

show up as purchases of goods and services by the Government. In the GNP accounts, the rise in defense production shows up first as an increase in inventory of goods in process. This process is explained in some detail, with comments on its important economic implications, in articles by Prof. Murray Weidenbaum, of Washington University (St. Louis). The chart shows defense spending on the two bases—budget and GNP—drawing together during 1967 as the rate of deliveries catches up with the placement of procurement orders and current production rates.

THE OUTLOOK FOR PEACE

The analysis presented here assumes continuance of hostilities in Vietnam through the entire calendar year 1967, in much the same general framework as at present, but with U.S. forces applying increasing efforts and spending increasing sums of money. The U.S. objective sounds modest enough. As stated by Secretary McNamara, it is "a stable and independent government free of Communist control." But perhaps the limited nature of the objective makes it all the more difficult to attain.

Because of repeated pressures on both sides in the conflict from most other nations in the world, I would expect some progress to be made during the next 16 months toward bringing the war to an end. But, in view of the pathology of the conflict over many years, it seems unduly optimistic to expect peace negotiations to reach a stage that would permit significant relaxation of the U.S. commitment in Vietnam within the horizon comprehended here.

In the other direction—that is, expansion of the area of conflict—developments of the past few weeks offer strong reason to expect that Communist China and the Soviet Union will not change the essential nature of their support of North Vietnam. There has been, in response to U.S. bombing of targets in North Vietnam, an escalation of rhetoric and the boycotting of a track meet which the Russians evidently were going to lose anyway. But there is no evident disposition to convert the conflict in Vietnam into World War III.

CONCLUSION

Thus we are left in this fairly narrow band of uncertainty regarding the prospective course of the war in Vietnam and of defense spending in 1967. It is an outlook that promises continuing strains on the U.S. economy, but only because other pressures on productive resources are present. As the final chart shows, the proportion of GNP going to defense goods and services will remain modest by any recent standard. The prospective magnitude of defense spending should therefore be within the capacity of the economy.

To conclude this analysis in the most practical economic terms, the increase in defense spending now in prospect for next year should not in itself require a tax increase.