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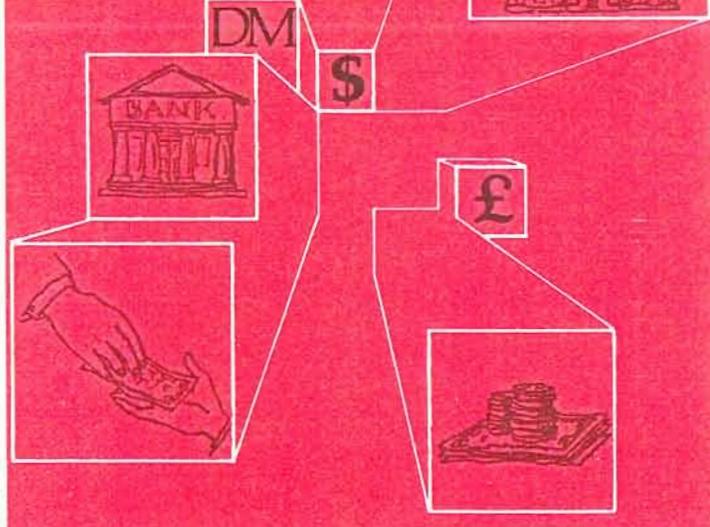
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VOLUNTARY
INFLATION
RESTRAINT:
A COMMENTARY

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for the Philadelphia Region
&
The Fed in Print

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**VOLUNTARY INFLATION RESTRAINT AND
CORPORATE SOCIAL RESPONSIBILITY**

Commentary by David P. Eastburn

**INTERNATIONAL BANKING
IN PHILADELPHIA**

Janice M. Westerfield

. . . International operations are growing at Philadelphia banks.

**A NEW JOB MAP
FOR THE PHILADELPHIA REGION**

John Gruenstein

. . . The shift of employment outward from Center City may call for new initiatives in transit, tax, and urban policy.

THE FED IN PRINT

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COMMENTARY

VOLUNTARY INFLATION RESTRAINT AND CORPORATE SOCIAL RESPONSIBILITY*

By David P. Eastburn, President
Federal Reserve Bank of Philadelphia

What responsibility does a corporation have voluntarily to fight inflation? I suppose there is not a corporate official in the country who is not asking this question today. The answer will largely determine the success of President Carter's anti-inflation program.

The arguments pro and con have been made for years. Pro: corporations stand to gain along with the rest of us if inflation can be brought under control. Con: a corporation's main job is to make profits for its stockholders, and competition prevents it from waging the inflation fight on its own (President Carter's analogy of one person's sitting down in the stadium while everyone else is standing).

I have nothing to add to these arguments, but I believe there is an important aspect of

the question which has been overlooked. This is the impact of inflation on activities of corporations to improve social conditions. High inflation rates threaten to reduce these activities severely.

To explain why this is so, let me paint with a rather broad brush a contrast between two eras. A decade or so ago, perhaps a little less, a debate was raging about corporate social responsibility. Business journals were full of articles about whether corporations should help solve such problems as hard-core unemployment, slum housing, and lack of minority participation in business, or whether, simply, the "business of business is business." The *New York Times Magazine* published an article by the Nobel prize winning economist, Milton Friedman, which argued that corporate officials who use their corporate power to try to solve social problems are playing fast and loose with stockholders' money and hastening the day of socialism. The Com-

*Adapted from remarks delivered before the Business Honor Society Colloquium, La Salle College, Philadelphia, Pennsylvania, November 14, 1978.

mittee for Economic Development cast its enlightened eye on the question and concluded that corporations *should* actively try to improve social conditions because it is in their long-run self-interest to do so.

The debate was interesting, especially because of the environment in which it took place. The nation had just gone through an exciting, if stormy, period. Civil rights had taken a tremendous forward stride, a war on poverty had been declared, and the Vietnam war had raised sensitivity about moral issues to new heights. The economy was growing so rapidly that the material well-being of those in lower income groups was measurably improved; official definitions of poverty were successively revised upward.

In short, the debate about corporate social responsibility took place in an era of great social concern and considerable social improvement. It was a time when people were looking outward to other people's problems. At the risk of overdrawing the point, one might say it was an era of growth and generosity.

Since then, corporate social responsibility has become an accepted fact. It is seldom debated. It has become institutionalized. Corporations are engaging in a myriad of activities to improve their communities and to help the disadvantaged.

But now we have serious inflation and the threat of serious inflation into the indefinite future. In contrast to the expansionary, outward-looking environment of the earlier period, we face the prospect of two developments, both of which would be inimical to the exercise of corporate social action.

One is the pressure of inflation on real corporate profits. Although it might appear that profits are rising, this appearance is illusory, because profits are overstated as a result of current accounting practices. Corporate officials see through this money il-

lusion, and inflation uncertainties make them more cautious. Furthermore, if the President's program fails, a likely course would be to fight inflation by overall monetary and fiscal action alone. And success in bringing inflation under control along that course would require a recession or at least very slow growth for a long period. What all this adds up to is an unpromising outlook on the *wherewithal* for corporate social action.

The other development is the impact of inflation on corporate *willingness* to engage in these activities. Inflation spawns an attitude of inward-looking and selfishness. Businessmen accuse labor of pushing up wages; labor accuses business of raising prices to make bigger profits; all accuse government. There is nothing new here, but inflation aggravates it. What is new, and even more symptomatic of the mood of the country, I believe, is the emergence of a variety of proposals to slash taxes. I am convinced that many sincere advocates of these proposals are motivated by a concern to limit the growth of government or a desire to stimulate economic growth. But I am also convinced that at least as many are concerned only about how inflation is picking their pockets.

Corporations cannot help but be touched by all this. Inflation forces them to look to their immediate self-interest rather than their long-run welfare. It could force them to take the position that their business is only business. It could win the ideological war for Professor Friedman after all.

So, for those who would like to see society continue to move ahead in solving its many social problems and who are eager to continue harnessing the power of corporations to that end, there is real reason for fighting inflation. I would hope that corporate executives will find this rationale further justification for entering the lists.