The Impact of Economic Decisions by American Presidents Series

Richard Nixon - Price Controls and Ending the Gold Standard

Most decisions by American presidents and other world leaders do not have an immediate impact on the economy, especially regarding the macroeconomic issues of employment and inflation. For example, President Franklin Roosevelt's bank holiday, President John Kennedy's tariff on imported steel, and President Ronald Reagan's Economic Recovery Tax Act had limited immediate effects on the economy, but their long-term effects were significant. The accomplishments or problems of a previous administration may impact on the administration that follows.

For example, President Biden faced criticism about the economy during his administration. The jobs created with the Bipartisan Infrastructure Law and the interest rate policy of the Federal Reserve Bank to lower inflation did not show results until years later. The drop in Real Disposable Income from the administration of President Trump is another example. Real Disposable Income is a measure of income that is adjusted for inflation. The drop between the administration of President Bident and Trump is the result of extended unemployment benefits, people working from home during the pandemic when businesses were closed, and stimulus checks from the government. The economic transition following the end of the pandemic had a significant impact on the economy.

President	GDP Growth	Unemployment Rate	Inflation Rate	Poverty Rate	Real Disposable Income
Johnson	2.6%	3.4%	4.4%	12.8%	$17,181
Nixon	2.0%	5.5%	**10.9%**	12.0%	$19,621
Ford	2.8%	7.5%	5.2%	11.9%	$20,780
Carter	4.6%	7.4%	**11.8%**	13.0%	$21,891
Reagan	2.1%	5.4%	4.7%	13.1%	$27,080
H.W. Bush	0.7%	7.3%	3.3%	**14.5%**	$27,990
Clinton	0.3%	4.2%	3.7%	11.3%	$34,216
G.W. Bush	**-1.2%**	**7.8%**	0.0%	13.2%	$37,814
Obama	1.0%	4.7%	2.5%	**14.0%**	$42,914
Trump	2.6%	6.4%	1.4%	11.9%	$48,286
Biden	2.6%	3.5%	5.0%	12.8%	**$46,682**

This series provides a context of important decisions by America's presidents that are connected to the expected economic decisions under the second administration of President Trump. The background information and questions provide an opportunity for small and large group discussions, structured debate, and additional investigation and research. They may be used for current events, as a substitute lesson activity or integrated into a lesson.

In the case study below, have your students investigate the economic problem, different perspectives on the proposed solution, the short- and long-term impact of the decision, and how the decision affects Americans in the 21st century.

The Economic Problem:

1. The world's economy collapsed as a result of World War II. The Bretton Woods Agreement provided stability with a fixed exchange rate of $35 U.S. dollars to an ounce of gold. The scarcity of the quantity of gold in the world has provided stability for paper money, which could easily be increased by printing more money. The fixed exchange rate of dollars as the reserve currency of the world with the option to exchange gold for dollars or dollars for gold in the market, supported global trade, economic growth, and stability in the balance of payments for each country. Bretton Woods was an important meeting of international cooperation to prevent another global depression that was caused by debt, tariffs, and speculation.

   Bretton Woods assembled more than 700 delegates from 44 countries, including the brightest and most distinguished economists in the world. It also established the International Monetary Fund to support developing economies with diversification, trade, and stability. The gold of most countries was at the Federal Reserve Bank in New York from the beginning of World War II, so it was easy to physically move gold from one vault to another. The strongest economies after World War II were in North America and Western Europe.

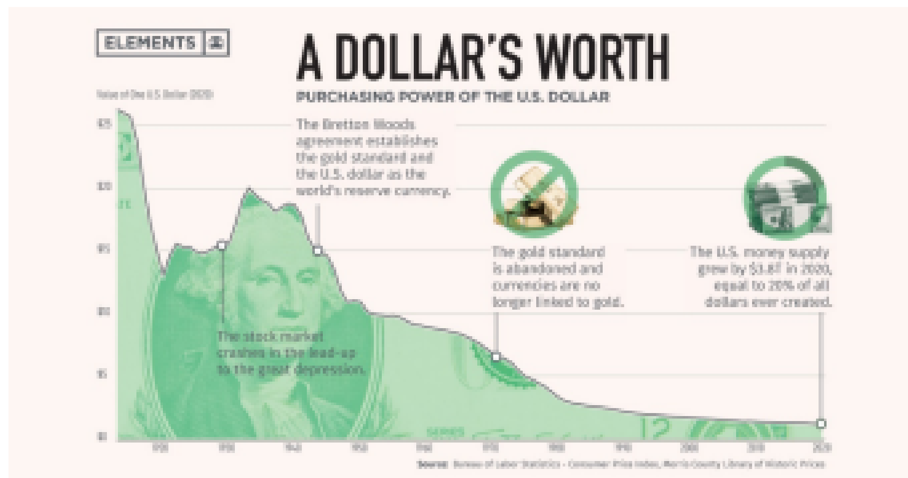
2. By 1960, the U.S. economy began facing new challenges from a dramatic population increase (Baby Boomers), national debt, Cold War (diplomacy and tension), trade deficits, higher unemployment and inflation. Economists introduced new research and economic theories. The ideas of John Maynard Keynes that were seen as helpful to the challenges of the Great Depression and World War II were questioned by Milton Friedman and Paul Samuelson and other economists. The problem for economists was a debate over the relationship between full employment and inflation. The debate was about Keynes' "General Theory" of an economic model, the role of institutions to address the problem, income stabilization with full employment, the influence of the amount of money in circulation, and the role of welfare. The demand for dollars increased as a result of the cost of the Vietnam War, the social programs that were part of the Great Society, and the increased consumption of the Baby Boomers.

3. By 1970 nations were purchasing more dollars to finance their expenses, which increased the amount of dollars in circulation to four times the amount of gold in reserves. As a result, the dollar was overvalued and very strong. This situation negatively impacted our balance of trade with other countries, and, in 1971, the United States reported its first trade deficit. In addition, Nixon's administration faced an inflation rate of 4.7%, which was an increase of 50% from the expected rate of 3% with a lagging GDP growth rate of 2%. President Richard Nixon understood the implications of prices increasing faster (inflation) than spending (GDP).

4. When inflation increases, the purchasing power of the dollar decreases. A simple solution would be to devalue the dollar. However, since the U.S. dollar was pegged to gold at $35 an ounce as a result of the Bretton Woods agreement, this was not possible. The situation became critical when Britain requested selling $3 billion dollars it had from a trade surplus for gold. However, the United States had only $10 billion in gold. As the supply of dollars increased over the quantity of gold, the United States Treasury feared that countries might request their gold, and the United States would not be able to meet their demands. An international crisis could result.

Activity #1 - The Strong Dollar

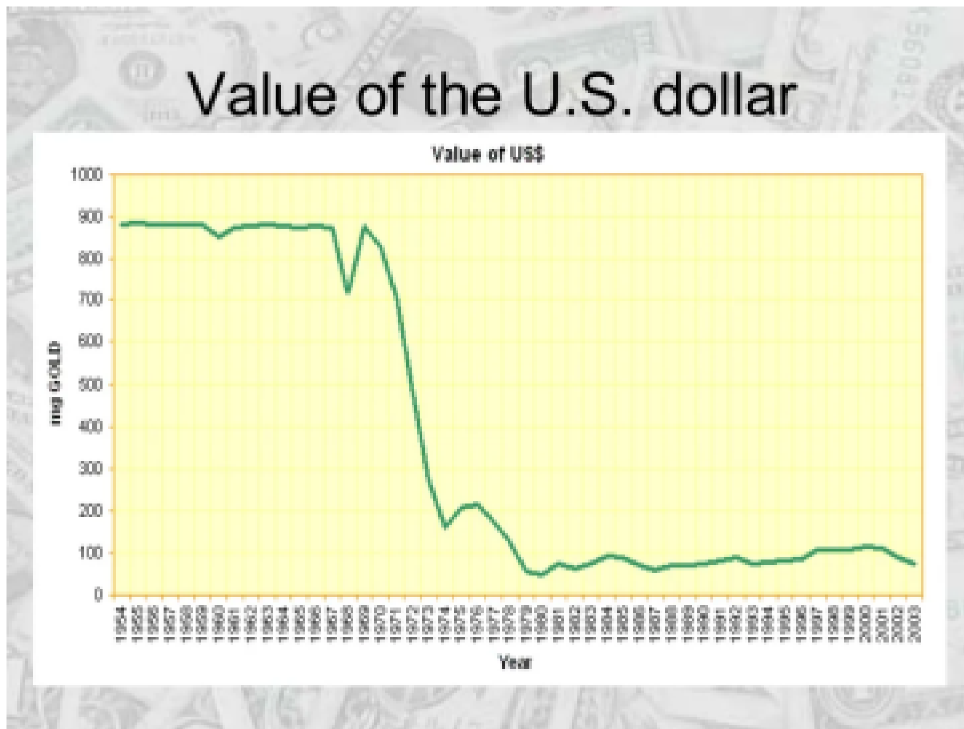
Examine the graph below for the years 1950-1970. Calculate the percent decline in the purchasing power of the dollar. How does a weaker dollar affect trade and the national economy? What are the advantages and disadvantages of a stronger and weaker dollar?



Activity #2 - The Weaker Dollar

Examine the data in this chart, especially for the years 1960-1980. The amount of gold reserves (left axis) is constant until 1971, when the value of the dollar declined. Which events in the 1960s likely affected the weakening of the U.S. dollar?

1. Which decisions or events in the 1970's contributed to the decline in the dollar?
2. How does a weaker dollar affect the economy differently for consumers and investors?



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Solutions to the Problem

President Lyndon Johnson responded to the “small" (18%) decrease in the value of the dollar in 1968 with a temporary (one-year) surcharge of 10% on income tax payments. The purpose of the additional tax was to reduce or stabilize the 3% rate of inflation. However, even with the surcharge, inflation increased to 4.7% within the year. On August 25, 1969, the federal funds rate was at 9.75%, the highest level since World War 2 and 6.5% above the GDP growth rate of 3.1%. A high federal funds rate increases the cost of loans, which slows spending and economic growth. This often leads to higher levels of unemployment and a recession. When Arthur Burns, Chairman of the Federal Reserve Bank, informed Nixon that traditional monetary and fiscal policy tools were not working, President Nixon extended the tax surcharge through 1970. With the presidential election looming in 1972, Nixon knew that he needed to control the rising rate of inflation and avoid causing a recession if he wanted to be re-elected to a second term.

1. **President Nixon called for a secret meeting at Camp David to freeze wages and prices.** He knew he needed to make a bold decision and wisely sought the perspectives of economists with different points of view. He would freeze prices and wages for 90 days.

On August 15, 1971, President Nixon addressed the nation from the Oval Office with his historic decision, Executive Order 11615:

1. Wage and price controls for 90 days
2. Ending the Bretton Woods Agreement on converting dollars to gold
3. 10% surcharge tax on tariffs

Activity #3 - Interviews/Oral History

Invite students to interview senior citizens who will have different perspectives as investors, bankers, union workers, homeowners, etc. on the “Nixon Shock.” For example, I was a high school teacher in New York City earning $5,500 a year. Prices were high from inflation, and I was looking forward to a 20% salary increase, about $1,000, on September 1, 1971. As a result of the Wage/Price Freeze my 1969-70 salary was frozen as was the pay scale for another year. In 1973, the price of gasoline increased from about 40 cents a gallon to more than 60 cents and gas was rationed. The energy crisis was the result of an embargo by OPEC against the United States for supporting Israel in the Yom Kippur War. After the embargo was lifted the higher cost of energy continued contributing to unemployment and continuing inflation. Economists call this ‘sticky prices’. This became known as stagflation.

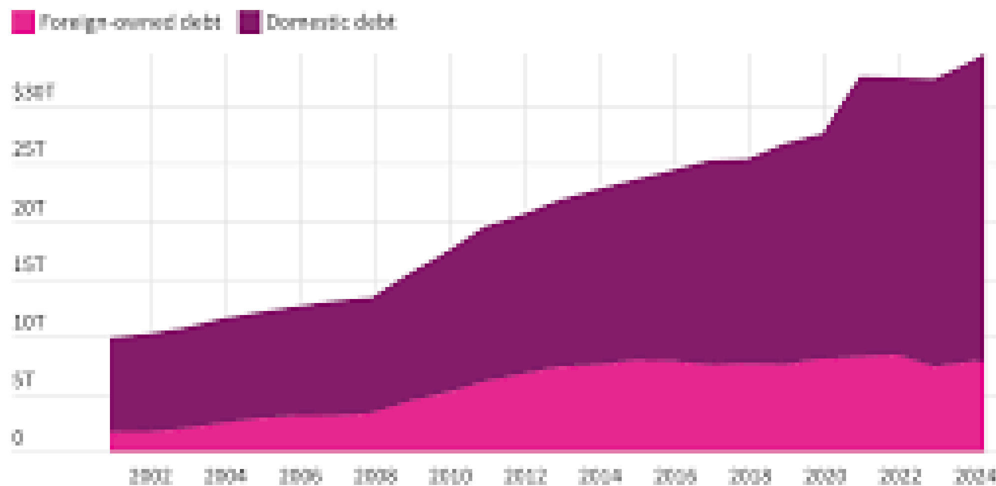
The Fed Funds rate in August 1971 was at 5.75%, about three percent higher than the GDP rate of growth. One of the objectives of the “Nixon Shock” was to force other countries, especially China, to revalue their currencies to allow for a competitive free trade market for the United States. The stock market jumped 4% on August 16, but President Nixon’s decision to allow gold to be bought and sold at market prices would lead to unexpected changes. The wage and price controls and tariff surcharge were lifted by the end of 1971.

2. **The impact of ending the Bretton Woods agreement on a fixed price of gold at $35 made the U.S. dollar the reserve currency of the world**. The implication of this for the economy was that countries would now purchase U.S. government bonds because they were guaranteed by the fact that the United States had never defaulted on a bond or debt. In times of instability and international crisis, countries purchased dollars. President Nixon won the 1972 election by a landslide but the negative effects of the ‘Nixon Shock’ would return in 1973.

Activity #4 – Bonds (Dollars) held by Foreign Countries

At its peak in 2014, foreign-owned securities made up over a third of total US debt.

Total US national debt, separated by ownership, adjusted for inflation, 2000–2024



Domestic-owned debt includes domestic public debt and intragovernmental debt. From 2000 to 2023, annual totals are based on data from December, while the 2024 data is updated through April. Inflation adjusted to the 2023 calendar year.
Source: Treasury Department

History of the Gold Standard

Foreign countries own about $8 trillion of the $35 trillion debt of the United States.

1. If foreign countries did not purchase U.S. government bonds, how would the United States finance its national debt?
2. What are the implications for the United States if the world returned to gold as the reserve currency, a basket of currencies supervised by the International Monetary Fund, or another currency (China, cryptocurrency) became the next reserve currency?
3. What scenarios might lead to countries abandoning dollars as the reserve currency in times of political instability or an international crisis?

3. **The 10% Tariff solution made imported goods more expensive.** This was an attempt to get other countries, especially Japan, to raise the value of their currencies to make goods produced in the United States competitive with those of other countries.

   "On August 15, 1971, President Nixon issued Proclamation 4074, in which he declared a national emergency and imposed a 10% ad valorem supplemental duty on all dutiable articles imported into the United States. That evening, in a televised address to the nation, President Nixon outlined his new economic policy, the targets of which were unemployment, inflation, and international speculation. He addressed the supplemental duty specifically.

   I am taking one further step to protect the dollar, to improve our balance of payments, and to increase jobs for Americans. As a temporary measure, I am today imposing an additional tax of 10% on goods imported into the United States. This is a better solution for international trade than direct controls on the amount of imports."

Many U.S. companies tried to keep prices the same to encourage consumer spending, especially for furniture, cars, and appliances. They offered rebates and interest free loans to counter the effects of the tariff. The danger was that other countries would boycott American products. The result was the Smithsonian Agreement (The meeting was held in the Smithsonian Museum) in December 1971 which adjusted the value of currencies to support the economy of the United States.

"The Smithsonian Agreement of the Group of Ten consisted of a series of interrelated measures to help resolve balance of payments problems, to restore more settled conditions to exchange markets, and to provide a framework for longer term reform. These measures included agreement by the United States to propose to the Congress a suitable means for devaluing the dollar in terms of gold as soon as a related set of short-term trade expansion proposals was available for Congressional scrutiny, and to suppress the 10 percent import surcharge and related provisions of the job development credit."

1. Was the Smithsonian Agreement one of the most significant meetings on the world's economy?
2. How did the adjustments to the major currencies in the world affect trade?
3. How did the three solutions of President Nixon lead to the recession of 1973-74?
4. Should President Nixon have used a laissez-faire strategy or was his decision to negotiate a deal that was favorable to the interests of the United States the preferred solution at the time?

Activity #5 - The Popularity of Credit Cards

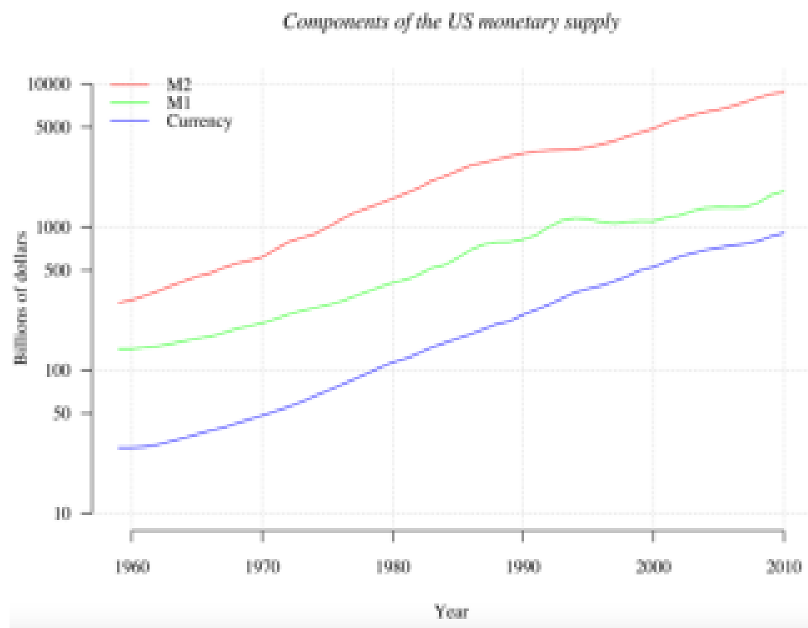
Although installment buying dates back to the 1920s, credit cards issued by banks only became popular around 1970. A credit card issued by a bank gave people a line of credit for money to spend. This led to revolutionary changes in the way people lived. They renovated homes, purchased second cars, traveled more frequently, and purchased more goods in the popular suburban malls. More people were getting college degrees, and more women were entering the workforce than at any other time in our history.

Gather information about the new technologies of how credit cards and money markets increased the supply of money spending, and the ease of transactions. Credit Cards, direct deposits, and ATM machines allow consumers to have instant access to money and to spend it more quickly than waiting for days for a check to clear or withdraw money from a bank during business hours. Credit cards may also increase the debt of consumers.

1. How did the banking industry change to 'create' new money in the economy?
2. What is the economic impact of making transactions easier and faster?

In the chart below, currency represents coins and dollars, what we call cash. **M1 money** represents currency plus money in a checking account which can quickly be exchanged for cash. **M2 money** represents money that requires going to the bank or waiting more than one month to convert the money to cash. (i.e. certificate of deposit)

Calculate the slope of the graph in dollars and also by the annual percentage change.



3. How did this contribute to inequality, consumer debt, and inflation?
4. What is the difference between installment credit and revolving credit?
5. How did the credit card change our standard of living?
6. What were the consequences of higher unemployment and full employment?
7. How did two income households affect the supply of money?

The Evolution of Consumer Credit in America

Activity #5 - Worker Productivity and Compensation

Workers generally do not receive a pay raise merely because it is a new year or because inflation has increased the cost of living. Sometimes cost-of-living raises are part of a negotiated agreement between workers and management. Companies will reward workers with pay raises when they produce more or when companies earn larger profits. Technology, health, education, experience, etc. are all variables that increase the productivity of workers and by extension, the profits of companies.

1. What information is provided in the graph?
2. What are several reasons for an increase in productivity by workers?
3. Should a worker be paid on the amount of work they produce or the wage they agreed to when they hired?
4. Why do the red and blue lines diverge after 1970? Why is there a significant gap between what workers are producing in one hour and what they are paid?

Reflection Questions:

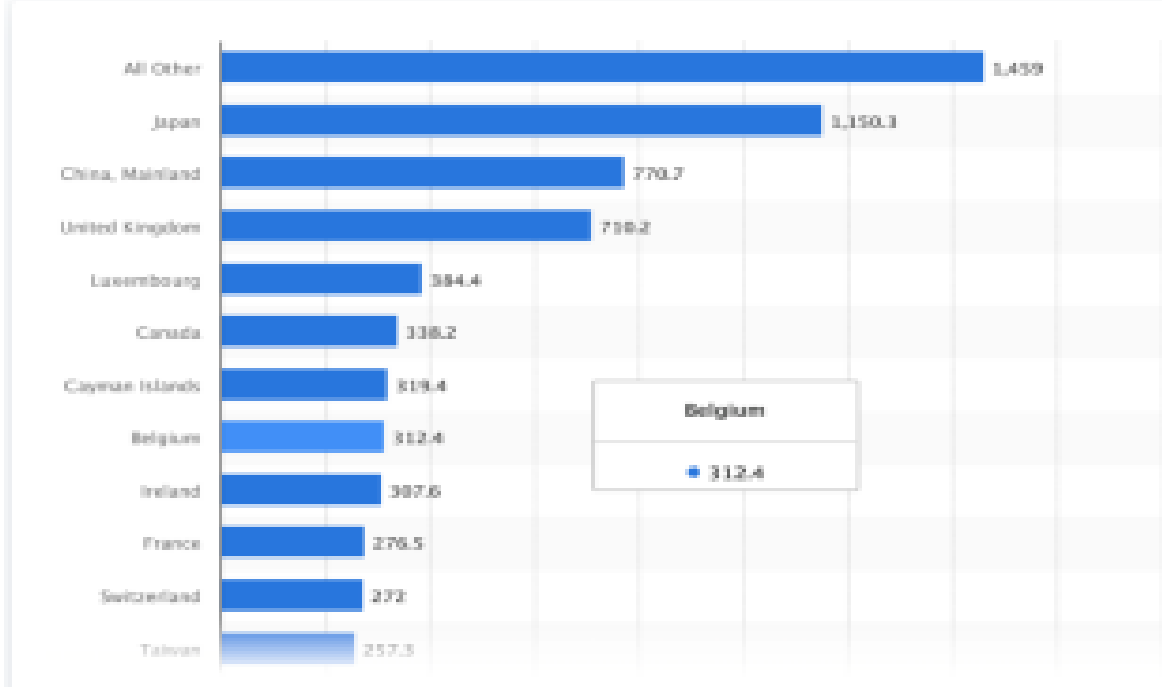
5. How can high school students become more productive in their social studies class? (i.e. better grades, complete additional assignments and projects)
6. Should a teacher be paid based on the output (grades) of the students in their classes?

How did taking the U.S. Dollar off the gold standard affect the economy?

The immediate impact of separating the value of the dollar from a fixed exchange rate of $35 was that the new value of gold increased by 10% to $38 an ounce. It took about four years for the global economy to stabilize and accept dollars as the new reserve currency (or safety net) in the event of a crisis. The supply of gold increased significantly after 1971 with about half of the current supply of gold being mined since the 'Nixon Shock'.

The economic power of the United States is significant because countries have looked to the United States and the International Monetary Fund (IMF) in times of severe economic crises. This power of having countries purchase U.S. dollars has enabled the United States government to enforce sanctions and prevent the gold kept at the Federal Reserve Bank in New York City from leaving.

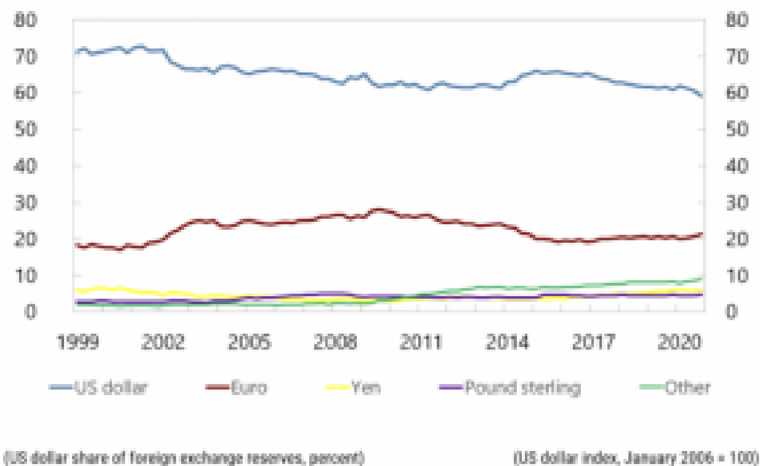
Major Foreign Holders of U.S. Treasury Securities as of April 2024



Source:

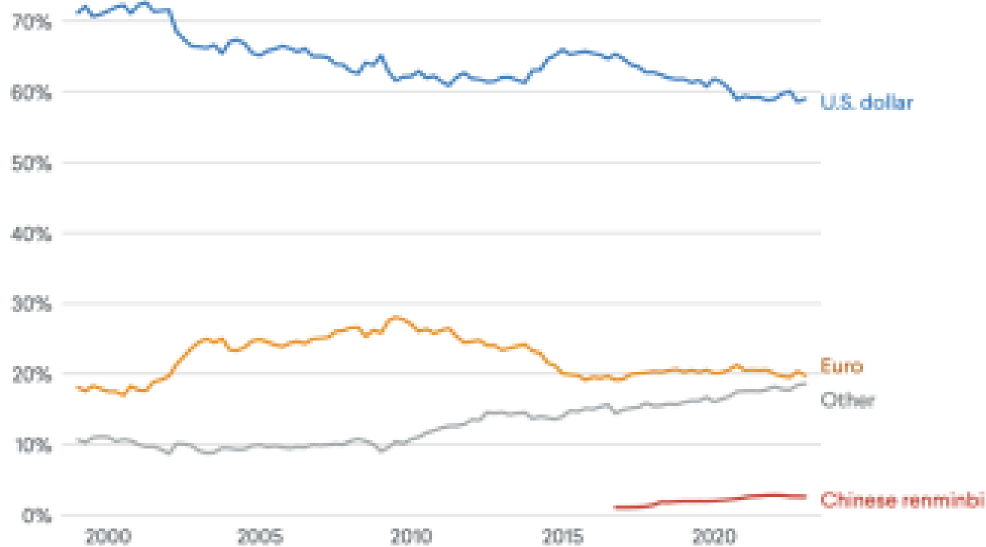
1. How do countries buy dollars? How does this affect our economy?
2. Is it possible for foreign countries to have too many U.S. dollars?
3. How would the decision of other countries to adopt a different currency affect the economy of the United States?

Demand for dollars by central banks
The US dollar's share in global foreign exchange reserves fell to its lowest level in 25 years in the fourth quarter of 2020, driven by exchange rates in the short term and central bank actions in the long term.
(currency composition of global foreign exchange reserves, percent)



1. If a group of countries made a secret agreement to sell their U.S. dollars in a short period of time

and purchase euros or the renminbi instead, how would the United States economy be affected?



5. What is the future of the dollar as the reserve currency? Does the United States have more advantages than disadvantages of being the dominant economic power in the world? The Dollar: The World's Reserve Currency

Debate Questions:

1. Resolved that President Trump adopt a weak dollar policy?
2. Resolved that the IMF adopt a basket of currencies as the reserve currency for the world?
3. Resolved that the IMF return to the gold standard using a floating exchange rate?
4. Will a cashless society benefit or harm the global economy?
5. Is the most effective way to control inflation through monetary policy the raising of interest rates by the central bank of a country?
6. The implementation of cryptocurrencies should be expanded to include consumer spending.
7. Resolved that the goal of full employment is preferred to rising inflation?

Additional Sources:

Richard Nixon Changed the U.S. Economic Policy (The New Republic)

How the Nixon Shock Remade the World Economy (Yale Insights)