

U.S. economy, and examines the resultant questions of domestic economic policy.

Several *key points* emerge from this study: (1) *persisting uncertainty as to the nature and extent of the United States commitment*, (2) *a lack of general understanding of the speed with which a military buildup affects the economy*, (3) *confusion in interpretation and delay in the release of budget information in 1966*, and (4) *resultant basic problems in national economic policy*. The final section of this study deals with the process of economic adjustment to peace in Vietnam.

A. *Some historical perspective*

Until comparatively recently, expenditures for national security were a minor factor in American economic activity. In the half century prior to 1930, such outlays normally equaled less than one percent of the Gross National Product (GNP), except for the World War I period. From 1931 to 1939, military outlays averaged 1.3 percent of GNP. Since World War II, however, the Cold War and the Korean and Vietnam conflicts have raised security programs to a relatively high level even in the absence of hostilities. Immediately prior to the Vietnam buildup, purchases by the Department of Defense were about 8 percent of the total output of the Nation. The proportion was of course higher during World War II (peak of 48 percent) and the Korean War (peak of 12 percent).

The most recent levels of military demand reflect an extended period of Cold War, interspersed by incidents leading to limited conflicts, such as Korea and Vietnam, and temporary thaws and defense cutbacks, such as in 1957-58 and in 1963-64. An abrupt change in the nature of the external environment—a sudden intensification of war or a cold war thaw—and in this country's reaction to it, might well cause another major shift from the present proportion of resources devoted to security programs. Unlike many other categories of demand for goods and services, the level and composition of national security expenditures are relatively independent of influences in the private economy. Yet, these military demands heavily influenced the private economy.

The impact of defense on the economy depends not only on the level and rate of change of spending. The availability of resources and the state of peoples' expectations affect the timing and extent of the impact on prices, production, and economic growth. Heavy reliance on deficit financing during World War II, in contrast to the emphasis on tax financing during the Korean War, produced different results on consumer income and spending both during and after the war.

Even before the Vietnam buildup, military spending had been dominating the Federal Budget. Such spending accounts for over 85 percent of all Federal Government purchases of goods and services. In real terms (when the dollar figures are adjusted to eliminate changes resulting from inflation) virtually all of the increase in direct Federal purchases of goods and services during the past two decades has been accounted for by defense programs. The aggregate of all other purchases by the Federal Government is at about the same real level as in 1940. The large increases in Federal spending for civilian purposes have been transfer payments and grants, which do not show up in the GNP as Federal purchases of goods and services. Hence, the rise in the Federal share of GNP from 6.2 percent in 1940 to 10.3 percent in 1964 was accounted for almost entirely by military and related security expenditures. On this basis, it can be seen that these security-related expenditures have been the primary factor in the expansion of the Federal Government as a purchaser and consumer of goods and services.²

B. *The U.S. commitment in Vietnam*

An evaluation of the impact of the Vietnam war on the U.S. economy requires first a review of recent developments in South Vietnam itself and of the changing nature of the U.S. involvement. The nature and extent of the American commitment in South Vietnam was continually unfolding during the period 1963-66. This, of course, created fundamental difficulties both in forecasting U.S. military expenditures and in analyzing their impact on the American economy.

It is the essence of present-day limited war for one side to be uncertain of the future actions of the other. However, in the hitherto conventional conflicts such as the role of the United States after Pearl Harbor, there was little uncertainty as to the extent of our own participation in World War II—the maximum effort

² For a more detailed analysis, see M. L. Weidenbaum, "Defense Expenditures and the Domestic Economy," in Stephen Enke, editor, *Defense Management*, Englewood Cliffs, Prentice-Hall, Inc., 1967, pp. 317-336.