as an interesting example of this phenomenon. One month prior to the *Lucia* celebration in 1955, the PKN stated that saffron buns would not be subject to price controls since 'it was not possible to devise a normal price due to the wide variations in the quality of the product' (*Svenska Dagbladet*, 15 November 1955).

In the mid 1970s, the price controls on bread gave rise to far-reaching plans regarding the introduction of a standardized loaf of bread. The price and the actual recipe to be followed were the subject of negotiations between the SPK and the bakery industry. The major private bakers together with the Cooperative and Wholesale Society proposed to the SPK that certain standard types of bread, 'K-loaves' would be introduced on the market provided that the price freeze on bread was removed. Three new variants of the 'K-loaf' were proposed; namely a wholemeal, a standard and a French loaf. However, the SPK demanded that 'a larger standard, sliced loaf should also be produced since this would ensure that the standard types of bread would secure a substantial share of total bread consumption'. However, the bakery industry did not accept these demands and as a result, no agreement was reached, (see SOU 1981:42, pp. 341–3).

*Conclusions.* The initial effect of price controls is to prevent the buyer and seller from freely agreeing on a price. Generally, the parties try to influence other aspects related to the purchase and sale of the product in order to adjust to and/or avoid controls. This may be reflected in a deterioration in after-sales service, the withdrawal of rebates and trade credits, a lowering of quality, a reduction in the supply of the product subject to price control, or the introduction of 'new' products that are sold at prices not subject to controls. (Contingent requirements may be introduced whereby the purchaser of the price-controlled good is also obliged to buy a product that is not subject to price control.)<sup>27</sup>

The authority responsible for the administration of price controls usually takes measures to counteract these effects. As a result, price controls are extended to cover aspects other than the price. For example, the mandatory prior notification that is part of the SPK's price monitoring system requires that companies report not only price changes to the SPK but also any changes that take place with respect to quality, quantity, terms of payment and package size.

Effects of price controls such as a reduction in supply (leading to shortages and queues) and the resources that companies devote in adjusting to and avoiding price controls represent costs to society.<sup>28</sup> As described in the case studies, the bargaining system that evolved between companies subject to controls and the SPK also gives rise to resource costs. Under the same heading, one must also include the resources allocated to the preparation of exemption requests and written replies to the SPK. These costs tend to increase with the duration and stringency of the administrative controls. It should be borne in mind that brief periods of 'moderate' price controls may also give rise to such resource costs. However, their manifestation will not be as evident.<sup>29,30</sup>

### *The distribution of income*

It is difficult to ascertain the effects of price controls on the distribution of income. A general price freeze can be expected to lead to a worsening of the relative position of groups that produce goods which are relatively homogeneous and thereby easily subjectable to price controls. However, this conclusion is dependent on the type of price controls that are adopted and the manner in which these controls are monitored.

As indicated in Chapter 7, selective price controls directed towards a particular industry tend to lower the incomes of both wage-earners and employers in that industry. This explains the joint demands of employers and employees for the removal of price controls in their particular industry, for example the participation of trade union representatives from Gullfiber AB in joint delegations together with the company's senior management.

Another example is provided by the deputy general secretary of the Swedish Confederation of Trade Unions (LO), Kurt Nordgren, who in 1971 considered that the price freeze which was then in force was incompatible with LO's policy towards low-paid workers: 'A wage policy based on solidarity would mean that the prices of certain goods would rise... Consequently the price freeze must be relaxed in order to avoid the imposition of a wage freeze on low-paid workers' (*Arbetet*, 25 March 1971). In December 1973, the deputy general secretary of LO, Lars Westerberg, was openly critical of price control on oil products, arguing that a system of more flexible oil prices would 'protect employment' in industries dependent on oil (see *Dagens Nyheter*, 1 December 1973 under the headline 'Abolition of oil price controls can save jobs').

The history of price controls provides several examples of industries where employers and employees jointly demand that price controls should be abolished in their sector.<sup>31</sup> Nor is it unusual for these demands also to encompass the imposition of price controls in other closely adjacent sectors.<sup>32</sup> For example, during the summer of 1983, members of section 9 of the Paperworkers Union at Värö requested that a price freeze should be imposed on timber and pulpwood.

It is necessary to impose a price freeze on forest raw materials in order to maintain Sweden's competitive position and profitability in the forestry industry. Any future price increases must take account of the need to preserve the competitive benefits of the devaluation. (*Dagens Nyheter*, 12 July 1983).

It is difficult to establish who 'gains' – if anyone does – from price controls. The answer depends on the institutional factors that affect the particular market subject to price controls. A short-term gain, in the form of a lower price than otherwise would have been the case may be temporarily gained by those purchasers who are actually able to get hold of the particular product(s) subject to price control.'

However, in the long run, a decline in output takes place. There may also be a deterioration in the quality and availability of goods subject to price controls. Queues and shortages tend to emerge. The 'lower price' disappears and purchasers run the risk of finding themselves in a worse situation than that prior to the imposition of price controls. Furthermore, there are reasonable grounds for the conclusion that price controls lead to a lower level of aggregate output in the economy. Consequently, all groups in society will receive lower incomes than would have been the case in the absence of price controls.<sup>33</sup>

## The international experience of the 1970s

During the 1970s, almost all OECD countries made use of different forms and combinations of wage and price controls for varying lengths of time. There are numerous econometric studies showing the effects of these measures on the rate of inflation and the rate of increase in money wages particularly in relation to the United States and Great Britain. On behalf of the Price Control Committee, Jan Herin carried out a comprehensive cross-country study of price and wage controls during the 1970s (Appendix 7, SOU 1981:42, pp. 40-41). He summarized these studies in the following manner:

Hence the international experience of legal price and/or wage controls has generally not been particularly favourable. Few serious empirical studies suggest that price and/or wage controls have succeeded in permanently lowering the rate of inflation. The principal negative results that emerge from various studies were the following:

- a) Controls may trigger off price and wage increases prior to their imposition since employers and employees learn to anticipate the introduction of government controls . . . .
- b) Controls may lead to a *higher* rate of inflation (than in the absence of controls) once controls have been withdrawn.

This is principally explained by the fact that government controls are often combined with an excessively *expansionary fiscal and monetary policy*. For

example, a general price freeze may frequently be introduced before an election and thus help to conceal the implementation of an expansionary economic policy.

A general problem associated with controls is that they eliminate the normal macroeconomic warning signals and accordingly provide an incentive for governments to conduct more expansionary policies than they would otherwise have dared to introduce.

- c) Wage and/or price controls may impede the adjustment of *relative prices* and thus prevent the market mechanism from operating properly. Incorrect relative prices may give rise to substantial economic costs as a result of the obstacles that they present to structural change and industrial growth.
- d) Investment activity and the growth of productivity will tend to be lower due to the squeeze on profits imposed by price controls. Accordingly the rate of inflation may actually turn out to be higher at the end of the period of control.
- e) Wage relations may also tend to diverge from market values during periods of wage and/or price controls.

An evaluation of the effects of wage and price controls must take account of changes in economic costs as well as benefits. As we have seen, the benefits would appear to be highly uncertain while there are costs associated with the negative effects of controls on resource allocation. Consequently, it would appear to be highly doubtful whether price and wage controls would yield any tangible long-term benefits.

Following this largely negative assessment of the effects of price and wage controls, i.e. of incomes policy, Herin discussed some of the positive effects that may be induced by such policies:

The following points represent some of the positive aspects that emerge from various studies dealing with price and wage controls:

- a) The costs of these policies must be compared with the costs of alternative anti-inflationary measures.
- b) If incomes policy measures can exert an influence on inflationary expectations, they may have a positive effect; particularly if the measures are combined with a generally restrictive economic policy...
- c) It is possible that statements advocating an anti-inflationary policy may be more effective if they are combined with some form of incomes policy... In this context, an incomes policy may help to make the macroeconomic signals more 'evident' at the same time as they emphasise the serious intentions underlying the policy.
- d) Price and wage controls may be able to eliminate temporary peaks in price and wage behavior....
- e) Incomes policy may be used as a short-term measure to halt inflation and allow decision-makers time to introduce more restrictive demand policies....
- f) Price and wage controls can only be used for a relatively short period of time. The longer that they are in operation, the more difficult it will be to secure their acceptance among wage-earners and employers. The political costs will prove to be excessive. No permanent effects can be anticipated.

Jan Herin is generally critical of the use of incomes policies in industrial countries during the 1970s. However, he did envisage that under certain special conditions, such a policy could dampen inflationary expectations and thereby lower the rate of inflation: this would require that the policy was in operation during a relatively limited period and that it was combined with a restrictive economic policy. Herin also mentioned that the imposition of controls could give the authorities 'time to introduce' more traditional forms of economic policy measures.

Herin's argument has some theoretical validity. However, the problem is that there is little in the way of persuasive empirical evidence to indicate that price and wage controls have produced any benefits, other than in the very short run. Historical experience indicates that controls have usually been in operation for relatively long periods of time. Moreover, they have frequently been combined with an expansionary rather than a restrictive economic policy.<sup>34</sup> According to available data, they have not had any particular success in lowering long-run inflationary expectations. The most detailed studies of the effects of price and wage controls relate to recent American and British experience. Herin concluded that the economic effects of controls in both these countries have been overwhelmingly negative – a conclusion consistent with our findings for Sweden.<sup>35</sup>

## Summary

The primary objective of price controls, according to official statements, has been to reduce the rate of inflation below the level that it would otherwise have reached. However, there is no evidence to indicate that any significant long run reduction in the rate of inflation has taken place. Similarly, price controls do not appear to have lowered inflationary expectations. The effects of price control on the allocation of resources have in several respects been negative. It is difficult to assess the impact that price controls have had on the distribution of income. To sum up, there is no evidence to indicate that price controls have made any clear, positive, long-run contribution to the Swedish economy.

This summary of the macroeconomic effects of price controls should be supplemented by a couple of remarks that help to bring together some of the findings discussed earlier in the book. First, it may appear contradictory to argue that on the one hand price controls have, as we saw in Chapter 7, lowered the rate of price increases in certain companies while on the other hand contending, as in this chapter, that price controls have not had any significant effect on the long-run rate of inflation. However, the coexistence of these apparently contradictory effects may be explained with reference to a number of factors.

The aggregate level of demand in the economy, present as well as expected, is most likely the principal generating force underlying the rate of inflation. It



is determined by factors other than price controls. Under these circumstances, selective price controls of the type adopted in Sweden will tend to raise the prices of goods and services that are not subject to price control in relation to the prices prevailing in the sectors subject to controls. The general price index, which measures the rate of inflation, need not be particularly affected by such a policy. However, price controls will affect the structure of relative prices.

The general price index conceals a number of changes at the microeconomic level. Companies that expect the introduction of price controls may safeguard their profitability by raising their prices earlier than otherwise as a precautionary step. Companies that have been subject to price controls can compensate themselves by raising their prices once price controls have been abolished. This would tend to increase the general level of inflation. At the same time, this upward pressure on prices may be partly offset by the fact that other companies may be subject to selective price controls.

Furthermore, companies whose range of products are only partially subject to price controls may compensate themselves by raising the prices of those products that have not been subject to price control.<sup>36</sup> It is also possible for companies that purchase inputs subject to price controls to temporarily increase their profit margins rather than to allow a possible impact of price controls in the form of temporarily 'lower' prices to be passed on to the customers.

Hence there are a number of factors which may help to explain why selective price controls have led to a decline in short-run profitability for individual companies without, at the same time, having had any permanent measurable effect on the rate of inflation.

The other point which should be borne in mind when attempting to summarize the Swedish experience of price control policy is concerned with the relationship between devaluations and price controls. The five devaluations that took place between 1977 and 1982 were all accompanied by a general freeze on prices. A devaluation should be seen as a form of market-oriented measure. It is intended to improve profitability and create more favourable competitive conditions for domestic industries. If this is to succeed, it is essential that the price mechanism is allowed to function with a minimum of government intervention. However, a price freeze will intervene in this adjustment process and tend to defeat the purpose of the devaluation by limiting the rate of change of domestic prices.

There is accordingly a clear conflict between the use of devaluations and the operation of price controls. However, there has been little discussion or analysis of this policy conflict. On the contrary, a freeze on prices has been considered as a 'natural' part of each devaluation.<sup>37</sup>

## Notes

- 1 A more detailed analysis of the relationship between the degree of price control, the rate of inflation and the political system is presented in Chapter 10.
- 2 See SOU 1981:42, Appendix 10.
- 3 Myhrman (1979) also concludes that these factors are of central importance to the Swedish inflationary process.
- 4 This conclusion accords well with various econometric studies of British and American price control policy in the 1970s.
- 5 It is conceivable that the reduction in inflationary pressure during 1971 – which has been attributed here to price control policy – may be wholly or partly associated with the contractionary policy that was in operation in the early 1970s.
- 6 The Business and Social Research Institute in Stockholm (SNS) carried out a survey in the autumn of 1980 of the inflationary expectations of 30 major industrial companies. The survey concluded that ‘the companies did not consider that price expectations were influenced by the SPK. The measures taken to monitor and control prices would not seem to have had much effect on the rate of inflation.’ This may be partially explained by the fact that companies gradually learned over time ‘to cope with price controls’. This result supports the conclusions above on the effects of price controls, see Bentzel et al. (1980, pp. 57–9).
- 7 This reasoning assumes that price controls were not made more severe than they were initially during the 1970s. A more comprehensive system of price controls subject to rigorous bureaucratic administration would have converted the Swedish economy from a decentralized market economy into an economy governed by bureaucratic controls. It is probable that in such a system, inflation would be ‘suppressed’ rather than ‘open’. Suppressed inflation is characterized by queues, shortages of goods and other forms of rationing of goods and services that would not exist in a traditional price system. This would inevitably undermine the vital information function provided by the price mechanism. (Cf. the discussion on pp. 144–52.)
- 8 Hansson (1983) has also used the simulation model to study the effects of price controls during the period from the first half of 1981 to the first half of 1982 – a period that was not investigated by the Price Control Committee. His results largely coincide with the findings from earlier periods of price controls, i.e. the lack of any significant long-term effect.
- 9 Axell (1979) examined the price freeze that was in operation from October 1970 to December 1971. According to his model, the price freeze did not have a significant effect on the rate of inflation. Price increases that occurred during the price freeze were as large as those that would have taken place in the absence of the price freeze. In addition, Axell found that the rate of inflation *after* the price freeze was higher than it would have been if the price freeze had not been introduced. Axell argues that this pattern of price behaviour suggests that the price freeze in 1970–71 changed company attitudes to the extent that they sought to protect themselves against the risk of a further price freeze by raising their prices by more than was called for in the short term.
- 10 More detailed econometric analyses are available for the British and American experience of price control than is the case for Sweden. Consequently the analyses of British and American price controls provide us with a basis for firmer conclusions (see p. 153).
- 11 A summary in English of the investigation is available in Jonung (1981).
- 12 See Appendix 4 in SOU 1981:41 for a detailed description of the years 1979–80.
- 13 A more comprehensive treatment would deal with other potential effects of price controls on inflationary expectations.
- 14 The first two effects assume that inflationary expectations are based on information regarding past changes in the price level, i.e. they are autoregressive. The third effect assumes that other information exerts an influence on inflationary expectations as well.

- 15 It is assumed here that changes in the degree of price control have symmetrical effects on inflationary expectations, i.e. an increase (reduction) in the degree of price control will lower (raise) inflationary expectations.
- 16 Moreover, the largest reduction in the degree of price control coincided with a fall – not a rise – in inflationary expectations. The degree of price control fell from a level of 77.7 per cent in December 1981 to 1.3 per cent in June 1982. During this period, there was a decline in inflationary expectations.
- 17 Unfortunately there are no data available for the inflationary expectations of the public during the years 1970–71. Such data would have helped to show whether inflationary expectations were affected by the introduction of price controls for the first time since the mid-1950s.
- 18 Price controls will become completely ineffective when a price ceiling is set at a level that exceeds the equilibrium price. In this case, buyers and sellers are free to conduct their transactions at the equilibrium price.
- 19 Figure 9.2 describes a non-inflationary situation. In the event of inflation, the difference in real terms between the lower controlled price and the higher equilibrium price would tend to increase. On numerous occasions, the authority administering price controls has tried to freeze the nominal price at the market price level that prevailed when price controls were introduced. However, as a result of ongoing inflation, the controlled nominal price will be lower than the market price. The final result will thus be the same as that illustrated by Figure 9.2.
- 20 See Lundberg (1953) for a detailed analysis of Swedish price control policy during the latter half of the 1940s.
- 21 This conclusion is supported by the findings of Schuettinger and Butler (1979) in their analysis of the ‘world history’ of price controls. It is tempting to conclude that few types of economic policy measures give rise to such foreseeable effects as those associated with attempts to control prices at levels below prevailing market prices.
- 22 See SOU 1981:42, pp. 527–8.
- 23 See e.g. *Arbetet*, 15 May 1976.
- 24 The inefficiency losses associated with a bargaining system are discussed in detail by Johansen (1979). See also chapter 8.
- 25 A further example of how price controls tend to replace the price mechanism with other forms of allocation (in this case, a lottery) is to be found in a press cutting from *Göteborgs Handelsstidning*, 19 December 1949:

204 people try to buy a car from the Customs. At an auction of goods seized by the Customs in Strömstad, two cars, a 1928 Ford and a 1938 Mercedes, attracted particular attention. The price control committee had set price ceilings of 500 and 2500 SEK respectively. In the event of several bids being made at the price ceiling, a lottery would take place. There were 204 people prepared to bid 500 SEK for the old Ford. The lottery was won by a person from Hälle.

- 26 ‘Price freeze on certain essential foodstuffs - an overview’. (A report from the Ministry of Commerce, DsH 1978:2, pp. 43, 63 and 3:25.)
- 27 For example, Swedish rent controls have led to the sale of dwellings at controlled prices but only on the condition that purchasers were prepared to buy the furniture and fittings at an ‘overcharged’ price.
- 28 The above discussion has dealt with markets characterized by competition. However, the arguments can also be partially applied to markets characterized by varying degrees of monopoly and market concentration.

It is often stated that a high degree of concentration within an industry is associated with inflationary pressures in that industry. Consequently, the regulation of monopolies could

be recommended as a method of countering inflation. However, it has proved difficult to obtain any empirical support for this viewpoint, see Chapter 10, p.180.

If the object of economic policy is to diminish the role of monopolies, priority should be given to the removal of the legally sanctioned obstacles to market entry that help to create monopoly conditions. Price controls are sometimes used as an anti-monopoly measure. However, as such they discourage the establishment of new firms and thereby tend to reinforce industrial concentration.

- 29 This analysis of the effects of price controls on resource allocation has taken the form of a catalogue of negative factors. In fact, this catalogue is probably far from complete. Price control policy can be expected to give rise to other negative effects. However, it is rather difficult to obtain empirical support for these effects. For example, the frequent use of 'special offer' prices in the retail trade in Sweden during the 1970s has been interpreted as a partial consequence of price controls. Companies maintain 'ordinary' prices at a fairly high level as a precaution against possible price controls at the same time as they cut prices in the form of special offers and periodic sales campaigns. It is difficult to obtain information regarding deterioration in quality, the existence of a black market, price rises introduced as a precaution against anticipated price controls etc. These are phenomena which can be expected to have arisen as a result of the price controls introduced during the 1970s. It cannot be expected that either customers, companies, branch organizations or the SPK would be particularly interested in revealing these phenomena. However, it was noted in Chapter 6 that Lilla Harrie Verkstads AB had raised its prices as a precaution against the expected introduction of price controls.
- 30 The experiences of centrally planned economies and economies that were subject to war-time price controls can also be used to illustrate the impact of a comprehensive system of price controls on resource allocation.
- 31 Two examples: The removal of price controls from hairdressing prices in 1956 was described as 'an attempt to meet the demands of both employers and employees for higher profit margins in order to finance higher wage levels in the industry' (*Stockholms Tidning*, 24 March 1956). In the magazine *Mål och medel* published by the Food Processing Industry Workers' Union, the PKN was criticized for 'their one-sided concentration on foodstuffs and certain service industries' (*Stockholms Tidning*, 21 February 1985).
- 32 The above discussion has been concerned with price controls that aim to reduce profitability in a particular branch, i.e. to maintain a price lower than the market price. However, there are also controls that seek to raise prices above the level that would have prevailed in the absence of controls. These controls have helped to raise profitability, promote monopolistic tendencies and contribute to the maintenance of higher wage levels in the controlled sector. For example, both employees and employers in the Swedish postal and telephone services, the government wine and spirits monopoly and in the banking sector have a mutual interest in the retention of such controls. The latter will not be discussed in the present context. Reference could also be made to Swedish agricultural price controls that seek to maintain Swedish farm prices above the price level prevailing on the international market.
- 33 One group that would undoubtedly 'lose' as a result of the abolition of price controls are the employees of the government agency responsible for the administration of price controls. Their self-interest in this matter is discussed in Chapter 10.
- 34 Cf. the discussion on the political economy of price controls in Chapter 10.
- 35 See SOU 1981:42, pp. 206 and 226.
- 36 This may be illustrated by the following example. During the author's interviews with representatives from Findus, it emerged that Findus products sold to catering departments at hospitals and schools etc. were exempt from price controls. However, price controls did apply to the same products when they were sold to retailers.
- 37 A clear contradiction also exists between price controls and the policy of reducing the

budget deficit by increasing prices of public goods and services. The following press cuttings illustrate this conflict.

*Throwing in the towel: a breach of the price freeze*

The withdrawal of the free towel from the municipal swimming baths in the middle of the current price freeze is not allowed.

On Thursday, the County Administration Board's prices unit informed the Leisure Services Department in Trollhättan that the former charge of 5 SEK for entry to the swimming baths would be reintroduced on Friday and that it would include the use of a towel. The Leisure Services Department had raised a number of its charges on January 1st, decisions that had been made in June or November last year. The purpose of this was to raise a further 300 000 SEK in order to meet the stringent savings requirements in the municipal budget. (*Dagens Nyheter*, 15 January 1983.)

*Concealed increases in office canteen prices*

A concealed increase in office canteen prices has taken place in spite of the general price freeze. This statement is made by the SPK following a decision of the District Health Board of Kristianstad County Council to withdraw the dessert from the canteen menu for hospital staff.

The County Council had counted on making considerable savings. An assessment of this measure will now be conducted by the County Administration Board (*Dagens Nyheter*, 18 January 1983).

## PART IV

# THE POLITICS OF PRICE CONTROLS



# 10. Price controls and the political system

This chapter examines the political economy of price controls, that is it studies the mechanisms in the political system that have contributed to the use of price controls as an instrument of economic policy. Following this account, the factors that influence the selection of goods and services subject to price controls are considered. Finally, an assessment is made of the role of the SPK in Swedish price control policy.<sup>1</sup>

## **The political economy of price controls**

Economic theory and empirical investigations suggest that price controls are an inefficient method of lowering the inflation rate. The question then arises as to why price controls have been so widely used, both in Sweden and other countries, during the 1970s and 1980s.<sup>2</sup> What are the political processes that prompt governments to impose price controls when such measures do not appear to exert any significant short-run or long-run influences on the rate of inflation? The answer to this question should be sought in the incentive structure of the political system.

### *The demand for controls*

Table 10.1 presents the results of a number of opinion polls, carried out by the Swedish Institute of Public Opinion Research (SIFO), during the period 1979–82, into public attitudes regarding price and wage freezes and rising



prices. The opinion polls indicate that the respondents viewed inflation in mainly negative terms. During the election years 1970, 1973 and 1976, between 80 and 86 per cent of those questioned were 'very worried' or 'fairly worried' about inflation. Prior to the 1976 and 1982 elections, many of the respondents stated that inflation, price freezes, and prices and wages were highly important political questions.

Table 10.1 shows that an overwhelming majority – four out of five respondents – desired a price and wage freeze, irrespective of political and trade union affiliations. According to the results of the polls carried out in 1972 and 1980, opinion in favour of a price and wage freeze remained remarkably constant. In June 1971, 82 per cent supported a price and wage freeze whilst in October 1980 the figure was 83 per cent.

However, it is uncertain whether these high figures can be altogether interpreted as a 'yes' in favour of the use of price and wage controls as an instrument of economic policy. They could be seen as reflecting the desire of the majority for an end to rising prices and wages. (See the interviews of June 1972, October 1980 and April–May 1981.) It is also possible that some of the respondents expressed a desire for unchanged levels of wages and prices rather than support for a freeze on prices and wages as a measure of economic policy.<sup>3</sup> The percentage of positive replies is somewhat lower when the question is phrased in terms of the use of a price and wage freeze as a counter-inflationary measure. In February 1981, 76 per cent of those questioned 'believed' in a price and wage freeze while 61 per cent would have chosen this measure if they had been in government. Several months later, in April–May 1981, the introduction of a wage and price freeze was the most popular economic policy option being favoured by 64 per cent of those interviewed.<sup>4</sup> Table 10.1 also indicates that in February 1981, a higher proportion of the respondents believed in the combination of a price and wage freeze (76%) than solely a price freeze (58%) or a wage freeze (45%).

Hence a freeze on prices and wages, in whatever form, must be seen as a highly popular measure. Gallup polls in the USA during the 1970s produced similar results: the American public wanted wage and price controls to be implemented when such measures were not in operation. If controls on wages and prices were already in force, the American public considered that they should be made more restrictive.<sup>5</sup>

### *The supply of controls*

According to the opinion polls in Table 10.1, there appears to be strong demand by voters for price and wage controls. Consequently, the introduction of such measures seems to be politically advantageous. Moreover, controls have certain attractive features from a political point of view: they can be put into effect immediately. Hence a government can create an impression that it is acting – taking positive steps. The general public receives a clear unequivocal

**Table 10.1 SIFO opinion polls on price and wage controls and inflation**

Time of interview	Question/answer		
June 1972	<p><i>Question:</i> 'The introduction of a price and wage freeze could be one possible method of limiting price increases. Which would you prefer, no price freeze and a general increase in wages or a price freeze and no general wage increase?'</p>		
<i>Answer:</i>	Total %	Non-socialists %	Socialists %
No price freeze – general wage increase	7	6	9
Price freeze – no general wage increase	82	83	81
Can't tell	11	11	10
March 1976	<p><i>Question:</i> 'There is an election in September. Which political issue is of greatest interest to you? Choose three issues which interest you most.'</p> <p><i>Answer:</i> A quarter of those interviewed state that prices i.e. questions on inflation (13.7%) and on a price freeze (11.3%) is one of the three most interesting questions in the election. ('Employment', 'the environment', 'taxation', 'social welfare' and 'law and order' were questions that obtained higher percentages.)</p>		
April/May 1976	<p><i>Question:</i> 'How worried are you about rising prices?' The same question was asked prior to the elections in 1970 and 1973. The following table compares the answers given during the three election years:</p>		
	April 1970 %	April 1973 %	April 1976 %
Very worried	47	26	29
Fairly worried	39	56	51
Not at all worried	13	16	17
Uncertain	1	2	3

October 1980      *Question:* 'Would you prefer a price and wage freeze to the present rate of inflation?'

Members of:

<i>Answer::</i>	Total %	LO %	TCO %	SACO/SR %
Yes	83	84	83	73
No	9	9	12	18
Uncertain				
Don't know	7	7	5	8

February 1981      *Question:* 'There is a lot of discussion about the different measures that could be taken to improve the Swedish economy. Which measures have you heard about? Which of the measures that you have mentioned do you yourself believe in? If you were the government and were able to choose one of the measures that you have just mentioned in order to improve the state of the Swedish economy, which measure would you choose?'

<i>Answer</i>	Heard about %	Of which I believe in personally %	I would choose if in government %
Lower marginal taxes, tax reform	23	46	32
Price freeze	15	58	42
Wage freeze	16	45	32
Joint price and wage freeze	14	76	61
Increase in interest rates	17	17	8
Increase in savings	16	43	25
Savings in public expenditures	12	52	24
Devaluation	12	18	15

April/May 1981      *Question:* SIFO distributed a card containing nine suggestions for the programme of economic austerity that had been discussed during the winter and spring and asked the question: 'Which of these proposals do you consider is desirable for the country's economic policy?' Only 6 per cent of those interviewed thought that the question was too difficult and declined to answer. The others suggested on average three proposals.

*Answer:* The three most popular answers were the following:

	%
Introduce wage and price freeze	64
Prohibit credit cards	57
Lower marginal rates	47

A further six alternatives were proposed, all of which received less support.)

January/  
February  
1982

*Question:* 'A general election will be held in September. Which political issue do you find most interesting?' The interviewed person could choose up to five possible subjects.

*Answer:* In the opinion of the voters, prices, wages and economic policy was, next to employment, considered to be the most important question. It was mentioned by 41 per cent of those interviewed.

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*Notes*

The interviews usually comprised between 1000 and 1200 randomly selected individuals.

LO: Confederation of Trade Unions

TCO: Central Organization of Salaried Employees

SACO/SR: Confederation of Professional Associations

statement of government intent: an unpopular inflation will be halted by government sanctions. Furthermore, controls on prices and wages are 'cheap' to introduce. They do not involve the government in any significant financial burden. These factors would appear to have exerted a major influence on the supply of price controls in both Sweden and many other countries.

The argument outlined above is confirmed by the American experience from the early 1970s of the price and wage controls introduced by President Nixon. Drawing on the latter's memoirs, Appendix 4 shows how the pressure to 'do something' about an unpopular inflation forced President Nixon – a longstanding opponent of controls on wages and prices – to introduce these very same controls. As a result of political pressures, the demand for price and wage controls gave rise to the imposition of a programme of controls that won immediate support from the American public. The subsequent abolition of these controls proved to be much more difficult. Two of President Nixon's

closest advisors, Herbert Stein and George Schultz, also confirmed (see Appendix 4) that the introduction of price and wage controls was due to short-term political considerations.

Price control policy yields immediate political gains whereas the political costs do not become evident in the short run.<sup>6</sup> Moreover these costs are often difficult to identify as the consequence of price controls. A policy of restraining aggregate demand that aims to reduce the rate of inflation produces the opposite time sequence of political costs and benefits. A contractionary, counter-inflationary strategy often results in rising unemployment in the short run whereas the fall in the rate of inflation tends to occur later. Hence voters/ the general public usually associate the introduction of a 'traditional' policy of economic restraint with increasing unemployment and an unchanged or possibly rising rate of inflation. This is hardly a desirable situation for a government, particularly prior to an election. Thus, price controls have obvious political advantages in comparison with a restrictive stabilization policy. Indeed price controls can be used to conceal an expansionary economic policy that will in the long run tend to increase the rate of inflation.

The short-run popularity of price controls among voters and politicians is most likely the major reason for the use of price controls in Sweden between 1970 and 1987. However, the degree to which price controls have been used varies markedly from year to year as displayed in Table 10.2, which measures the extent of legally binding price controls as the 'degree of price control'. How can these annual variations be explained? Two hypotheses will be considered here. Firstly, according to the election hypothesis, price controls are used for reasons of electoral tactics. According to the second hypothesis, here termed the inflation hypothesis, price controls are a reaction to a rising rate of inflation. The higher the rate of inflation, the greater the use of price controls.<sup>7</sup>

### *The election hypothesis*

Since the early 1970s, economists have examined formal models of the relationship between the economic and the political systems. The theory of the political business cycle has attracted much attention. This theory typically assumes that voters assess the performance of the government on the basis of the prevailing economic situation. In other words, governments are held responsible for economic development as measured by the rate of inflation and the level of unemployment. It is often assumed that the government attempts to control inflation and unemployment in a manner that would maximize its chances of re-election. Hence a relatively expansionary economic policy would be pursued during the year of an election. This would tend to lower unemployment and raise the rate of inflation. According to this model, stabilization policy will become more restrictive *after* an election since the inflation rate would need to be reduced before a more expansionary policy can be adopted prior to the next election. This hypothesis also assumes that

**Table 10.2 Degree of price control, rate of inflation and electoral periods 1969–83**

	Year	Degree of price control %	Rate of inflation %
	1969	0.0	2.8
Election	1970	20.9	6.8
	1971	54.0	7.6
	1972	0.0	5.9
Election	1973	8.7	6.7
	1974	14.0	10.1
	1975	12.3	9.8
Election	1976	14.0	10.1
	1977	30.6	11.5
	1978	59.7	10.0
Election	1979	56.1	7.0
	1980	51.1	13.7
	1981	45.0	11.0
Election	1982	30.0	8.6
	1983	29.3	9.0
	1984	22.3	8.0
Election	1985	32.4	7.4
	1986	0.0	4.2
	1987	69.0	4.2

*Source:* See Appendix 1.

*Notes:* The degree of price control measures the proportion of total consumption of goods and services subject to controls based on the Price Control Act, expressed as an annual average of monthly data. If price monitoring is also included in the degree of price control, almost all private consumption with the exception of housing was subject to price controls.

The rate of inflation is measured by the change in the annual average of monthly figures.

political competition prevails within a democratic system subject to general elections held at regular intervals.

An economic policy based on the above model would in theory give rise to politically determined cyclical fluctuations, i.e. to electoral cycles. It is an

open question to what extent the stabilization policies of modern industrial nations are actually conducted as outlined by this theory. The few available studies of the Swedish experience may be summarized in the following manner. There is considerable support for the view that macroeconomic variables such as inflation and unemployment do affect voters' behaviour. However, there is substantial uncertainty concerning the extent to which governments have actually tried to, and succeeded in, controlling economic events in the manner suggested by the theory of the political business cycle.<sup>8</sup>

If the political business cycle approach is used to explain the degree of price control in the Swedish economy, the volume of price controls ought to be greatest during an election year. The short-term political advantage of the possibly lower rate of inflation brought about by price controls together with the electorate's appreciation of price controls would be of particular importance immediately prior to an election. During non-election years, the losses in welfare associated with price controls assume greater importance at the same time as the potential political gains from controls are more limited. Hence the degree of price control during non-election years should be expected to be lower.<sup>9</sup>

In four of the six elections held between 1969 and 1987 (1970, 1973, 1976 and 1985), the degree of price control was higher during the election year than in the year previous to the election (see Table 10.2 and Figure 1.2). The increase in the extent of price controls introduced under the Price Control Act that took place between the year previous to an election and the actual year of the election was relatively limited between 1972 and 1973, 1975 and 1976 and 1984 and 1985. The degree of price control during the election years 1979 and 1982 was lower than in 1978 and 1981, respectively.<sup>10</sup>

Monthly data on the degree of price controls is shown in Appendix 1. In the election years of 1970 and 1979, an increase in the degree of price control took place in the August–September period immediately prior to the election and in 1985 the election was preceded by a price freeze that ended a few days before the election. There is no sign of a similar use of price controls for purposes of electoral tactics before other general elections in this period. The introduction of price controls at the end of August 1970, several weeks before the election in September, provides a clear case of the use of price controls for electoral purposes. The question of rising prices had threatened to become a highly sensitive issue for the government. The introduction of price controls under the Price Control Act removed this threat and instead allowed the Social Democratic Government to turn the issue to its advantage.

In June 1982, three months prior to the election, the Centre–Liberal coalition in power almost completely abolished price controls. This withdrawal of controls was actually used by the government as an electoral campaign issue. Once the Social Democrats regained power in 1982, the degree of price control was again raised. In conclusion, it can be said that neither the monthly nor the annual data on the degree of price control for the

period 1969–1982 provide strong support for the hypothesis that price controls were subject to a systematic electoral pattern.

### *The inflation hypothesis*

According to the inflation hypothesis, as we formulate it here, the use of price controls is explained by changes in the price level. Rising prices or anticipated price increases induce policy makers to raise the level of price controls. Hence, years of high inflation would according to this view be accompanied by high degrees of price controls. Table 10.2 and Figure 1.2 provide some visual support for this hypothesis. The rising trend of inflation is associated with a trend increase in the level of price controls. Moreover, periods of rapid inflation are also periods when the degree of price control tends to increase.

A more formal test of the inflation and the election hypothesis is summarized in Table 10.3 where the degree of price control is estimated as a function of the rate of inflation and of the election year, represented by a dummy variable, for the period 1969–87. According to the regression, the rate of inflation is a significant explanatory factor behind the degree of price control. A logarithmic function has been chosen, thus the coefficient for the rate of inflation represents an elasticity, i.e. a 1 per cent change in the rate of inflation gives rise to a more than 3 per cent change in the degree of price controls. Thus, the regression estimate provides support for the view that price controls represent a policy response to rising prices. On the other hand, the dummy variable for the election year is much less significant than the rate of inflation. Table 10.3 provides very limited support for the election hypothesis.

The correlation between inflation and price controls suggested by Table 10.3 may be partially explained by the general pattern of Swedish stabilization policy. As a result of the devaluations in the spring and early autumn of 1977, the degree of price control in March–April and September–October of that year was above 70 per cent. The devaluations of September 1981 and October 1982 also gave rise to substantial price controls. These devaluations should be viewed as the result of a more rapid domestic inflation in relation to the rate of inflation in countries with whom Sweden maintained a fixed exchange rate. A more rapid domestic rate of inflation than the international one causes an increase in price controls – albeit indirectly and subject to a certain time lag – via devaluations.<sup>11</sup>

The process of wage bargaining has contributed to the link between inflation and price controls. In the event of the consumer price index exceeding a certain stipulated level during the wage contract of 1978–79, the wage agreement would then become subject to new negotiations. During 1978, the government raised the degree of price control in order to keep the rate of inflation within the limit specified by the agreement and thereby to avoid renegotiation of the central wage contract. The high level of price controls during 1979 – 56 per cent – is also partially explained by the existence of a



**Table 10.3 The degree of price control, the rate of inflation and the election years 1969–87**

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$$\log \text{DPC} = -5.15^{**} + 3.61^{**} \log \text{INF} + 0.91^{*} \text{ELY}, R^2 = 0.46, \text{DW} = 2.14$$

(2.12)            (1.02)            (0.84)

\*\* significant at the one per cent level

\* significant at the 10 per cent level

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*Source:* See Appendix 1

*Notes:* The degree of price control (DPC) is the dependent variable, and the rate of inflation (INF) and election years (ELY) are the independent variables. The election years are represented by dummy variables. Standard error in parenthesis. The estimates are based on the view that price controls have not affected the rate of inflation, i.e. the direction of causality runs from inflation to price controls and not in the opposite direction. The econometric work on price controls reported in Chapter 9 provides support for this view.

‘guarantee clause’. The general price freeze and the accompanying high degree of price control during the spring of 1980 as well as during the spring of 1984 should be seen as government attempts to ‘smooth’ the way towards a new wage agreement. In 1985 price controls were introduced as part of a package to restrain economic activity. Price controls introduced in January 1987 were due to a guarantee clause in the wage agreement of 1986/87. The consumer price index surpassed by a very slim margin the critical level that gave the unions the right to renegotiate existing contracts. The union movement accepted at that point price controls as a substitute for renegotiations. This linkage between the wage bargaining process and price inflation has tended to strengthen the incentives for the use of price controls.

The above argument may be summarized in the following manner. Price controls have been introduced primarily as a policy reaction to a change in the rate of inflation in the 1970s and 1980s. There is weak support for a systematic electoral pattern during the entire period.

### **Choice of goods and services subject to selective price controls**

Price controls have been introduced under the provisions of the Price Control Act of 1956. In 1973, the Act became more stringent as a result of legislative amendments. It is clearly stated in a preparatory report that price controls are

to be used for the purposes of stabilization policy – no other objective is mentioned.<sup>12</sup> The Act stipulates that price controls will be introduced when there is ‘a risk for serious price increases in the country affecting major goods and services’. This raises a number of questions. Which goods and services should be made subject to price controls? In other words which sectors were considered to be major ones? What were the predominant motives – stabilization policy or other objectives?

The following discussion is based on Table 1.1 in Chapter 1 which lists the goods and services that were made subject to selective controls between 1973 and 1983. These controls were applied in addition to the general controls introduced during the period, that is the price freezes and mandatory prior notifications. The table is based on a classification into five categories: (1) food products, (2) household goods, (3) passenger cars and petroleum products, (4) building materials, paper and wood products, and (5) miscellaneous. Food products and building materials have been the prime target of these selective price controls. In certain respects, Table 1.1 underestimates the importance of these sectors. The imposition of price controls on agricultural machinery and fertilizers (Group 5) was justified on the grounds of rising food prices (Group 1). Controls on electrical household appliances (Group 2) were closely associated with price controls on building materials (Group 4).

The frequency of price controls on food products and building materials is largely explained by the central role played by food and housing costs in the political debate. These items represented close to 50 per cent of household expenditures and were consequently given a large weight in the consumer price index.<sup>13</sup> Economic policy makers have therefore considered it appropriate to concentrate price control measures to these sectors.

On what basis have the goods and services listed in Table 1.1 been selected? A fairly accurate presentation of the preferences and motives underlying the use of selective price controls is found in the press releases issued by the Ministry of Commerce in conjunction with the introduction of different controls.

When a price freeze was brought into force in March 1974 covering bread, flour, various building materials, newsprint, paper towels, table napkins, toilet paper and baby napkins, the Minister of Commerce justified these measures as a continuation of ‘our policy of seeking to protect households against the rising costs of food and housing’.<sup>14</sup> Similar arguments were put forward when price controls were introduced on potatoes in November 1975. The Minister responsible for the measure stated that the recent sharp increases in the price of potatoes meant that ‘families and low-income earners were especially hard hit. The Government has therefore directed its immediate attention to the use of price controls to reduce the price of potatoes to a more reasonable level’.<sup>15</sup>

Similar distributional arguments in favour of price control also appear in some of the press releases from the Ministry of Commerce. The introduction of price controls on canned and frozen foods in March 1976 was partly justified

on the grounds that the substantial price increases that had taken place in the industry 'has contributed to an increase in the profits of many foreign-owned companies'.<sup>16</sup> A transfer of income to foreign-owned companies was thus not considered desirable.<sup>17</sup> Price controls on food products and building materials were thus introduced in response to distributional considerations as well as to those of stabilization policy.

Government intervention in one sector of the economy sometimes contributes to price controls in another area. For instance, the price controls on insulation materials in 1977 were justified by the need to save energy.<sup>18</sup> The loans that were made available for energy savings were the cause of the price controls that were introduced on plate glass and insulation panes in August 1978.<sup>19</sup> The subsidies on basic foodstuffs were the principal grounds for the introduction of the price freeze on basic foods between 1973 and 1980 as well as for various other forms of price control on food products introduced during this period. Similar reasons were put forward for the introduction of price controls on fertilizers and agricultural machinery in September 1974.<sup>20</sup> These products had been subject to price rises and it was feared that a continuous increase in prices would affect food prices via the agricultural price support system.

Another reason frequently put forward in support of the introduction of selective price controls is that substantial price increases have either occurred or are expected to occur in the future. This applies, for example, to price controls on raw materials such as petrol and other oil products, wood products, pulp and coffee, all of which are traditionally subject to substantial price fluctuations. The aim of the price controls on these items has been to dampen the rise in their prices. However, sooner or later, Swedish raw material prices must come in line with world market prices. This is also the view expressed in the departmental press releases. Nevertheless the use of price controls is considered justified on the grounds that they protect the Swedish price level from the immediate, full impact of international price increases and/or from international prices that the Ministry of Commerce and the SPK consider to be 'abnormally' high.

Price controls have thus been introduced as a reaction to price increases that have already taken place. This type of regulatory response supports the view that the political system introduces price controls in order to demonstrate that something is being done to deal with a problem that is considered to be politically acute.<sup>21</sup>

What are the factors that account for the introduction of price controls on sanitary towels in July 1974? The price of sanitary towels had become a political issue as a result of the demands by socialist women's organizations that had been made for free sanitary towels. The politicization of a previously non-political question attracted government interest which was subsequently expressed in the form of price control.<sup>22</sup>

An examination of the goods and services that have been subject to selective

price controls under the provisions of the Price Control Act indicates that price controls have often been introduced unsupported by any clear stabilization policy considerations. This is contrary to the rationale underlying the legislation on price controls. Arguments phrased in terms of stabilization policy are certainly presented as a principal motive for price controls. However, other factors also appear to have been important. Political considerations concerning the distribution of income have exerted a major influence on the choice of goods and services subject to price controls. Moreover these distributional considerations played a central role during the years of Social Democratic government than during the period of non-socialist governments (1976–82) when the use of price controls primarily took the form of general price freezes in conjunction with the devaluations of 1977 and 1981. After the return to power in 1982, the new Social–Democratic government did not adopt selective controls during the period 1982–1987.

The above discussion on the selection of goods and services subject to selective controls has been based on an examination of the press releases issued by the Ministry of Commerce. An American economist, Charles Cox, has developed a model which seeks to explain how a price control policy is implemented in practice. This model is of great interest in the present context as it appears to be applicable to Swedish conditions.

Cox (1980) begins by stating that price controls cannot abolish inflation. It is generally recognized in economic theory that a price which is fixed at a level below the market price will give rise to excess demand, rationing on the basis of other criteria than price and to a misallocation of resources.<sup>23</sup> On the other hand, according to Cox, there is a lack of knowledge of how price controls function in practice. He poses the following questions:

- 1 How do controls vary from industry to industry and which industries are subject to control?
- 2 Who are the winners and losers as a result of controls?
- 3 What adjustments do companies make in order to avoid or limit the effects of controls?

Cox then tries to answer the first of these questions.

Cox starts out from the assumption that the authorities responsible for price controls seek to maximize political support for the ruling political party (parties) in terms of votes, money or other resources. In other words, Cox considers that the objectives of the price controlling authority are identical with those of the government.<sup>24</sup> A cut in the inflation rate is assumed to increase support for the government while the welfare losses associated with controls lead to a decline in government popularity. Hence the existence of queues and shortages of products subject to price controls represent a political cost for a programme of price control. Within the constraints of a given budget, the regulatory authority then seeks to balance the political gains from each

industry or product group subject to price control against the political and monitoring costs of the price control programme.<sup>25</sup>

Cox points out that the political benefits of price controls are somewhat ambiguous. They can be of two types:

- a) a stabilization policy benefit where price controls lead to a temporarily lower rate of inflation than otherwise would have been the case, and
- b) a redistribution policy benefit where price controls gives rise to a transfer of income between different groups in society.

Cox leaves this question unanswered in his model but suggests that it would be useful if a theory could be developed to determine the relative importance of stabilization and distributional policy objectives. However, in his model, the objective of the regulatory authority is to cut the rate of inflation by limiting price increases in various sectors of industry, where the costs of regulatory control depend upon the industrial structure.

Cox's model gives rise to a number of testable implications. The model assumes that the degree of price restraint will be greater in those industries whose goods and services have a large weight in the official price index since the effect of price controls on the price index is proportional to the product's weight. The degree to which prices are kept below equilibrium prices will be greater in industries characterized by an inelastic supply and an elastic demand since the welfare loss associated with these conditions is lower than in the case of an industry that has an elastic supply and an inelastic demand.<sup>26</sup>

The model also indicates that prices will tend to be kept below equilibrium levels in industries subject to a high degree of concentration, producing homogeneous goods, characterized by stable market conditions and selling a high proportion of their output to the public sector. Industries that have these characteristics are relatively easy to monitor. Cox carried out a series of empirical tests for a large number of US industries and his results provided support for his hypotheses.

Cox concluded that the maximization of political support provides a good explanation of the formulation of the American price control programme between 1971 and 1974. During this period, the inflation rate was most effectively dampened in those industries that yielded high political benefits and where the political and regulatory costs were relatively limited.

The Swedish experience of price control policy is consistent with Cox's arguments on a number of points. The choice of goods subject to selective controls provides support for the view that price controls are oriented towards the maximization of political support for the ruling government. Swedish price controls have frequently had a marked distributional character in spite of the fact that the Price Control Act is based on the view that controls are primarily intended to be an instrument of stabilization policy.

## **The Price and Cartel Office as a lobby for price controls**

An analysis of the political economy of price controls must take account of the regulatory agency responsible for the administration of price controls. The wide-ranging American literature on regulatory agencies focuses on several central hypotheses. Each regulatory agency develops an inherent self-interest in its own sphere of operations. It guards its area of control and endeavours to expand it by the use of various measures. These agencies are frequently analysed by economists in terms of growth maximizing, power maximizing or budget maximizing behaviour. The modern literature also stresses similarities between government bureaucracies and profit-maximizing companies.<sup>27</sup> Consequently, traditional economic theory is used to analyse both phenomena. Hence a description of the incentive structure of regulatory agencies may allow us to draw conclusions regarding their behaviour.

As a rule, the regulatory agency finds itself in a competitive situation with other government bodies in relation to the funding of its budget. Consequently, government agencies become involved in political tactics. They are after all a product of political decisions and their existence depends on continuous political support. This view is summarized by Schuck (1979) in the following manner.<sup>28</sup>

Regulation is not only a legal, administrative and technical phenomena. It is also ultimately and inevitably a political phenomena.... Once a regulatory agency has become established, it must continue to seek political support in order to both protect the legislation that provided it with the initial opportunity for control and to ensure that it is allocated sufficient funds to carry out its internal operations and maintain its external regulatory activities.

Different authorities achieve different measures of success in this competition for political support. Success in this field is largely dependent on the ability of the agency's senior administrators to adjust to and derive benefits from the prevailing political situation. Competition in this market may be as intense as in traditional markets.<sup>29</sup>

On the basis of this very general line of reasoning, several specific points can be made regarding the operations of the SPK. During the 1960s, the SPK was mainly involved in the fields of research and monitoring prices. The creation of price controls in the 1970s opened up opportunities for growth for the SPK. In utilizing these opportunities, the SPK actually act as a pressure group, a lobby, for the furtherance of price control policies.<sup>30</sup> On a number of occasions, the SPK clearly operated, sometimes quite independently, in a manner that contributed to the growth and establishment of price controls. Two particular areas should be mentioned in this context: the creation by the SPK of a system of negotiations and controls with individual companies – the 'SPK system'; and SPK's budgetary requests which are basically a catalogue of demands for new forms of control.

During the 1970s, the SPK's regulatory activities expanded markedly as a result of its price monitoring operations which were in accordance with its directives and the special guidelines issued by the government to the SPK in 1971. According to these directives, price monitoring would be based on 'consultations' that would seek to 'influence price movements in a manner favourable to the interests of consumers'. However, in combination with the mandatory prior notification procedure where companies were required to provide advanced notification to the SPK of planned price increases, price monitoring, was on many occasions transformed into a comprehensive system of price control.<sup>31</sup> Viewed from the perspective of the individual company, the SPK's activities could, for instance, take the form of a threatening appeal to the government which could lead in turn, via the 'good contacts' of the SPK with the Ministry of Commerce, to the introduction of a mandatory price freeze. This interpretation of the SPK's 'expansionist' approach to price controls is supported by the evidence presented previously regarding the individual companies.

According to its directive, the SPK is required to monitor price movements and to notify the government of 'price movements that might warrant special measures'. This means in practice that the SPK informs the government via the Ministry of Commerce of any price movements that would justify the introduction of price controls. In effect, this requirement gives the SPK an important right of initiative. It is then up to the government to decide if any price controls shall be introduced. The literature on price controls indicates that there is no clear-cut method for determining whether price increases are 'motivated' or 'unmotivated'. Consequently there are no simple rules regarding when a particular case should or should not be reported to the government. There is thus considerable scope for the SPK to make its own assessments. During the period 1977-80, the SPK notified the Ministry of Commerce on 123 occasions regarding companies whose pricing decisions had taken account of factors such as compensation for anticipated increases in costs, lower volume of sales and/or wage drift. According to the government guidelines given to the SPK in October 1977, each of these factors could provide by itself sufficient grounds for the introduction of price controls.<sup>32</sup>

The government introduced either a price freeze or a price ceiling in 12 of these 123 cases. Hence the SPK's regular use of its right of initiative has an important bearing on the use of price controls in the 1970s. These figures may be interpreted as an indication that the SPK adopted an 'expansionist' approach to price controls, at least in relation to the government. Alternatively, the SPK may be viewed as having interpreted very strictly government directives by reporting every price increase that was considered to represent a 'threat' to a 'stable pattern' of price movements. This would help to explain why marginal items such as plaster, coffins, American cars, candles and the magazine 'Vi' became the subject of SPK notifications to the government.

In their budgetary requests, the SPK has emphasized that an efficient

administration of price control and price monitoring in accordance with government 'demands' necessitates the allocation of additional resources to the SPK, partly in the form of more staff. In the expenditure request for 1980/81 (p. 18), it is stated for example: 'Experience indicates that the resources available to the SPK in certain important areas are quite inadequate in terms of the SPK's ability to satisfactorily carry out government directives.' This argument appears in many different contexts in support of demands for additional resources being made available not only to sectors already affected by controls or monitoring procedures but also to enable an expansion into areas that had not previously been subject to control by the SPK (p. 18):

Against this background, the SPK requested in its budgetary submission for 1979/80 that a special unit for price monitoring and price investigation should be created for the housing sector. This unit would require the creation of eleven new posts. In the following fiscal year 1980/81, the SPK also requested that funds should be set aside for price monitoring and investigative activities in the area of fruit, vegetables and root crops. No resources have yet been made available to meet the urgent requirements of the SPK in relation to both these areas. This will naturally have had a prejudicial effect on the results of the SPK's operations.

In anticipation of the fiscal year of 1980/81, the SPK declared (p. 18):

The limited personnel available to the SPK has however meant that it has not been possible to maintain efficient monitoring in all of the sectors that are of major interest to consumers. In the previous section, we have drawn attention to the SPK's inability to carry out some of its important monitoring and investigative activities.

The shortage of resources affects such vital areas as housing, transport, municipal taxation and charges and fruit and vegetables. The general efficiency of the SPK's operations could have been improved if adequate resources had been made available for work on statistical methods and company analysis. Improvements in efficiency could also have been made if clerical and other auxiliary staff had been maintained at proper levels.

In their budget submission for 1981/82, the SPK put forward the following argument: if the government wishes to improve the price monitoring system, a series of legislative changes should be introduced. This could involve, for instance, an extension of the period of mandatory prior notification from one to two months and a change in legislation which would allow individual companies to be made subject to price control. The latter was not possible under existing legislation. The SPK also proposed that the Price Control Act should be extended to cover real estate (p. 92). The abolition of rent controls has removed one of the reasons put forward for the exclusion of real estate from the provisions of the Price Control Act. Consequently there are now grounds for amending the scope of the Price Control Act to include the real estate sector. In its budgetary request for 1981/82, the SPK also discusses the possibility of



introducing control of profit margins under the provisions of the Price Control Act (p. 91):

The control of profit margins offers the only opportunity to stop rapid price rises in sectors subject to marked changes in the composition of goods. It is at present uncertain whether such a change could be introduced under the provisions of the Price Control Act. The question has been dealt with in a report published by the Price Control Committee entitled 'Price freeze on certain essential foodstuffs – an overview'. It is essential that the present uncertainty surrounding this issue is cleared up and that the provisions of the Price Control Act are amended in order to provide opportunities for control of company profit margins and methods of calculation. This would enable government authorities, in so far as it is required, to intervene selectively but also efficiently in an inflationary price spiral.

The SPK's budgetary requests contain many references to the need for price monitoring due to the presence of oligopolistic market structures. However, the theoretical and empirical grounds for this argument are weak.<sup>33</sup> The establishment of a monopoly or oligopoly may lead to an initial rise in prices. However, this does not give rise to inflation, that is, to a prolonged rise in the general level of prices. The proponents of the view that monopolies or oligopolies create inflation must accordingly believe that the rapid inflation in industrialized countries in the 1970s was due to a continuous increase in monopolistic concentration in Sweden and elsewhere. However, there is hardly any empirical support for this view. The origins of inflation are found in the general formulation of macroeconomic policies – monetary, fiscal and exchange rate policies – rather than in a high or growing degree of business concentration. Differences in macroeconomic policies represent the major cause of differences in the rates of inflation between countries with similar industrial structures.<sup>34</sup>

The budgetary requests submitted by the SPK since the early 1970s may be viewed as a long list of arguments and proposals in favour of an expansion of the agency's monitoring and regulatory activities. This is hardly surprising. The SPK conducts the same type of budgetary tactics as other government authorities do.<sup>35</sup> However, the SPK operates as a lobby in support of measures which are quite dubious from an economic point of view. The role of the SPK as a pressure group for price controls tends to lead to a greater degree of price control and thereby to impose greater costs on the Swedish economy than otherwise would have been the case.

Within the Price Control Committee, working 1976–1981, senior officials of the SPK clearly expressed their support for price controls. With reference to the following three arguments, they refuted the criticism of price controls made by economists working for the committee:

- a) At the theoretical level, the criticism by economists of price controls may be correct. However, in practice, conditions are different. Thus, the critique does not apply to actual conditions.

- b) The criticism by economists of price controls is based on historical experiences. However, the world has now changed. Consequently, these experiences are no longer relevant to the current situation and accordingly must be rejected.
- c) The criticism by economists of past price controls is partly correct. However, the SPK has entirely learned how to manage the system. The SPK has now sufficient knowledge to ensure that any markedly negative repercussions of controls will not arise in the future.

These arguments, which were presented in different variants and combinations, were put forward without the support of any empirical studies. During the work of the Price Control Committee 1977–81 they were used to continually defend price controls and the activities of the SPK.

## Summary

Swedish price control policy 1970–1987 was overwhelmingly determined by political factors. The introduction and use of controls was not based on any balanced assessment of economic costs and benefits. On the contrary, price controls were largely a political reaction to rising prices. The choice of goods and services subject to selective price controls in the 1970s under the provisions of the Price Control Act was to a substantial extent determined by distributional considerations. The stabilization policy objectives of price controls outlined in the preliminary work on the Price Control Act were thus in many cases overshadowed by distributional motives.

The SPK functioned as an active pressure group in support of price controls in the 1970s. It succeeded in establishing a comprehensive regulatory system on the basis of its price monitoring procedures. This was achieved without any major political discussion or public examination. Moreover, as the case studies have illustrated, price controls gave rise to a prolonged bargaining process between the SPK and individual companies. In summary, price controls became a question of politics at three levels: the level of the company, of the regulatory authority and of the government.

## Notes

- 1 This chapter is based on the author's report, 'Priskontrollens politiska ekonomi. Några observationer' (The political economy of price controls. Some observations), SOU 1981:41, Appendix 2.
- 2 Price control is not a new phenomenon. The use of price controls as a counter-inflationary measure can be found as far back as the ancient civilizations. See Schuettinger and Butler (1979) and Rockoff (1984).
- 3 Different framings of the questions would enable a distinction to be drawn between the interviewed persons who wanted to end the price-wage spiral and those who advocated a wage and price freeze as a counter-inflationary measure.

- 4 According to SIFO's commentary to the opinion poll carried out in October 1980, the positive attitude to a price and wage freeze applied 'with only very small variations, irrespective of age, sex, housing area, social group, occupation and trade union affiliation'.
- 5 See Blinder (1979, pp. 110–11) and Appendix 4.
- 6 The introduction of price controls as a counter-inflationary measure has often been greeted with satisfaction from almost all quarters. However, enthusiasm appears to decline with the passage of time and support for controls becomes less widespread, suggesting a life cycle of price controls.
- 7 The one hypothesis does not exclude the other. Both hypotheses can contribute to an explanation of variations in the degree of price control.
- 8 See Jonung (1985) for a discussion of the existence of political business cycles in Sweden.
- 9 The relationship between price controls and political tactics is discussed in Jan Herin's examination of foreign price and wage controls. See his conclusion (SOU 1981:42, p. 30):

Consequently, it would appear that governments in several countries have introduced electoral tactics into economic policy. Price freezes have been brought into force prior to elections in the USA, Italy and France in 1972 at the same time as these governments conducted expansionist economic policies in order to reduce unemployment. Similar measures were undertaken in Great Britain before the election in 1974. A price freeze was also introduced in Sweden prior to the election in the autumn of 1970.

- The price freeze imposed by the Social Democratic Government in Norway in August 1981 may also be viewed as a response to the approaching parliamentary election in September of that year.
- 10 The degree of price control is measured in Table 10.2 as the proportion of total consumption of goods and services subject to controls based on the Price Control Act. In addition to the price controls introduced under the Price Control Act, the SPK has also carried out price monitoring during most of the 1970s and 1980s which has in practice constituted a form of price control. However, variations in the scope of price monitoring is difficult to assess. Consequently the following discussion will only deal with legally binding price controls.
  - 11 The rate of inflation has generally increased *after* elections. This was the case following all the elections held during the 1970s, namely 1971, 1974, 1977 and 1980, as well as after the election of 1982. Governments have raised indirect taxes and devalued after rather than before elections. This has led to a higher rate of inflation in the year following an election as well as a higher degree of price control. See Jonung (1985).
  - 12 See the departmental report 'Prisreglering som stabiliseringspolitiskt instrument' (DsH 1972:49). (Price controls as an instrument of stabilization policy.)
  - 13 Food products received a weight of 25 per cent while the corresponding figure for housing costs, heating and lighting was slightly over 20 per cent of the consumer price index of the 1970s. With the exception of the 'miscellaneous' category, these were the major items in the index.
  - 14 Ministry of Commerce press release, 8 March 1974.
  - 15 Ministry of Commerce press release, 18 November 1975.
  - 16 Ministry of Commerce press release, 26 February 1976.
  - 17 The price controls introduced on passenger cars in July 1976 were also partly motivated on the grounds of a 'fair' international income distribution. According to the press release of 28 July, 'the decision must be viewed against the background of the rapid expansion of the Swedish market for automobiles. It is naturally unacceptable that Swedish purchasers of cars should finance possible losses of car producers made on the international market'.
  - 18 Ministry of Commerce press release, 24 March 1977.
  - 19 Ministry of Commerce press release, 3 August 1978.
  - 20 Ministry of Commerce press release, 11 September 1979.

- 21 Cf. discussion in previous section.
- 22 This price control was not based on stabilization policy considerations. However, distributional motives may have exerted a certain influence.
- 23 Cf. discussion in Chapter 9.
- 24 A possible development of the model of Cox would be the inclusion of different goal functions for the regulatory authority and the government.
- 25 In the short run, the authority responsible for the administration of price controls receives a fixed budget. In the long run, this budget may be increased if the programme of price control succeeds in increasing the political support for the politicians responsible for price controls.
- 26 The model also provides an explanation for the increasing dissatisfaction with price controls over time and for their eventual abolition. At the time of their introduction, the supply of goods and services subject to price control are initially relatively inelastic. In the long run, supply becomes more elastic. Welfare losses increase and finally price controls are abolished, giving rise to a life cycle for price controls. See also note 6.
- 27 See e.g. Mueller (1980).
- 28 A comparison can also be made with Cox's (1980) model of price controls where the objective of the authority responsible for price control is the maximization of political support.
- 29 See Posner (1974) who emphasizes that regulatory authorities are forced to turn to their capital market every year, i.e. to the government and the parliament in order to obtain budgetary resources, which strengthens the element of competition.
- 30 During 1980, the SPK had approximately 200 full-time posts. Approximately 30 members of staff were directly concerned with the administration of price controls. However, the other members of the SPK's staff were also closely involved in price control matters as a result of the investigative activities carried out by the agency.
- 31 Cf. description in Chapter 1.
- 32 See SOU 1981:41, Appendix 2, part 2.
- 33 See e.g. Lustgarten (1975).
- 34 SPK's interpretation of the causes of inflation is illustrated by its monthly news-sheet, 'Price trends'. Inflation is caused by a series of price rises affecting individual goods and services as analysed under the heading 'factors that influence rising prices', subsequently changed to 'factors behind prices'. This approach ignores the basic causes of the inflationary process, e.g. the role played by economic policy. Intervention in the form of price controls in order to stop inflation is a natural outcome of a view that concentrates on reporting current price increases of individual goods and services. This very short run view of inflation may be considered as part of a policy that seeks to justify price controls.
- 35 Cf. the following conclusion of Tarschys and Eduards (1975, p. 121):  
 The greater the expansion of the bureaucracy, the more misleading it is to see it as controlled. This type of analogy does not allow us to examine the opportunities open to the bureaucracy. Work on the budget, for example, is a genuine political process in which the various actors pull in different directions. In a large organisation such as the Swedish public administration, neither a remaining civil service spirit or the shared political beliefs of the government and civil servants can prevent each department and sector from making its own interpretation of 'public welfare'. The expenditure requests made by various bureaucracies clearly illustrate this. They are the expression of a sectional interest in that most political of all activities, the competition for budgetary resources.

# 11 Conclusions

Price controls were widely used in Sweden during the period 1970–1987. They comprised both legally binding controls introduced under the Price Control Act and a system of price monitoring that the SPK, the government agency in charge of administering the control measures, built up largely on its own initiative. On several occasions, price controls covered approximately 75 per cent of total private consumption in Sweden. The remaining area, housing expenditure, was at the same time subject to wide-ranging controls. The use of price controls thus became a permanent feature of Swedish economic policy during the 1970s and 1980s.

This book has reached the following conclusions with regard to the effects of price controls. The major finding established by the case studies of five firms subject to controls is that the control measures frequently developed into a prolonged bargaining process consisting of a series of negotiations, bids and counterbids. The outcome of this process depended on the bargaining strength of the parties engaged. The negotiations with the SPK placed heavy demands on the companies subject to price controls. The case studies also show that price controls led to financial difficulties for the firms involved, to postponed investments and to uncertainty regarding the future. These are serious effects in view of the severe problems that confronted Swedish industry in the 1970s: low profitability, financial instability and low growth.

With regard to the macro-economic effects, the empirical evidence suggests that price controls did not have a significant effect on the rate of inflation in the long run. Neither does available data allow us to conclude that price controls dampened inflationary expectations. Moreover, price controls undoubtedly

had a negative effect on the use of resources in the Swedish economy. They contributed, for example, to increased cooperation between companies in sectors of the economy subject to price controls. In some cases, price controls were used to redistribute income, i.e. stabilization policy motive was combined with or replaced by distributional considerations.

In view of the negative economic effects associated with price controls and the lack of any evidence which clearly demonstrates that price controls had a significant effect on the rate of inflation, the question arises as to why price controls were used at all. The answer is that during the 1970s and 1980s, inflation was considered to be a more serious political problem than had previously been the case. Traditional stabilization policies seemed to be unable to come up with an answer to the problem of rising prices. Consequently, the response of the political system in Sweden, as well as in other countries, was to introduce controls.

In summary, the price controls of 1970–1987 were not associated with any significant long-run gains to Swedish society. On the other hand, the economic costs appear to have been substantial. The burden of proof with regard to the effects of price controls has generally lain with those who criticize the use of such controls. However, the converse situation ought to prevail: the proponents of price controls should be asked to demonstrate in advance how they expect the introduction of controls to give rise to a net economic gain to society.

\* \* \*

In the final report of the Price Control Committee, published in the summer of 1981, a majority of the Committee's members recommended that the price control policy adopted during the 1970s should be brought to an end. This recommendation referred both to the price controls introduced under the Price Control Act and the system of price monitoring used to influence the pricing decisions of individual companies. The majority of the committee proposed a return to the price policy of the 1950s and 1960s, where the emphasis had been on 'collecting data on price changes, consumer information and measures to promote competition'.

As a result of the Committee's report, the Centre–Liberal coalition government decided in June 1982 to change government policy on price controls by means of a drastic reduction in the use of price controls. Price monitoring and price controls introduced under the Price Control Act were abolished. Milk was the only product that remained subject to price controls. At the same time, the government stated that it intended to expand the role played by the Anti-Trust Ombudsman (NO).

Following the election victory of the Social Democrats in September 1982, a general price freeze was introduced in conjunction with the devaluation of the krona in October 1982. This price freeze was largely abolished in March 1983 and replaced by the compulsory notification of price increases for certain

groups of products. This requirement was subsequently withdrawn in September 1983. General price freezes were used again in 1984, in 1985 and in 1987 in order to 'restrict' the rate of inflation. The price freeze of 1984 was combined with a short freeze on rents.

Sweden is at the end of the 1980s unique in international comparisons. It has relied on price controls longer than any other western economy. The Social Democratic party has previously displayed a strong ideological attachment to controls: the markets for money and credit, foreign exchange, housing, agricultural produce, and, since 1970, goods and services, have all been subject to price controls during the long post-war period of Social Democratic government. Price control policy was introduced by a Social Democratic government in the early 1970s and used prior to the election victory of the non-socialist parties in 1976. The return of the Social Democrats to power in 1982 marked a new period of the frequent application of price controls in spite of a declining trend rate of inflation. On the other hand, from 1976 to 1982 the non-socialist governments also made considerable use of price controls.

The evidence now available regarding price controls in the period 1970-1987 fails to provide any support for such a policy. The knowledge gained from this experience ought to provide a strong counter-argument against the future reintroduction of price controls irrespective of which political party or parties in power.

This study of the actual conduct of Swedish price control policy strongly suggests that price controls *should not* be used as an instrument of anti-inflationary policy. However, political parties and various interest groups can be expected to raise demands in the future for the introduction of price controls whenever the Swedish rate of inflation is considered to have reached a 'high' or 'critical' level. It is tempting for a government to appear strong and decisive by introducing or extending price controls, thus creating support among voters and various interest groups. Similarly, a proposal by the opposition party or parties to introduce price controls may convey a sense of a willingness to act, strengthening the political support of the opposition.

Against this background, it is important to develop an institutional framework that minimizes the risk of the introduction of price controls. An appropriate step in this direction would be the abolition of the SPK. Even though this agency may take on duties other than price control, there is a great risk that as long as the SPK remains in existence, governments will be tempted to resort to price controls when confronted with a rapid rate of inflation. Moreover, interest groups who wish to see the introduction of price controls would be able to refer to the experience of the SPK in the field of price controls, arguing that this experience should be utilized for controls. It is also quite probable that the SPK would itself be interested in the reintroduction of price controls.

The abolition of the SPK would provide a firm commitment – a strong signal – that price control policy has been brought to an end. This step would also help

to assure companies and the general public that price controls would not become an established feature of future economic policy in Sweden.



# Appendix 1. The degree of price controls and the rate of inflation, January 1970 – December 1987

Share of total consumption of goods and services subject to price control at the end of each month, and the rate of inflation. Price monitoring is not taken into consideration. Almost all private consumption except housing was subject to price monitoring 1972–87. Hence the table refers only to price controls covered by the Price Control Act.

Month	Degree of price control %	Rate of inflation per annum %	Month	Degree of price control %	Rate of inflation per annum %
1970			1971		
Jan.	0	4.6	Jan.	75	10.0
Feb.	0	6.4	Feb.	58	8.1
Mar.	0	6.4	Mar.	58	8.1
Apr.	0	6.4	Apr.	58	7.2
May	0	6.8	May	58	6.3
June	0	7.3	June	56	6.3
Jul.	0	7.2	Jul.	56	6.3
Aug.	13	7.2	Aug.	50	7.5
Sep.	13	7.6	Sep.	50	7.1
Oct.	75	7.6	Oct.	43	7.9
Nov.	75	8.0	Nov.	43	6.6
Dec.	75	8.0	Dec.	43	7.4

Month	Degree of price control %	Rate of inflation per annum %	Month	Degree of price control %	Rate of inflation per annum %
1972			1973		
Jan.	0	4.8	Jan.	7.5	5.7
Feb.	0	5.2	Feb.	7.5	6.1
Mar.	0	5.2	Mar.	7.5	6.0
Apr.	0	6.0	Apr.	7.5	6.4
May	0	6.8	May	7.5	6.4
June	0	6.8	June	7.5	7.1
Jul.	0	7.1	Jul.	7.5	6.7
Aug.	01	5.9	Aug.	7.5	6.6
Sep.	01	6.3	Sep.	7.5	6.6
Oct.	01	5.4	Oct.	12.2	7.3
Nov.	01	5.8	Nov.	12.2	8.4
Dec.	01	6.1	Dec.	12.2	7.6
1974			1975		
Jan.	12.0	8.3	Jan.	13.1	10.0
Feb.	12.0	10.4	Feb.	13.1	8.1
Mar.	14.2	11.0	Mar.	13.1	7.7
Apr.	14.2	9.5	Apr.	13.1	8.7
May	14.2	8.8	May	13.8	10.7
June	14.2	8.4	June	14.6	10.6
Jul.	14.4	8.3	Jul.	11.1	11.9
Aug.	14.4	9.0	Aug.	11.1	12.1
Sep.	14.4	9.7	Sep.	11.2	11.0
Oct.	14.4	11.9	Oct.	11.2	8.8
Nov.	14.4	11.8	Nov.	11.6	9.1
Dec.	15.1	11.4	Dec.	10.1	9.0
1976			1977		
Jan.	10.5	10.9	Jan.	9.3	9.0
Feb.	10.5	10.8	Feb.	9.3	9.5
Mar.	14.3	11.0	Mar.	8.8	9.7
Apr.	14.3	11.6	Apr.	73.8	10.1
May	14.3	11.1	May	73.8	10.3
June	12.3	11.3	June	8.1	11.7
Jul.	12.2	9.7	Jul.	8.1	12.8
Aug.	17.6	9.3	Aug.	6.8	12.2

Month	Degree of price control %	Rate of inflation per annum %	Month	Degree of price control %	Rate of inflation per annum %
Sep.	17.6	9.3	Sep.	77.7	13.5
Oct.	17.6	9.8	Oct.	77.7	12.2
Nov.	17.6	9.4	Nov.	6.8	12.4
Dec.	9.3	9.7	Dec.	6.8	12.6
1978			1979		
Jan.	6.7	14.0	Jan.	53.9	5.9
Feb.	6.7	13.8	Feb.	54.2	5.6
Mar.	77.8	13.0	Mar.	54.2	5.8
Apr.	77.8	12.3	Apr.	54.2	5.8
May	77.8	11.5	May	57.2	6.0
June	77.8	9.3	June	57.2	6.2
Jul.	77.8	8.8	Jul.	57.2	6.6
Aug.	77.8	8.3	Aug.	57.2	8.3
Sep.	77.8	8.0	Sep.	57.0	7.8
Oct.	49.6	8.0	Oct.	57.0	8.4
Nov.	54.1	7.4	Nov.	57.0	9.4
Dec.	54.1	7.4	Dec.	57.0	9.8
1980			1981		
Jan.	57.0	12.6	Jan.	28.7 <sup>1</sup>	12.5
Feb.	46.8	13.3	Feb.	28.7	13.0
Mar.	79.9	13.5	Mar.	28.7	13.0
Apr.	79.9	13.6	Apr.	28.7	12.9
May	46.8	13.3	May	28.7	13.2
June	46.8	13.1	June	28.7	13.3
Jul.	46.8	13.2	Jul.	28.7	13.4
Aug.	46.8	12.2	Aug.	28.7	13.7
Sep.	40.7	14.9	Sep.	77.7 <sup>2</sup>	11.4
Oct.	40.7	15.5	Oct.	77.7	10.4
Nov.	40.7	14.6	Nov.	77.7	10.2
Dec.	40.7	14.0	Dec.	77.7	9.2
1982			1983		
Jan.	25.9	9.5	Jan.	75.6	10.0
Feb.	25.9	9.0	Feb.	75.6 <sup>5</sup>	8.2
Mar.	25.9	8.6	Mar.	33.3	8.4

Month	Degree of price control %	Rate of inflation per annum %	Month	Degree of price control %	Rate of inflation per annum %
Apr.	25.9	8.7	Apr.	33.3	8.5
May	25.9	8.5	May	33.3	8.6
June	1.3 <sup>3</sup>	8.5	June	33.3	8.8
Jul.	1.3	8.2	Jul.	33.3	9.0
Aug.	1.3	7.7	Aug.	33.3	9.2
Sep.	1.3	7.5	Sep.	0 <sup>6</sup>	9.4
Oct.	75.6 <sup>4</sup>	8.2	Oct.	0	8.6
Nov.	75.6	8.8	Nov.	0	8.6
Dec.	75.6	9.6	Dec.	0	9.3
1984			1985		
Jan.	0	8.4	Jan.	0	7.4
Feb.	0	7.9	Feb.	0	8.8
Mar.	0	9.0	Mar.	70.5	8.1
Apr.	73.0	8.9	Apr.	70.4	7.8
May	73.0	8.9	May	70.5	8.3
June	82.2	8.1	June	59.0	8.2
Jul.	9.7	7.5	Jul.	59.0	7.8
Aug.	9.7	7.8	Aug.	33.0	7.0
Sep.	9.7	7.7	Sep.	26.7	6.7
Oct.	9.7	7.3	Oct.	0	6.9
Nov.	0	7.4	Nov.	0	7.0
Dec.	0	8.2	Dec.	0	5.7
1986			1987		
Jan.	0	6.1	Jan.	0	3.2
Feb.	0	5.3	Feb.	75.0	3.4
Mar.	0	4.3	Mar.	75.0	3.8
Apr.	0	4.5	Apr.	75.0	3.4
May	0	3.3	May	75.0	3.5
June	0	3.4	June	75.0	3.3
Jul.	0	3.7	Jul.	75.0	4.3
Aug.	0	3.6	Aug.	75.0	5.0
Sep.	0	4.1	Sep.	75.0	5.0
Oct.	0	4.0	Oct.	75.0	5.1
Nov.	0	3.5	Nov.	75.0	5.4
Dec.	0	3.3	Dec.	75.0	5.2

*Source:* SOU 1981:42 Appendix 10, SPK and Central Bureau of Statistics.

*Notes:* The table is illustrated graphically in Figure 1.2. It takes account of the following price control measures covered by the Price Control Act: price freezes, price ceilings and mandatory prior notification. The table excludes pledged prices since it has not been possible to devise a comprehensive measure for this measure. However, pledged prices have only been used for three products: chicken, bread and potatoes and for a very short period of time in the 1970s.

- 1 During the period January – August 1981, mandatory prior notification and price freeze measures accounted for 27.5 and 1.2 per cent respectively of total price controls. The equivalent figures for January – May 1982 were 24.6 and 1.3 per cent, respectively.
- 2 In conjunction with the devaluation of 17 September 1981, a general price freeze was introduced for the period up to 31 December 1981.
- 3 Mandatory prior notification was abolished on 23 June 1982. The price freeze on milk remained in force.
- 4 In conjunction with devaluation, a general price freeze was introduced on 9 October 1982.
- 5 The price freeze was withdrawn on 1 March 1983. At the same time, mandatory prior notification was introduced. The government stipulated that certain authorities and public utilities should consult with the SPK prior to price changes. This stipulation covered 2.9 per cent of private consumption between 1 March and 24 September 1983.
- 6 Mandatory prior notification was abolished on 24 September 1983.

## Appendix 2. Price controls: the view of the Anti-trust Ombudsman

The task of the Anti-trust Ombudsman (NO) is, briefly, to safeguard competition in the Swedish economy by means of anti-trust and other measures that seek to prevent the creation of monopolies. The views of the NO on the relationship between price control policy and competition were presented to the Price Control Committee at a hearing held on 15 October 1980. As indicated by the following memoranda from this meeting,<sup>1</sup> the hearing was attended by, among others, Torsten Löwbeer, NO, Gunnar Hermanson, Deputy NO, Lars Jonson, Chairman of the Price Control Committee, Erik Dahmén and Nils Lundgren, members of the Committee, and Lennart Göranson, Secretary to the Price Control Committee.

Torsten Löwbeer's contribution provides valuable insights into the operation of Swedish price control policy. It expresses the considered views of a 'practical man' who has substantial experience of Swedish business and industry. In his judgement, price controls have, from the standpoint of competition, given rise to a number of negative effects: an increase in price rigidities, growing cooperation between companies, a tendency for controls to preserve existing economic relationships, and a growing unwillingness on the part of companies to cut prices. Moreover, the NO found that price controls have tended to make long-term company planning more difficult and to have reduced the willingness of companies to invest in sectors subject to price controls. This list is then supported by a number of practical examples which bear out the NO's contention that price controls have had a damaging effect on competition in the Swedish economy.

In his summary of the price control policy of the 1970s, the NO stated that price controls 'ought to be a measure used only in emergency situations'. He also criticized the absence of legal grounds for the SPK's system of prior notification which in practice led 'to the same results as those achieved by the system of mandatory prior notification that is sanctioned by the Price Control Act'. The NO concludes with the statement that he has seen little evidence to indicate that price controls have had a beneficial effect. The critical tone of the NO's views regarding the administration of price control policy by the SPK should be seen in relation to the inherent conflict between competition and price control policies. The task of the NO is to seek to prevent the formation of cartels, to resist collusion between companies and to endeavour to increase competition in the Swedish economy. However, according to the NO, the price controls administered by the SPK have tended to operate in the opposite direction, that is to increase cooperation between companies and weaken competitive forces in the economy.<sup>2</sup>

The memoranda ought to be seen in relation to the account, provided in Chapters 2–8, of the experiences of individual companies regarding the operation of price controls. Many of the effects of controls discussed in these chapters are dealt with by the NO.

The memoranda presented below are drawn from the minutes kept by Lennart Göranson. They are reproduced here with only minor omissions:

Löwbeer began his presentation by agreeing with the findings presented in a paper on pricing policy produced by the working party dealing with price monitoring issues (Ds H 1965:2). According to Löwbeer, long-term or frequently recurring price controls – or price monitoring of a type considered to be more or less identical with price controls – are generally incompatible with competitive forces. Effective competition that actively influences resource allocation requires the existence of a market economy where prices act as the principal channel of information. According to Löwbeer, if this basic rule is disregarded, it will not be possible to avoid a series of negative effects on consumers, industry and the economy as a whole. There are numerous examples of such negative effects. However, Löwbeer pointed out that the effects of measures such as price controls were invariably difficult to separate from the influence of other factors. In addition, the negative effects of price controls tended to emerge in the long run.

From the standpoint of their impact on competition, Löwbeer groups these negative effects into six different categories:

1. Increased price rigidities e.g. price levels have to be 'approved' by the SPK.
2. Increased cooperation or understanding between companies e.g. the coordination at branch levels of the submission of price increases to the SPK and a better understanding, as a result of discussions with the SPK, of the plans of competitors.
3. Effects which tend to maintain existing prices and preserve market structures e.g. the costs of less efficient companies are given greater consideration than they would have received under free market pricing. Other examples mentioned by

Löwbeer under this heading are the price increases made in anticipation of a price freeze, the growing reluctance of companies to lower their prices when they consider that they will not receive compensation for expected increases in costs and finally, a growing lack of interest to reduce costs.

4. Difficulties of long-term planning and an increased reluctance to undertake investment e.g. by the avoidance of expansion in sectors subject to frequent price control and in extreme cases, by the closure of plants.
5. Distortions of production, sales and the distribution of costs, e.g. the disappearance of products from the market, a refusal to supply products at unprofitable, controlled prices, the introduction of compensatory price increases for products not subject to price control, the respective advantages and disadvantages of imports *vis-à-vis* domestic production and a deterioration in quality.
6. A reduction of consumer awareness regarding price movement and an increased reliance on government action.

Accordingly, Löwbeer pointed to the risk that conflicts may arise between the role of the SPK as the authority responsible for the administration of price controls and its duties regarding the promotion of competition in the economy. Moreover, Löwbeer also emphasised that the administrative costs of price controls for both companies and the SPK should be borne in mind.

Löwbeer doubted whether these misgivings, particularly in relation to the price control policy of the 1970s, could be interpreted as being purely theoretical without any basis in reality. If this was in fact the case, it would imply that even long-term price controls could be managed in such a fashion that they would not give rise to any negative effects on competition. Moreover such an interpretation would also suggest that the experience and findings of previous years were no longer valid. However Löwbeer considered that this was not the case and that there were many current examples which provided support for the theories and experiences of past years.

Löwbeer cites references to the approval of prices by the SPK in relation to competitors, retailers (shoes), customers (shoe repairs) and the NO (building materials, hairdressers etc.).

Regarding the risks of cooperation or collusion between companies, a number of statements by the representatives of Swedish industry indicate, in Löwbeer's opinion, that contacts have taken place at branch level, prior to price negotiations with the SPK.<sup>3</sup> This was the case, for example, in relation to radiators, wallpaper, chipboard, everyday commodities and road haulage. Löwbeer also pointed out that in certain cases, negotiations with the SPK were carried out on a joint company basis, e.g. everyday commodities, road haulage, paint manufacturers and fine paper mills. Although it was not always the case that companies had reached 'an agreed position' prior to these negotiations, Löwbeer suggests that at these meetings with the SPK, companies were able to inform themselves regarding the price increases that competitors had been able to obtain. This took place, for example, in the case of sanitary porcelain manufacturers. Löwbeer also found that the existence of price controls made it important for companies to ensure that all of the companies in a given branch actually charged the 'approved' prices. If this was not done, it would be difficult for companies to justify further price increases. Löwbeer mentions the chipboard industry as an example of this type of effect.



For practical reasons, the SPK has been unable to carry out separate negotiations with each individual company in a branch where there are a large number of companies, e.g. building materials, everyday commodities and road haulage. In the absence of a price leader, negotiations will instead be concerned with common adjustments to a particular list of prices. According to Löwbeer, this type of arrangement has tended to reinforce cooperation between companies on the question of prices and at the same time has given the price lists a semi-official character. . .

Löwbeer then discussed the role of price controls in the maintenance of prevailing price levels and the preservation of existing market structures. According to Löwbeer, the price control guidelines enabled companies to raise prices when faced with a threat to employment. As a result, companies in a weak financial position were able to exert upward pressure on prices throughout the industry and at the same time resist demands for rationalisation. Löwbeer found that under these guidelines, companies were more concerned with the justification of cost levels than the efficient management of their companies. This has tended to raise prices. It was also highly probable that companies have tended to raise prices in anticipation of a price freeze. Similarly companies have also tended to show a reluctance to lower prices when they expect to encounter resistance to future price rises. If the opposite had been the case, this would have suggested a lack of foresight on the part of the company. . .

Löwbeer emphasised that industry was very concerned about the difficulties for long-term planning caused by frequent intervention in company pricing decisions. In Löwbeer's judgement, these undoubted problems had seriously affected the willingness of companies to undertake investment and risks. At the same time, intervention by the SPK endangered existing employment levels<sup>4</sup>. . .

The trend of investment in recent years has been highly unsatisfactory. In Löwbeer's opinion, it would be difficult to exclude the role played by price control policy.

Low profit levels have also tended to weaken the financial stability of companies, endanger competitive advantage and threaten employment opportunities. Hence the short-run savings gained by consumers tend to be converted into substantial long-term losses.

Regarding distortions to production, sales and the distribution of costs, Löwbeer pointed out that the price freeze on wood products had to be followed up by special arrangements to ensure adequate supply to the domestic market.

Furthermore, he pointed out that the oil companies had on occasions refused to deliver oil because of the imposition of price ceilings at unprofitable levels. Certain agricultural machinery producers had been reported to have had to alter their production as a result of a price freeze. It had also been alleged that the producers of everyday household commodities had compensated for the losses associated with the price freeze by raising the prices of goods and services unaffected by price controls.

Löwbeer emphasised that changes in quality could occur insidiously. A purchase is not only a matter of price. It also relates to factors that are more difficult to verify such as quality and service.<sup>5</sup>. . .

The overall impression derived by Löwbeer of the different forms of price

controls and similar measures adopted during the 1970s was that they succeeded in postponing certain price increases but failed to have any significant influence on the rate of inflation. Löwbeer considered that this finding was also largely in agreement with the experience of other countries. In Löwbeer's view, the positive effects of price controls were outweighed by their serious negative effects. Löwbeer considered that price controls ought only to be used in emergency situations. In his view, the existing legislation on competition together with price monitoring procedures would normally provide adequate opportunities for intervention against the abuse of free market pricing. According to Löwbeer, the Price Control Act's function as a purely emergency measure ought to be revived. The fact that the Price Control Act has been in force continuously for a period of several years has meant that price controls have been extended to new areas without the actual fulfilment of the criteria laid down in the act for the extension of controls. In this way, Löwbeer considered that the Act lost much of its original character.

Finally, Löwbeer refers to the government directive given to the SPK which requires that the authority seeks, in its discussions with companies, organisations and other price-setting bodies to influence price determination in a manner favourable to consumers. Löwbeer pointed out that according to the Swedish constitution, the exercise of government authority is subject to the 'laws of the land'. In other words, a government cannot request an authority to take actions which come into conflict with existing legislation. Once again Löwbeer emphasised that opportunities to influence price determination already exist under The Restrictive Practices Act and under the provisions of the Price Control Act. However in Löwbeer's view, this did not mean that a government directive to an administrative agency could be used to justify a system of prior notification of price increases which in practice achieved the same results as those obtained by the mandatory system of prior notification that operated under the Price Control Act.<sup>6</sup>

Hermansson illustrated the conflict between measures designed to promote competition and price controls with reference to price determination in the local road haulage industry. He pointed out that the NO had succeeded in persuading the Association of Haulage Contractors to give up their system of recommended charges. In its attempt to monitor price movements in the industry, the SPK was forced to conduct discussions on prices with The Association of Haulage Contractors since it was obviously not possible to negotiate with 20 000 individual companies. According to Hermansson, these discussions resulted in the approval by the SPK of specific percentage increases in charges which were then interpreted by the industry as price recommendations. In the case of everyday household goods, the NO had instructed the SPK to conduct separate negotiations with each of the main retail groups. In conclusion, Hermansson stated that for practical reasons, the SPK was often forced to negotiate with representatives for the entire industry or from companies that acted as price leaders in the industry. In the long run, this tended to lead to a uniform pattern of price determination.

## Notes

- 1 These memoranda are kept in the National Archives along with the rest of the Price Control Committee's papers.
- 2 The SPK was obliged to reply to the arguments put forward by the NO. This reply takes the form of a special report entitled 'A commentary to the critical views on price control and price monitoring', mimeo, SPK, 26 November 1980.
- 3 This is also evident from the description of the experience of Gullfiber and Siporex, presented in Chapters 2 and 3.
- 4 Cf. the conclusions presented in Chapter 7.
- 5 Cf. the description in Chapter 9, section 3.
- 6 Cf. the discussion in Chapter 1 concerning the scope of price control policy.

## Appendix 3. Price controls. The view of a former Minister of Commerce

Staffan Burenstam Linder was Minister of Commerce in 1976–78 and 1979–81. He represented the Conservative party in the non-socialist governments under Torbjörn Fälldin as Prime Minister. As Minister of Commerce he was responsible for the price control programme.

He was a member of Parliament for the Conservative Party 1969–1986. He was trained as an economist, receiving his doctorate in 1961 at the Stockholm School of Economics. Among his publications should be mentioned his doctoral thesis *An Essay on Trade and Transformation* and *The Harried Leisure Class*. He has served as professor of international economics at the Stockholm School of Economics since 1974. He was appointed President of the Stockholm School of Economics in the spring of 1986.

He replied to the following ten questions in May 1985 for the English version of this book.

**Question:** When you were a member of parliament for the Conservative Party and the party was in opposition, you were extremely critical of price controls in the early 1970s, prior to 1976. Why did you not abolish price controls immediately when you became Minister of Commerce after the election in September 1976 and politically in charge of the price control policy?

**Answer:** Because a Minister does not decide everything himself – particularly not in a coalition in which the partners hold different views on the problem at hand.

*Question:* Far from abolishing the control policy, several new control measures were instituted in 1977–1978 and in 1979–1981 while you were the Minister of Commerce. How do you explain your position on these matters?

*Answer:* For brief periods we introduced overall price controls. I can possibly see some virtues with such a step in an effort to cool off inflationary sentiments after devaluations, and to prevent domestic producers from taking advantage of the fact that prices on import-competing products go up.

In articles and in debates during these years, I clearly spelled out my belief, namely, that, if inflation could be done away with by outlawing it, inflation would have been stopped a thousand years ago.

*Question:* How much did you know about the relationship between the SPK, the agency in charge of the price regulations, and the regulated firms? Were you aware of the bargaining process taking place between the SPK and the firms subject to price controls?

*Answer:* I have and had no illusions on how price controls work when they are in effect for some length of time. For those reasons I, for instance, during my years did away with most of the so-called ‘price stops’ on food products which we inherited and which had not prevented food prices from rising faster on an average than other prices.

*Question:* Did you try to influence the Price and Cartel Office in any way as the Minister of Commerce?

*Answer:* Yes; we reduced the budget of the Office and gave it the task of not monitoring each and every price change but rather concentrating on what appeared, in their view, to be spectacular price changes. To achieve more deep-going changes we organized an effort to review in a scholarly way the effects and non-effects of price controls in order to let the results affect public opinion and the position of the other political parties. In this way it would, hopefully, become possible to combat inflation not through controls but through competition and sound macro-policies.

I think these hopes have materialized, even if the Social Democratic party over the last years has imposed many price controls.

*Question:* Did the Price and Cartel Office try to influence you in your position as the Minister of Commerce?

*Answer:* They resisted budget cuts and behaved in most ways as institutions can be expected to behave but I did not discover any efforts to disobey our guidelines.

*Question:* Did other groups try to influence you concerning the policy of price controls?

*Answer:* Not much – except businessmen who protested sometimes. The clamour for price controls – which made their dismantling difficult – was rather built into the political process.

*Question:* The management of the SPK was closely connected to the Social Democratic Party. Did this affect price control matters in any way?

*Answer:* Not that I am aware of although it is hard to distinguish between the pro-control stand that is natural for an agency like this one and the pro-control approach that is part of the Socialist baggage.

*Question:* In hindsight, do you regret the way you handled the policy of price controls?

*Answer:* Well, things can always be done better and it is always possible to be self-critical. Yet, given the political circumstances, I see few reasons to sink into any deep regrets. I think it is now a more widely held view that price controls are cosmetics, and although this assessment and reassessment follows from much rethinking on the role of government in general, I believe that it to some extent has to do with the fact that there was a gradual moving away from these controls during my government years and this process was underpinned by the debate that followed as the result of committee-work and research that we instituted.

*Question:* If your party were to return to power in the future, and you were again appointed Minister of Commerce, what would you do with the present policy of controls and the Price and Cartel Office?

*Answer:* Since 1982 the Social Democrats have had recourse to wide price control measures not because they really believe in that but as a surrogate for real anti-inflationary policies. It is part of the general disorientation of the left that characterizes also the Social Democrats in Sweden. We would do away with these controls. From this would also follow changes in the relevant authorities.

*Question:* What have you learnt from your experience of Swedish price controls as (a) a politician and (b) as an economist?

*Answer:* I see all my beliefs as well as my disbeliefs confirmed. The fine-tuners, a majority of the economists some fifteen years ago, were critical of our positive views of the market mechanisms. Now that is different. The marketeers, and I agree with their economic interpretations, however, sometimes forget that decisions must be made not only at the writing desk but also in Parliaments. Parliaments somehow change with a lag. Many politicians act upon beliefs distilled from what a previous generation of economists advocated or condoned.

## Appendix 4. The political economy of price controls. The Nixon experience

The American experience of wage and price controls during the period 1971–1974 provides a useful complement to the discussion on the political economy of Swedish price controls presented in Chapter 10. The American wage and price controls were introduced on 15 August 1971 by President Nixon. In a speech to the nation, he declared that wages and prices would be ‘frozen’ for a period of 90 days. This represented a dramatic departure from traditional stabilization policy in the United States. It was the first time in the history of the country that wage and price controls were applied during peacetime. Moreover these measures were adopted by a Republican politician who had previously been a firm opponent of any form of incomes policy.

This programme of price controls that was in force during the years 1971–1974 went through a number of different phases. The first phase which lasted from August to November 1971 was subsequently replaced by Phase II. Phase III started at the beginning of January 1973 and was designed to lead to the abolition of controls. However, due to the rising rate of inflation, Phase III led instead to the introduction of ‘Freeze II’ in June 1973. This period of tighter controls was, however, short-lived. Two months later, in August 1973, Phase IV was introduced during which wage and price controls were gradually relaxed. By 30 April 1974, all controls on prices and wages were abolished.

A detailed analysis of American stabilization policy during the years 1971–1976 has been carried out by Blinder (1979). Referring to the opinion polls, carried out by the Gallup organization into the attitudes of the general public towards wage and price controls before, during and after the period of controls, Blinder contrasts the views held by the general public and by

economists on the question of wage and price controls. Between 1958 and 1966, the interviewees were evenly divided into blocs: for and against controls. This period was characterized by relatively low inflation. However, the pattern changed after 1968 once inflation began to increase. Starting in January 1971, five opinion polls indicated that there was a majority in favour of a freeze on prices and wages as long as the Vietnam war continued. In June 1971, 50 per cent of those interviewed supported such a policy, 39 per cent were against while 11 per cent were undecided.

An opinion poll carried out several days after President Nixon's speech to the nation indicated that 91 per cent of those interviewed were aware of the new policy programme, 68 per cent gave it their support while only 11 per cent were opposed to it. The views of the American general public on wage and price controls was surveyed on six separate occasions during the period November 1971 – April 1973. The interviewees were asked whether they believed controls should be made more stringent or more relaxed or remain unaltered. On each occasion, there was a majority – usually an absolute majority – in favour of more rigorous controls. The seven opinion polls carried out, between 1974 and 1978, after the abolition of wage and price controls, indicated that there was substantial support for the introduction of new controls.

Blinder (1979, p. 111) argues that the Gallup polls indicated that the American people had continually demanded the introduction of price and wage controls for four years prior to their inauguration by President Nixon. Moreover the polls showed that the general public wanted existing controls to be made more restrictive and that it also hoped for their reintroduction after they had been phased out. According to Blinder, there was a general demand for wage and price control when they were not in use and for more stringent controls when they were in force.<sup>1</sup>

However, in Blinder's view, the Gallup institute would have obtained a different pattern of answers if their questions had instead been put to American economists. According to Blinder, an overwhelming majority of economists were probably against wage and price controls during the 1960s. This opposition had weakened by the early 1970s. However, the introduction of the Nixon wage and price controls undoubtedly gave rise to widespread criticism among economists.<sup>2</sup>

### *Richard Nixon*

The political side of wage and price controls is illustrated by the memoirs of Richard Nixon (1978). During his first year in the White House, i.e. 1969–70, both inflation and unemployment rose. During 1970, the Democrat-controlled Congress voted in favour of legislation that would give the President powers to control wage and price movements. Nixon viewed this legislation as a 'political play' on the part of the Democrats. An unwillingness to implement such legislation could then be interpreted in terms of the Republican admini-



stration's neglect of the country's economy. Nixon feared that a lack of policy action on his part would tend to reduce confidence and generate a feeling of uncertainty with regard to the future health of the economy. Consequently, he decided as a first step, to appoint an all-party commission to monitor movements in productivity and costs.

In early 1971, the American economy was still in the throes of a recession. Political patience began to run out. The White House was inundated with demands for action. Mass media criticism grew in intensity. Republican and Democratic members of Congress were confronted with growing demands for new measures that would tackle the twin problems of inflation and unemployment. Government control of wages and prices was increasingly considered as an appropriate solution. President Nixon tried to resist this growing tide of opinion. At the end of June, John Connally, the President's spokesman on economic issues, officially stated the Nixon administration was opposed to the introduction of wage and price controls.

In mid-July, a meeting was held between President Nixon and members of Congress in order to discuss the President's new policy on China. However, it soon became evident that the congressmen were primarily concerned with unemployment and inflation rather than with foreign policy. Following this meeting, Nixon decided that policy action was required. However, he remained uncertain about the type of measures to be introduced. He asked Connally to draft a proposal. Nixon had anticipated that Connally's proposal would represent a fairly radical departure from existing policy. However, he had not expected Connally to go so far as the proposal of total wage and price controls. Connally explained 'I am not at all certain that this program will work. However, I am convinced that any less drastic measures will certainly fail.'

President Nixon was also advised to delay the introduction of controls on wages and prices. An unexpected opportunity for policy action arose a week later in conjunction with a request from the British government to convert \$3 000 million into gold. The American reaction to this request would have major international repercussions. A crisis meeting was held attended by Nixon's leading economic advisors. This meeting led to the announcement of an economic programme that would have far-reaching repercussions: convertibility of the US dollar into gold was abandoned and a 90-day freeze on wages and prices was introduced.

Nixon was obviously highly concerned about the public reaction to his price and wage freeze. He was shortly to address the nation on television. Would he be met by headlines that stated 'Nixon makes a bold decision' or alternatively, would it be 'Nixon changes his mind'. As it turned out, it was the former. In his memoirs, he expressed delight at the reception given in the mass media to the introduction of controls on wages and prices. The Dow index rose on Wall Street and an opinion poll carried out six weeks later indicated that 53 per cent of the American people believed that the new policy had 'worked'.

Wage and price controls proved to be much more difficult to abolish than to introduce. Against the wishes of his advisors, Nixon declared a new freeze in 1973. The situation was summarized by George Schultz, one of the President's economic advisors: 'At least we have now succeeded in persuading everyone that we were right initially when we believed that wage and price controls did not provide the answer.' When controls were finally abolished in 1974, inflation and unemployment were higher than in 1971. Nixon also expressed a certain degree of nostalgia in relation to the good old days prior to controls.

What lessons does Richard Nixon draw from this period of wage and price controls? First, he points out that the decision to introduce controls 'was a political necessity and also extremely popular in the short run.' However, in the long run, he is convinced that it was 'wrong'. At the same time, he dissociates himself from the whole idea of wage and price controls which he considered 'philosophically' unacceptable. It was the economic and political circumstances of the period that forced him to introduce controls.

### *Herbert Stein*

Herbert Stein was one of President Nixon's closest advisors on economic affairs. Stein (1978) summarized his experience of the wage and price control programme. His views are more analytical and less biographical than those of Nixon.

Stein attempts to answer two questions:

1. How could a government that was 'almost religiously opposed to wage and price controls' bring itself to introduce such controls?
2. Could the failure of price and wage controls have been avoided if the controls had been administered differently? Alternatively could the failure have been avoided if the programme had been in the hands of a different group of decision-makers?

Stein draws attention to four essential factors that accounted for the introduction of controls as well as for their long duration. The first factor was the legislation passed in August 1970 that gave the President 'stand-by' authority to introduce wage and price controls. The purpose of this legislation was entirely political. Nixon was consequently placed in a difficult situation. The Democratic-controlled Congress was then able to place the blame for inflation at the door of the President. According to Stein, it was widely believed that Nixon would not implement this legislation. If this had not been the case, Congress would have been flooded by demands for exemptions from the legislation.

Once this 'stand-by' authority had been given to the President, it was only a matter of time before it would be brought into operation. The first opportunity arose six months later in February 1971 in conjunction with wage negotiations in the construction industry. The President asked the leadership of the construction workers' union to agree to a voluntary limitation of their wage demands. However, the union leaders feared that their own position would be undermined within the union if a voluntary agreement was reached. This dilemma was solved by the formal use of the President's 'stand-by' powers which gave an impression that the union had been legally forced to accept only limited wage increases. In reality, an agreement was reached by negotiation.

In March 1971, John Connally asked Congress on behalf of the administration to extend the stand-by legislation. The argument put forward in support of this measure was that the administration did not wish 'to appear so modest in its anti-inflationary endeavours that it was reluctant to include this definitive weapon in its armoury'. However, he did give an assurance that there were no plans to implement these controls. Five months later in August 1971, President Nixon introduced a complete freeze on prices and wages.

In Stein's view, these controls on wages and prices would never have seen the light of day if Congress had not given the President stand-by powers. The Republican administration would not have asked Congress to approve such legislation because of the political risks involved. As pointed out above, Stein maintains that if Congress had been convinced that the President would make use of these powers, opposition in Congress would have prevented the passage of such legislation. Stein concludes that 'political games should not be played with lethal economic instruments'.

According to Stein, the other major reason that accounts for the introduction of wage and price controls was the unrealistic expectations surrounding traditional stabilization policy measures in the USA. The American general public believed in the late 1960s that inflation could be reduced rapidly and relatively painlessly with the aid of conventional fiscal and monetary policy measures. These expectations had been largely created by successive governments – both the Democratic administration led by President Johnson and President Nixon's Republican administration. However, inflation proved to be more difficult to control than had originally been believed. At the same time, unemployment was rising. With a growing lack of confidence in the wisdom of economic forecasts, traditional stabilization policy was increasingly called into question. Wage and price controls were considered to provide a possible new solution. As Stein points out, governments continued to create unrealistic expectations with regards to the efficiency of stabilization policy. Subsequent failures in this area paved the way to the introduction of controls.

A third factor that operated in favour of controls can be found in the actual processes that form public opinion on economic policy matters. Stein now finds himself moving into a relatively controversial area of discussion. It is his contention that the demand for controls is stimulated and canalized by

influential politicians, intellectuals and commentators from the mass media. It was argued that some form of policy action was required, possibly along the lines of voluntary agreements. In this way, indirect support was given to compulsory, legal sanctions. The distinction between voluntary and compulsory controls disappeared. This 'miseducation of the public' helped to pave the way for the introduction of compulsory controls.

The fourth factor raised by Stein is the inherently dynamic nature of control policy. Initially, the administration had envisaged short-term controls – a freeze on wages for a period of 90 days. However it soon became apparent that it was politically and psychologically impossible to abolish controls after this 90 day period. The wage and price freeze had become the most popular economic policy measure in living memory. The freeze seemed to demonstrate to the public that inflation could be stopped directly by means of legal sanctions. As a result of this popularity, controls remained in force for a much longer period than the administration had originally intended.

American wage and price controls during the period 1971–74 have been criticized on the grounds that they were not administered with sufficient enthusiasm and commitment. Consequently, the value of the experience that was gained from this period of controls has been called into question. It is argued further that if the administration of wage and price control policy had been pursued more whole-heartedly by another administration, the results would have been correspondingly different.

In his discussion of this viewpoint, Stein draws a distinction between 'approving' and 'believing' in controls. Stein argues that there is nothing to be gained from the actual approval by administrators of the controls that they are obliged to enforce. On the contrary, there is a considerable risk that personal satisfaction in this area could lead to the excessive use of controls.

On the other hand, Stein is aware that those who administer controls on wages and prices – and who have gained a position of power and a sense of some importance in such a system – will also be positively disposed to the use of controls.<sup>3</sup> The agencies responsible for the administration of wage and price controls were allowed to work out the details of policy without any interference from the White House. On this point, there is no doubt at all about the commitment of the administrators to the detailed implementation of controls.<sup>4</sup>

In his summary, Stein draws two lessons from the American experience of the 1970s. Firstly one cannot play with the idea of wage and price controls without also being affected by them. The inefficiencies associated with such controls cannot be removed by the enthusiastic commitment of the bureaucracy to the task at hand. Secondly, the programme of wage and price controls was the result of 'heavy external pressure', that is strong political pressure. Stein considers that the major obstacle to the introduction of new controls is the absence of legislation similar to that which was available to President Nixon in August 1971.

George Schultz, the present Secretary of State, held a number of senior positions in President Nixon's administration. He also emphasizes the inherently dynamic nature of price and wage controls (Schultz and Dam, 1977). He poses the following question: 'Why is it not possible by means of detailed planning to devise a simple, once-and-for-all, program of controls that will apply to all future wage and price movements?'

His answer is straightforward. Each attempt at wage and price controls gives rise to a dynamic process characterized by counter-offers, negotiations and expectations from other groups in society. This interaction between public and private sectors creates a process of change which it is difficult to foresee. In such circumstances the programme of control will certainly not remain unaffected – it will be subject to a series of different phases, as in the American experience, prior to its abolition. Another major problem with controls is that once they have been withdrawn, they tend to create expectations regarding their possible reintroduction.

Schultz emphasizes the ease with which the political system is able to introduce controls. As the pressure on the administration to 'do something' increased during 1970 and 1971, expectations were raised regarding the introduction of some form of incomes policy package. At the same time, the expected change in economic policy had given rise to price increases in certain sectors. In Schultz's judgement, it was this internal momentum within the political process that gave rise to President Nixon's decision to freeze wages and prices.

The subsequent problem that arose was what to do after the initial 90-day freeze. There was always a tendency among regulatory agencies to make controls permanent. Trade unions and industry adjusted their behaviour accordingly. As a result, the bureaucrats responsible for the administration of wage and price controls found themselves in a position where they were trying to anticipate and adjust to the behaviour of employers and wage-earners. This process tended to create rules and strategies of a type that no one had been able to foresee when controls were initially introduced.<sup>5</sup>

Wage and price controls did not only affect the private sector. They also exerted an influence on general economic policy, particularly stabilization policy. In Schultz's view, the very existence of controls on prices and wages created an impression that inflation was not as serious a problem as had previously been the case. Consequently, it was no longer necessary to maintain as restrictive a stance on fiscal and monetary policy as would have prevailed in the absence of price and wage controls. As a result, the grounds were laid for a more expansionary economic policy which would lead to a higher inflation rate and thereby undermine the very purpose of controls. Interest groups opposed to a restrictive stabilization policy used controls to further their case.

In his summary, Schultz emphasizes 'the temptation to introduce wage and price controls and the difficulty of getting rid of them'. As was the case with Nixon and Stein, the political element underlying wage and price controls receives considerable attention. However, Schultz shows much more clearly than either Nixon or Stein how wage and price controls tend to develop their own momentum and generate processes and patterns of behaviour which were not envisaged at the time of the initial introduction of controls in August 1971.

### *Conclusions*

The writings of Nixon, Stein and Schultz clearly demonstrate the crucial role played by the political process in the generation of wage and price controls in spite of the opposition of the Nixon administration to the introduction of such controls. The economic policy makers did not consider the controls to provide the right solution to the administration's economic problems. However, wage and price controls represented the political answer to inflation and thereby legitimized such measures.

Other western countries that were the subject of wage and price controls during the 1970s have not provided us with similarly frank accounts of the operation of price control policy as those of Nixon, Stein and Schultz. All three had a responsibility for economic policy. It is hard to believe that the structure of political incentives that applies to the United States does not also have a bearing on the political life of other democracies. It should therefore be concluded that the operation of the political process provides us with a central part of the explanation for the widespread introduction of wage and price controls in many industrial countries during the 1970s.

### **Notes**

- 1 Cf. the Swedish opinion polls summarized in Table 10.1.
- 2 Blinder's own econometric analysis of the effect of wage and price controls 1971–74 leads to a highly critical conclusion. The programme represented 'a remarkable act of national self-flagellation', see Blinder (1979, p. 132).
- 3 Stein mentions Galbraith's support for price controls in this context. During the Second World War, Galbraith held a leading position in the agency in Washington concerned with the administration of price controls.
- 4 The principal individuals responsible for economic policy including Nixon, Schultz and Stein, did not 'approve' of controls but, according to Stein, they believed strongly that controls could be used to lower the rate of inflation. However, the intention was that controls would be administered in such a fashion that the American economy would not become subject to a permanent control regime. The eventual abolition of controls was always considered to be a primary requirement. Consequently, Stein and his colleagues had no wish to establish a large and permanent system of bureaucratic control.
- 5 Cf. the descriptions of the operation of price controls in Chapters 2–6.

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