

beginning to stir, the war is already having noticeable effects upon the economy.

Act III. The U.S. buildup in the war zone has continued. The administration has asked Congress for large supplemental appropriations. Spending still lags behind costs, but it is rising fast—the recruits in training have to be paid, and so do the additional civilians hired. The war's economic effects, moreover, are expansionary out of all proportion to the actual increases in defense spending: the surge in defense orders has increased demand for skilled workers, materials, components, and credit in advance of deliveries and payments. To some extent, the Defense Department's matériel buildup is being temporarily financed by the funds that contractors and subcontractors borrow from banks against future payments from the U.S. Treasury.

Act IV. The U.S. military buildup in the war zone tops out. Defense production continues to rise, but the *rate* of rise is much less rapid than in Act III, and the expansionary economic force exerted by the war begins to wane. Deliveries of arms, ammunition, and equipment rolling into military depots more than match the chewup of matériel in the war, and so some replenishment of inventories takes place. Men are moving out of training and into operating units faster than forces are being sent overseas, and so there is a net buildup of trained, deployable military forces in the United States. Expenditures catch up with costs.

Act V. The war ends. The dropoff in contract awards and the collapse of inflationary expectations reverberate throughout the economy. Far from falling steeply, expenditures continue to rise a bit before entering into a gradual decline: the incoming deliveries must be paid for, and the men brought into the Armed Forces must be provided for until they are mustered out. With deliveries no longer partly offset by wartime chewup, inventories fill rapidly, and begin to overflow. During the period of readjustment, military manpower and military inventories exceed normal peacetime requirements. Expenditures for this excess readiness largely make up for the expenditures deferred through reduced readiness in the early phases of the war.

In January, 1965, the Vietnam war was still in act I, and to all appearances nobody in the administration expected an act II. The President's budget message declared that, with the "gains already sheduled," U.S. military forces would "be adequate to their tasks for years to come." The new budget projected a *decrease* in defense spending in fiscal 1966, and a *decline* in total uniformed personnel. Maj. Gen. D. L. Crow, then Controller of the Air Force, subsequently testified at a congressional hearing that "the guidelines for the preparation of the budget as they pertain to Vietnam were actually a carry-forward of the guidelines that were used in the preparation of the 1965 budget, and they did not anticipate increased activity, per se, in Vietnam."

IT'S NOW ACT III

Not until last May was it entirely evident that act II had begun, but there were intimations earlier. In January 1965, after declining for four consecutive quarters, the Federal Reserve Board index of "defense equipment" production turned upward, beginning the precipitous climb depicted at the bottom of the page opposite. In February the United States began bombing targets in North Vietnam.