

A war economy without industry?

Informed sources are concerned that projected U.S. defense spending now exceeds the projected capacity of industry to produce defense goods...

Defense industry sources interviewed by *EIR* last week raised serious questions as to whether the U.S. economy is in any shape to embark on a course of increased military spending at the present time.

The big question mark in their minds is the availability of unused capacity in the capital goods and raw material extraction sectors of the economy. According to one source at the Department of Defense in Washington, the situation in the economy is very different from the early period of the Vietnam war, when a margin of unused industrial capacity could be shifted to defense production without straining the limits of capacity. "From 1964 to 1972 was a period of steadily increasing defense expenditures, yet increased defense production did not outstrip existing capacity," he noted. "We got through the period with literally no allocations of resources necessary." A source at a major Long Island-based defense contractor pointed out that the small machine shops on Long Island, to which Grumman subcontracts its defense work, already have more orders than they can meet; the same situation holds at other industry subcontractors such as electronics houses and minicomputer firms. "If the government makes the decision to increase defense spending," he concluded, "then

the government will have to make the other decisions, too—allocate engineering talent, skilled labor, tooling capacity, and raw materials."

Until the release of the fiscal 1981 budget by President Carter Jan. 28, the Department of Defense will not comment on actual plans for escalating government spending on defense or on the existence of allocation programs which might be in the works. "If I told you that we were working out programs to allocate materials and labor, you'd know that we did in fact have plans to increase defense spending in the next budget," a spokesman for the DOD commented. Expectations in the defense industry are that the bulk of any increase will come in the shipbuilding area.

Economists are now projecting that the Carter Administration will seek to raise real defense outlays around 5 percent or higher a year over the next five years. This is just slightly higher than the 4.5 percent annual increase in the five year program announced prior to the launching of the "Carter Doctrine" this month. The current cold war posturing of the Carter Administration could easily translate into real increases of 10 percent per year, between now and 1985, industry insiders say.

The implications for the economy of even the conservative estimate are disturbing. A 5.5 percent

real annual increase combined with a 9 percent annual rate of inflation would lift defense outlays from an estimated \$123.6 billion in fiscal 1980 to a staggering \$243 billion in fiscal 1985. The consequences would be a mushrooming of the federal deficit, spiraling interest rates, and hyperinflation.

The deficit in the fiscal 1981 budget, to be unveiled by President Carter later this month, is now certain to surpass the \$15 billion figure projected by government sources late last year. We are projecting a deficit in the range of \$70 billion based on the following considerations: Carter's embargoing grain to the Soviet Union could add over \$15 billion to government expenditures over the next calendar year, in the form of price supports, grain set asides, and the whole gamut of financial support mechanisms that could be called into play for the farm sector (see accompanying article). In addition, we expect that for political reasons, Carter will both increase defense expenditures and forego any off-setting cuts in domestic programs.

One immediate effect of the growth of the federal deficit will be the squeeze on private sector credit demand. Even before the cry for more defense spending went up, total government borrowing (federal, state and local) was expected to increase to around \$118 billion in 1980 from \$101 billion in 1979.

Given the recent talk about increased defense spending, we expect Federal borrowing needs to escalate, and we expect to hear revived discussion of the Credit Control Act of 1969 or some other mechanism for rationing credit in the economy.