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The Coming Demand Surge Brings Back Memories of 1970s Inflation

The lifting of lockdowns and easy monetary and fiscal policy will likely lead to much higher prices.

By William N. Walker
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Protesters march against inflation in Chicago, October, 1973.
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The last bout of inflation the U.S. experienced was in the 1970s. Commentators duly note this historic reference but don't really understand it—many weren't yet born, and few were adults, at the time. It was no mere inconvenience; it was a catastrophe.

During the first quarter of 1973, consumer food prices shot up at an annual rate of nearly 30% and the wholesale price index for farm products rose at an annual rate of 52%. Red-meat prices surged at an annual rate of 90% during the first quarter. Home heating oil prices nearly doubled in that quarter alone, and soybean prices rose to record highs.

The Journal reported recently that "commodity markets are roaring" and noted dramatic increases in prices of crude oil, copper and nickel as examples of what some predict to be "a supercycle . . . when prices of livestock, grains, metals, oil and gas all climb for years, even decades."
That article that could have been written in the spring of 1973, when demand also exploded, putting such severe pressure on supplies that within a matter of months, prices of virtually all commodities—foodstuffs, minerals and petroleum—would soar. By the summer, the rate of inflation had shot up to 11%. It would continue at near double-digit annual rates until 1980, when the Federal Reserve, led by Paul Volcker, raised interest rates to nearly 20%. That crushed inflation but ushered in a harsh recession.

There are eerie parallels today. In 1973, the U.S. was coming off a two-year experiment in wage and price controls, which artificially depressed prices and muted signals that the economy was overheating. Then, too, the Fed pursued an easy-money policy, keeping interest rates low—though considerably higher than now, and without today's purchases of bonds and mortgage securities.

By the end of 1972, before the inflationary jump, the U.S. economy seemed even stronger than it is now, growing at an annual rate of more than 8%. Unemployment was down to 3.4%, and inflation was a seemingly manageable 5.6%. The prepandemic 2020 U.S. economy was also very strong, growing at a 3% annual rate, with historically low unemployment of under 4% and inflation hovering around only 1%.

In 2021 we're emerging from the pandemic shutdown, which cratered growth and slammed the economy—depressing price pressures, not unlike what the price-control program did 50 years ago. Today's Fed policies are even more expansive. And Congress has just enacted a $1.9 trillion stimulus bill—on top of earlier relief bills costing another nearly $2 trillion, a lot of which remains unspent and will continue to fuel demand this year and beyond.

Does that mean that we're doomed to repeat the earlier disaster? Today's fiscal stimulus clearly dwarfs anything even considered in the 1970s. Moreover, there is a palpable excitement that Americans will finally be able to discard the shackles of Covid and spend the money they saved last year and the wages they're starting to earn again. So demand is likely to soar.

As was the case 50 years ago, there are constraints on supplies: shipping delays are blocking deliveries; manufacturers can't get parts to ramp up production; real-estate values are skyrocketing, while lumber shortages constrain home building; and most commodity prices are rising precipitously. Experts reassure us that the annual inflation rate will rise only to about 2%. We hope they're right, but when demand increases faster than supply, prices tend to go up.

One relief is that the Biden administration won't repeat the colossal mistake President Nixon made in June 1973, when, faced with mounting anger over inflation, he imposed a new 60-day price freeze. The discredited Economic Stabilization Program of the 1970s, which tried to reduce inflation through government-enforced price controls, is an object lesson of a failed government policy that is properly consigned to the ash heap of history. Congress let the president's authority to impose such controls lapse in 1974.

Inflation may be in check today. But once it gets its claws into a demand-fueled, supply-constrained economy, it can become a scourge, and history teaches that there’s not an easy or painless way to tame it.

Mr. Walker is a retired diplomat and lawyer and author, most recently, of “Target Switzerland: A Paul Muller Novel of Political Intrigue.” He served as general counsel and deputy director of the federal Cost of Living Council, 1972-74.