

and its first stage took effect in June 1965, cutting taxes by \$1¼ billion (annual rate). A liberalization of social insurance benefits, designed to help the aged, was enacted to take effect retroactively. The larger benefits were to be financed by a payroll tax increase at the beginning of 1966. Meanwhile the liberalization of benefits was expected to give the economy a significant stimulus in the fall of 1965 when an anticipated liquidation of steel inventories might otherwise have threatened a slowdown. The retroactive portion, which was disbursed in September, amounted to \$900 million. Thereafter annual benefits were raised by about \$2 billion.

SPURT IN ECONOMIC ACTIVITY

The economic environment was significantly changed by the expansion of defense requirements. On July 28, 1965, the President requested additional funds for defense and indicated that further increases would be required in January. Military outlays, at an annual rate, rose by nearly \$2 billion a quarter in late 1965 and early 1966 (table 3). Defense orders expanded very rapidly, spurring demands for labor and inventories by contractors.

Yet the defense buildup itself was not enough to account directly for the acceleration in the overall economic advance. Rather, it reinforced the previously planned fiscal stimuli and the forward momentum of a strong economy close to full employment. Furthermore, the expansion of defense spending contributed to a significant change in the climate of opinion. The Vietnam buildup virtually assured American businessmen that no economic reverse would occur in the near future. The impact on business attitudes was intensified by unwarranted fears that the Vietnam conflict might have consequences like those of the Korean conflict: direct controls, excess profits taxes, and a huge jump in prices of raw materials.

TABLE 3.—Changes in gross national product during 2 periods since mid-1965

[Billions of dollars, seasonally adjusted annual rates]

Expenditure category	Change	
	1965 II to 1966 I	1966 I to 1966 IV ¹
Gross national product.....	48.3	37.9
Personal consumption expenditures.....	28.8	18.8
Durable goods.....	5.9	— .2
Nondurable goods.....	12.5	6.8
Services.....	10.4	12.2
Gross private domestic investment.....	10.8	3.5
Fixed investment.....	9.6	— 2.0
Business fixed investment ²	9.1	4.7
Residential structures.....	.5	— 6.7
Change in business inventories.....	1.3	5.5
Net exports of goods and services.....	— 2.2	— 1.2
Government purchases of goods and services.....	10.7	16.9
Federal.....	6.3	10.6
National defense.....	5.5	10.9
Other.....	.9	— .4
State and local.....	4.4	6.3

¹ Preliminary.

² Nonresidential structures and producers' durable equipment.

NOTE.—Detail will not necessarily add to total because of rounding.

Sources: Department of Commerce and Council of Economic Advisers.