The Legacy of Nixonomics

Fueled by the Vietnam war, the U.S. economy was booming when Richard Nixon ran for President in 1968. But the war had also touched off a vicious wave of inflation—and Nixon coupled his campaign pledge to extricate the nation from its Indochinese nightmare with a heady promise to stop the price spiral without tumbling the economy into recession. "Peace with prosperity!" went the slogan that helped elect him.

Six years later, the departing President admitted in his resignation speech last week that his goal of "prosperity without inflation" had eluded his Administration. Nixon left the White House with the economy slumping, unemployment rising and inflation eating away at the U.S. dollar at twice the rate suffered during his first months in office (chart).

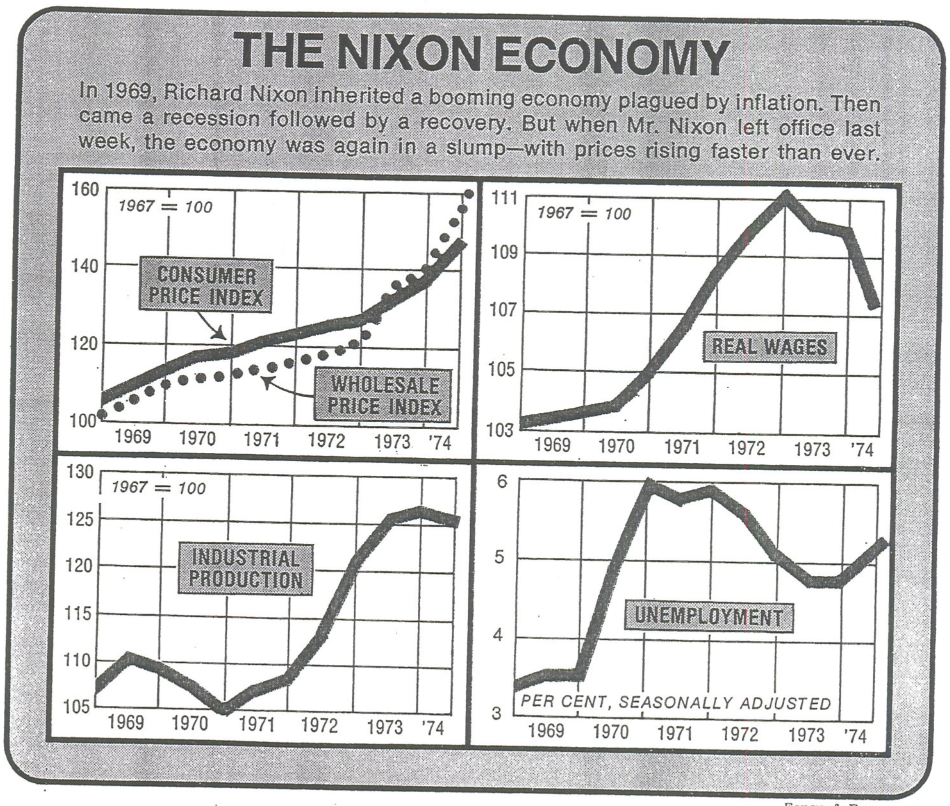
Clearly, Nixonomics—that paradoxical amalgam of reluctant jawboning, full-scale government intervention and old-fashioned Republican orthodoxy—has been by and large a failure. Not even Nixon's stunning decision in August 1971 to freeze wages and prices for the first time in the nation's peacetime history was enough to put a lid on inflation. And his widely heralded plans for welfare reform and revenue sharing never really did get off the ground. Indeed, the only economic area in which he can claim real success is international trade. His two decisions to devalue the dollar bolstered American industry's fading strength in world markets.

A LACK OF PHILOSOPHY

Where did Nixon go wrong? It certainly wasn't in any exaggerated devotion to a particular economic ideology. Rather, it was precisely the opposite—a virtual lack of any fixed economic philosophy beyond the traditional Republican distaste for government intervention (and even this Nixon was willing to abandon when he felt the time was right).

"It was not only that he was disinterested in economics," notes Walter Heller, chairman of President Kennedy's Council of Economic Advisers. "He disliked economics." As President, Nixon seems to have regarded economic policy as something to be exercised all too often for political advantage. "The Nixon economic policies were circumscribed by political debts," says Otto Eckstein, a CEA member under President Johnson. "Every corporate call by his fund raisers gave away a small piece of economic policy."

Of course, the nation's current economic woes aren't entirely Nixon's fault. "America's economic-policy machinery simply cannot control the weather, the Arabs or the superinflationary economic policies of other countries," points out economist Albert H. Cox Jr. What's more, notes NEWSWEEK's chief economic correspondent, Rich Thomas, "Any President in a period of inflation confronts one nasty fact: there is simply no proven way to halt inflation without putting people out of work and business through the wringer."



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That did not keep Nixon from trying—with a policy called "gradualism." The theory was that if the government applied the conventional anti-inflation policies of budgetary and monetary restraint gradually and with scientific precision, that would produce just enough of a squeeze to curb spending while avoiding a recession. The problem, however, was that business and labor leaders read the newspapers. Knowing that this kid-gloves treatment was designed to keep them from getting hurt, they could safely ignore it.

So the inflation rate continued to climb and the government found itself forced to keep squeezing the economy longer than it had planned. The result was stagflation—prices kept rising, unemployment skyrocketed and the nation found itself in its first recession since the Eisenhower years.

By early 1971, with unemployment at a ten-year high and inflation as bad as ever, memories of the late-1950s recession that helped thwart his 1960 bid for the Presidency tempted Nixon to switch his approach. With the end of his first term in sight, Nixon coolly rejected a lifetime of laissez-faire pronouncements and announced that he had become a Keynesian—a believer in the doctrine that the economy could be "tuned" by fiddling with taxes and government spending. And the President ordered large increases in government spending to pump up the economy.

By August inflation was clearly getting out of control, and Nixon dramatically announced a 90-day wage-price freeze in hopes of containing the inflationary pressures ravaging the now-surging economy. The controls worked at first; but ultimately they proved a disaster.

TOO HOT TO HANDLE

For one thing, the domestic economy was boiling at a rate impossible to cool off with wage and price controls. Moreover, at about the same time, grain-crop failures overseas triggered a worldwide explosion in food prices. And then in late 1973 and early '74, the Arabs stunned the world by quadrupling the price of oil.

In response, Nixon's shell-shocked planners gave up trying to control economic events with precision. Thus, as effortlessly as he had converted to Keynesianism, the President reverted back to what his advisers called "the old-time religion"—the idea that a stiff dose of unemployment and reduced demand would bring inflation to heel.

That has yet to happen. Whether it ever will, of course, is no longer Richard Nixon's problem—though the damage his sudden policy shifts did to the American economy remains, in part at least, his legacy. His economic stewardship was cursed with bad luck, to be sure, but it was also crippled by his habit of swaying in the winds of expediency. "He let his political instincts rule over his economic instincts," says Heller. "That was his major problem."