

United States has entered a major war with a very large existing defense establishment.

The second set of differences relates to the fact that, unlike Korea or World War II, the present military buildup was superimposed on an economy which was rapidly approaching full employment. Using June 1950 and July 1965 as the respective beginning points, a comparison shows that unemployment was higher in the earlier period (5.4 percent versus 4.5 percent) and the operating rate of industry was lower (80 percent versus 90 percent).

Summarizing these two conflicting tendencies, it may be concluded that even though the current defense program utilizes a smaller fraction of the nation's resources, it represents to a considerable extent a displacement of civilian demand rather than a total addition to actual production of goods and services. Hence, in the absence of direct controls over materials, wages, and prices, it is not surprising that inflationary pressures should have accompanied the rapid shift of resources from civilian to military use.

The Korean experience showed that the strongest inflationary pressures occurred during the first year of the buildup, while the economy was initially adjusting to the new level of military demand. The actual peak in defense spending a few years later occurred shortly before the onset of recession. *If there is any lesson to be gained from the Korean experience, it is that the Nation particularly needs to understand the timing of the impact of the different stages of a defense buildup (and subsequent cutback). Otherwise the United States can find itself fighting yesterday's inflation with a tax increase that will compound tomorrow's recessionary problems.*

III. THE U.S. MILITARY BUILDUP FOR VIETNAM

A. The expansion of U.S. military spending for Vietnam

The relatively minor American involvement in Vietnam during the 1954-63 period was hardly visible in the U.S. military budget. However, applying the average annual cost per U.S. soldier (\$23,000) to the number of American troops in South Vietnam during that time yields a rough order of magnitude of the demand on U.S. resources.

On that basis, the American commitment was costing about \$15 million a year during 1954-60 and rose to somewhere around \$18 million in the fiscal year 1961. In contrast, total U.S. defense spending was \$43,227 million in fiscal 1961. By the crude estimating technique used here, U.S. defense spending in South Vietnam was around \$31 million in fiscal 1962, \$227 million in fiscal 1963, and \$381 million in fiscal 1964, still quite minor amounts compared to the military budget totals.

An official estimate is available for "special support of Vietnam operations" in fiscal 1965, \$103 million.²³ That figure seems low in view of the fact that U.S. troops in South Vietnam rose from 23,300 to 103,000 during that year. Presumably, a high proportion of the costs was financed from regular operations or by drawing down inventories of weapons and supplies previously purchased.

The significant impact of Vietnam on the Federal Budget and hence on the American economy began in the fiscal year 1966. The January 1966 Budget Document estimated that \$14.0 billion of the requested appropriations and \$4.4 billion of the estimated expenditures for the fiscal year then in progress—the year ending June 30, 1966—resulted from Vietnam. The actual amounts turned out somewhat higher, \$14.9 billion in appropriations and \$5.8 billion in expenditures. A review of the data in Table 1 confirms the fact that the fiscal year 1966 was the period of major expansion of American armed forces in Vietnam. Prior to July 1, 1965, U.S. armed strength stationed there had risen to 103,000. Between July 1965 and June 1966, there was an increase of over 200,000 American troops in Vietnam. To date, further increases have been somewhat in excess of 100,000.

As pointed out earlier, the basic detail in the defense budget is not broken down to show the Vietnam components of each item separately. Hence, it is necessary to infer the impact of this commitment from movements in the more

²³ *Budget of the United States Government for the Fiscal Year Ending June 30, 1968, 1967, p. 77* (hereafter referred to as *1968 Budget*).