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MILITARY BUILD-UP AND THE U.S. ECONOMY

One and a half trillion dollars! That's what the Reagan Administration proposes to spend on the military over the next five years. In absolute terms, even taking inflation into account, it's the largest military build-up in history. Who will pay, and how?

The last major U.S. military build-up occurred during the Vietnam War. Democratic President Johnson assured Americans that the U.S. economy could produce both "guns and butter." It did so, but look what it cost: federal deficits swelled, inflation increased, and U.S. competitiveness in world markets declined as resources were diverted from productive investment to the military. Will this happen again the the current build-up? The Reagan Administration says no. Much industrial capacity lies unused today, and millions of American workers have been idled. Surely, Administration spokesmen claim, the military build-up could tap unused resources without substantially crimping recovery or future growth.

Bottlenecks: Or can it? The largest increases in military outlays are for new weapons, rather than for personnel for for operations and maintenance. Manufacturing these new weapons requires highly skilled workers and high-technology components. Eventually, new workers and engineers can be trained and industry retooled. Until then, however, the high-tech sectors will experience severe bottlenecks. Wait-times in 1981 for delivery of aluminum forgings, aircraft landing gear, and integrated circuits ranged from 60 to 120 weeks, up from 20 to 50 weeks in the late 1970s, according to a panel of the Pentagon's Defense Science Board. According to the National Tooling and Machine Association, the shortage of skilled workers was 60,000 in 1981, and could reach 250,000 by 1985. Already "head hunters" are being paid \$1,000 or more for recruiting engineers, computer experts, and other skilled personnel.

Bottlenecks are compounded by regional imbalances in military spending. Military contracts go disproportionately to the South and West, while idle capacity and unemployment is more concentrated in the older industrial areas of the North and Midwest. Thus the military build-up helps account for one of the peculiar features of the current economic crisis: the extreme variation by industry and region in performance.

Escalating Costs: The competition for skilled labor and critical parts tends to push prices higher for military goods. In both 1980 and 1981, prices increased 5% faster in the military sector than in the economy as a whole. A number of forecasts, including the Defense Department's own relatively optimistic one, conclude that military costs will continue to increase faster than civilian costs. Yet official budget calculations ignore this trend. According to a staff study for the Joint Economic Committee of Congress, the Administration may have underestimated the cost of the planned build-up by \$80 billion on this count alone.

Bottlenecks in the military sector will increase costs in the civilian sector as well, as civilian firms are forced to compete with military contractors for scarce inputs. And, of course, increasing military expenditures will do nothing to halt mismanagement within the Pentagon, waste that Budget Director David Stockman estimates to cost between \$10 and \$30 billion a year.

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Unemployment Not Resolved: As unemployment climbs over 10%, many workers look to military spending to create jobs. To a certain extent it will. But it will create fewer jobs than the same amount of money spent for civilian programs. Take the B-1 bomber, for instance. A leading economic forecasting firm, Chase Econometrics, was hired by Rockwell International Corporation to compare the effects of the B-1 expenditures with a tax cut and a public housing program of equal dollar costs. The results: over five years, the tax cut yielded 30,000 more jobs than the B-1, the housing program, 70,000 more jobs.

Why the difference? The main reason is that military spending in general and especially the weapons procurement central to this build-up, demands relatively high amounts of capital and skilled labor, and relatively little other labor. So, for example, in guided missiles and electronic communication only three out of every ten jobs go to production workers, compared with nine out of ten for U.S. industry as a whole.

Declining U.S. Competitiveness: Military spending is neither the sole nor the main cause of the U.S.'s relative economic decline. Nevertheless, given the Administration's stress on the need to invest in new, more efficient plants and equipment, it seems important to point out the obvious: the greater the military expenditures the less surplus available for productive investment.

In the short run, military build-up pulls resources from civilian development in the very high-tech industries that the U.S. needs to encourage. Advocates of build-up such as Secretary of Defense Weinberger retort that in the long run, increased military-funded investment and research and development in high-tech industries will result in civilian spinoffs and increased capacity. But would not those same funds be more productively invested directly in civilian industry and civilian research and development? Increasingly European and Japanese firms, not U.S. firms, are first to translate U.S. military technology into competitive civilian products. For example, while solid-state integrated circuits were developed with U.S. military research money, it was the Japanese who successfully used them to reduce the costs of TV sets and radios. In general, the problem is not so much any decline in American "ingenuity" as the difficulty of converting from production of small-run, state-of-the-art weapons to production of high-run, low-cost consumer goods.

Decreased Social Spending: The military budget puts tremendous pressure on social spending. By 1986, the military share of the federal budget is expected to rise to 37.6%, compared with 24.7% in 1981. Big as these shares are, they underestimate the military burden. If we include veterans' benefits in military expenditures, and separate debt payments and trust fund payments like Social Security from more freely disposable funds, we find that military spending is slated to climb from 54.2% of discretionary general funds in 1981 to 78.8% in 1986. (Note that part of debt payments should be included in military expenditures too, since debts were incurred to finance the military.)

At current tax levels, revenues will not grow nearly fast enough to maintain social services alongside military spending. Last year the Congressional Budget Office estimated that by 1986, military expenditures will consume 98% of revenues left over for discretionary general funds. Since then new taxes have been imposed, but they cannot make up the gap, especially given the continued stagnation of the economy. Not only Social Security and welfare benefits, but also essential public investments in energy conservation, manpower training, mass transit, and housing are bound to suffer.

Let us put it another way. What is the Administration's answer to Johnson's discredited "more guns and butter" program? Less butter.

- Kent Osband

For more information on the economic impact of the build-up, see The Costs and Consequences of Reagan's Military Buildup, by the Council on Economic Priorities, available on request from the Labor Center, U.C. Berkeley, at \$3.00 per copy.