Government contractor delivers the finished items, the transaction shows up in the national income accounts as a decline in business inventories.

It also is then recorded as a Government purchase of goods and services. These two entries tend to cancel each other out, with no net effect on GNP. At the time it is recorded in the national income accounts, the Government purchase does not represent payments to the factors of production; it is more in the nature of an intersectoral transfer—a reimbursement to the Government contractor for his outlays during earlier periods.

It is at the order stage that the government action normally will have its initial and often major impact on the markets for labor, raw materials, and financial resources. The contribution to economic activity is made during the production period prior to the actual government "purchase." Indeed, the recording of the government purchase may coincide in time with a reduction in governmental impact on total demand.[3]

HISTORICAL EXPERIENCE

If we reflect upon a previous military buidlup effort of the United States—the Korean mobilization—we can see that the proper understanding of the timing of the economic impact of such government activity can have important consequences for Federal fiscal policy. The $3.5 billion budget surplus during the first year of that defense expansion—fiscal year 1951—was hardly adequate in a period of rapid military buildup, as indicated by the accompanying inflationary pressures of substantial proportions.

Using conventional measures, Federal expenditures remained fairly stable during 1951. In contrast, the amount of appropriations and other "new obligational authority" granted by the Congress for the year was 68 percent above the 1950 total. The aggregate amount of contracts let and other obligations entered into by the Federal agencies almost doubled in the first year of the Korean mobilization program. The interplay during that crucial period of the opposing tendencies of the opposite ends of the Federal spending process was clearly brought out in the following comment on this period by the Joint Committee on the Economic Report:

> The ineffectiveness of the governmental cash surplus, normally a deflationary force, was, in large part, attributable to anticipatory forces on the inflationary side arising from the current or expected placement of orders for future deliveries.[4]

The following year, fiscal 1952, was the period of the actual major increase in Federal defense expenditures; it was one of comparative stability in the American economy. Several interesting points emerge from an examination of the Korean mobilization program:

1. The major expansion in economic activity occurred at approximately the same time as the announcement and authorization of the program, and while many of the defense orders were being placed.

---

[3] "Statement of Murray L. Weidenbaum" in U.S. Congress, Joint Economic Committee, *Inventory Fluctuations and Economic Stabilization*, 1962, pp. 170-179. See also Edward Greenberg, *Employment Impacts of Defense Expenditures and Obligations*, Washington University, Department of Economics, Working Paper 6505, April 29, 1965; Michael Spiro, *Impact of Government Procurements on Employment in the Aerospace Industry*, Massachusetts Institute of Technology, Alfred P. Sloan School of Management, Working Paper 134-65, November 1965.[2]

[4] U.S. Congress, Joint Committee on the Economic Report, *National Defense and the Economic Outlook for the Fiscal Year 1953*, 1952, p. 49.