Comment on David Laidler's "Are Wage and Exchange Rate Flexibility Substitutes?"

By Douglas D. Purvis*

I was very pleased to see in *David Laidler's* paper an explicit discussion, albeit brief but nevertheless explicit, of what might be called "second-order, super non-neutralities". That is, recognition that monetary phenomena can have real effects (that arise from other than money illusion or expectational disequilibrium) by influencing the transactions technology and portfolio, accumulation and time-allocation decisions.[1] However, I was surprised that this discussion, which arose in the paper's early sections dealing with long-run phenomena, did not receive more emphasis in the discussion in the second half dealing with the short run. Surely the short-run displays more pronounced non-neutralities, and it is on these grounds that I found the discussion of the relative merits of exchange rate versus nominal wage rate adjustment not entirely satisfactory.

Before turning to that point, it should be noted that the two alternatives of wage *or* exchange rate adjustment are not exhaustive, and in the absence of a theory of how the exchange rate regime influences the flexibility of wages, a much more complete taxonomy is required.

However, even if we accept the alternatives *David Laidler* has presented us with, I would contend that there is a sense in which his discussion is somewhat misleading. Granted, by virtue of the homogeneity postulate, a given shock requires the same *ultimate* real wage to be established independent of whether nominal wages or the exchange rate (i. e. the price level) adjust. But the *equilibrium short-run* behavior of the real wage will be very different.

This is simply because more than the real wage is influenced by the adjustment process, and the general equilibrium spillovers will be very different depending upon whether the nominal wage rate or the ex-

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[1] For elaboration, see *D. Purvis* (1976), Inflation, Employment, and the Phillips Curve: A Comment on the Phelps-Friedman Twist, Discussion Paper No. 228, Institute for Economic Research, Queen's University.

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change rate adjusts.[2] The homogeneity postulate has no real force in a short-run characterized by fixity of some nominal magnitudes. Speeds of adjustment aside, wage flexibility and exchange rate flexibility are not substitutes in the short run.

[2] For example, compare the second and fifth rows of Table 3 in my paper for this conference.

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