

Regling, Horst

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Economic Effects of the Vietnam De-escalation

by Dr Horst Regling, Hamburg

A military policy measure as incisive as the withdrawal of over 500,000 US troops from Vietnam and the cutback in expenditure entailed—equivalent to 35 p.c. of the defence budget, 15 p.c. of the total Federal budget and about 3 p.c. of the GNP—over a few years is obviously bound to lead to repercussions in the American economy. The quantitative assessment of these repercussions is subject to a far greater degree of uncertainty than is common in forecasts of economic trends.

If the theses of the critics who impute to industry a massive material interest in military procurement programmes are to be believed, the "wide profit margins" of at least those industries are bound to narrow which have profited from Vietnam contracts in the past, and there would be a consequent contraction in the profit total of US industry. Conversely, it has been pointed out repeatedly that "the Vietnam war hasn't been good for business profits".

Louis Lundborg, the chairman of the Bank of America, recently remarked that "during the four years prior to the escalation of the conflict in Vietnam corporate profits after taxes rose by 71 p.c. From 1966 through 1968 corporate profits after taxes rose only by 9.2 p.c.". In testimony before the Senate Foreign Relations Committee Mr Lundborg said that the Vietnam war and the associated rise in defence spending "distorts the American economy" and is a "major contributor in inflation"¹. As evidence in support of this thesis it can be pointed out that Wall Street regularly responded to announcements of a withdrawal from Vietnam by raising stock prices.

Sector Effects

To gain an idea of the economic consequences of withdrawal from Vietnam it appears useful to apportion past Vietnam procurement buying to individual sectors and regions.

From a Department of Labour analysis for the fiscal period that ended in mid-1968² it emerges

clearly that the main impact will fall on aircraft, transport equipment and ordnance. These industries will feel most of the blow because they together provided 4 of every 10 jobs created by the war.

The proportion of Vietnam-related employment shows this dependence to be especially significant in the aircraft and ordnance sectors. As much as one-quarter of total employment in the aircraft industry depends on Vietnam-related contracts, and the degree of Vietnam dependence in the ordnance sector is as much as 42 p.c. Most of its 140,000 Vietnam-generated jobs are in ammunition plants, and sharp cutbacks here are inevitable once peace is restored and stockpiles have been replenished. On the other hand, little difficulty should be met in finding alternative jobs for the 165,000 transport equipment workers made redundant because they account for no more than 6 p.c. of an industry with widely dispersed outlets.

Table 1
Significance of Vietnam Expenditure for Individual Industries

Industry	Vietnam-related jobs (in thousands)	Per cent of industry's employment	Per cent of all war created employment
Aircraft	233	27	17
Transport equipment	165	6	12
Ordnance	140	42	10
Wholesale-retail trade	76	0.5	5
Communications equipment	74	11	5
Business services	50	2	4
Electronics	41	11	3
Textiles	41	10	3
Medical, education, nonprofits	36	0.7	3
Primary iron-steel manufacture	33	4	2
Machine shop products	33	14	2
Construction	29	1	2
Electrical equipment	24	6	2
Primary nonferrous metal manufacturing	24	7	2
Finance-insurance	24	0.9	2
Rubber goods	20	4	1
Shipbuilding	20	7	1
Chemicals	19	4	1
Printing-publishing	16	2	1
Metalworking machinery	15	4	1
Scientific instruments	15	5	1
Food	15	0.8	1
All other	279	—	19

Source: How peace will cut employment, in: Business Week, February 14, 1970, p. 130.

¹ Vietnam War's Cost will fall to \$ 9.1 bn in fiscal '71, former budget director says, in: The Wall Street Journal, No. 74, April 16, 1970.

² Defence-generated employment rose by 903,200 from the start of the Vietnam buildup in June, 1965 to June, 1967 — a 44 p.c. increase. But from June, 1967 to June, 1968 total employment turned down slightly. War work payrolls start heading down, in: Business Week, June 14, 1969, p. 134.

In other industries Vietnam-related contracts are also neither absolutely nor relatively so large that an order cutback could create insuperable difficulties, which of course does not rule out delicate adjustment problems arising in conversion from military contracts, for instance in the machine shops.

Regional Effects

Since mid-1965, when the Vietnam buildup began, the Pentagon has kept records on "defence dependency" for each separate Federal state. This ratio shows the relative bearing of defence spending on the states in terms of direct employment impact. For the USA as a whole Vietnam has raised the defence dependency ratio from 2.7 to 3.6 p.c. Regionally the ratio varied in June 1968 from 2.2 p.c. in the Midwest and 3.3 p.c. in the East to 4.9 p.c. in the South and 5.1 p.c. in the Far West.

At a first glance there emerges the interesting result that Vietnam contracts were by no means divided between the regions in proportion to their prewar dependency ratios. Compared with the pre-Vietnam situation, dependence on military contracts rose in the Midwest by 57 p.c., in the South by 44 p.c., in the East by 38 p.c., and in the Far West by 21 p.c.³ The South apart, Vietnam thus tended to favour regions with a formerly rather low dependence on defence contracts. This trend is predominantly due to the marked structural divergence of the Vietnam programmes from the pattern which emerged at the time of the cold war. Whereas prewar orders had gone mostly to the science-orientated, aerospace and electronics industries established in the South and West for this specific purpose, Vietnam made, in addition, special claims on the industries located in the Midwest and South which produce such war-consumable items as textiles and munitions and basic equipment like vehicles and tires⁴.

Correspondingly, a reduction of the Vietnam engagement will impinge chiefly on the regions which derived special benefit from these contracts. In order to plan for "the impact of peace", the Pentagon has identified 100 small communities likely to meet serious problems. They are mostly localities near reactivated ammunition plants, reactivated or expanded military bases and textile manufacturing plants. From Table 2 it will be seen that these areas, mostly in the

³ In both percentage and dollar terms Texas is the state that has benefited most from the extra spending induced by the Vietnam war — thanks partly to the presence of a Texan in the White House at the time. *The Economics of Vietnam*, in: *The Economist*, February 21, 1970, p. 56.

⁴ War work payrolls start heading down, *ibid.*, p. 134.

⁵ Will US shrink its global role? In: *Business Week*, June 7, 1969, p. 147.

Table 2
Defence-generated Employment as a Percentage of Total Civilian Labour Force

	June 1965	June 1966	June 1967	June 1968
Utah	7.6	9.9	9.9	8.9
California	4.9	5.5	6.5	6.2
Maryland	5.6	6.4	6.9	6.2
New Hampshire	4.5	5.0	6.3	6.2
Rhode Island	3.7	3.7	5.3	4.4
Georgia	3.6	4.1	4.8	4.3
Missouri	2.7	3.8	4.5	4.0
Washington	3.9	4.0	4.3	4.0
New Jersey	2.4	2.9	3.3	3.1
South Carolina	1.9	2.3	3.0	2.8
Kansas	2.3	3.2	3.3	2.6
Vermont	1.2	1.5	2.1	2.2
Minnesota	1.1	1.4	2.2	2.1
Montana	.6	1.7	2.7	1.9
Illinois	1.1	1.3	1.8	1.7
Kentucky	1.2	1.5	1.9	1.7
Nebraska	.8	1.0	1.4	1.5
Louisiana	.8	1.1	1.6	1.3
Delaware	.9	1.2	1.3	1.2
Michigan	1.0	1.1	1.4	1.1
Iowa	.7	.8	1.2	1.1
Wyoming	.5	.6	.9	.5

Source: War work payrolls start heading down, *ibid.* p. 135.

South and Midwest, are by no means identical with the regions with the highest defence dependency ratios.

Overall Offsets against Cutbacks

Although curtailment of Vietnam spending entails aggravating cuts in some sectors and regions, it must not be left out of account as regards the national economy as a whole that at most 3 p.c. of the GNP is involved. Besides, not only will this rundown be spread over several years consecutively but there are various indications that the sums set free have already been allocated to other projects.

In the event of its own troops being withdrawn the United States will, for instance, have to back the South Vietnamese troops to be employed on an increased scale, at least for a transitory period, by supplying arms and ammunition; and even when military operations have ceased altogether, the USA will have to support a reconstruction programme in South Vietnam.

Moreover, the greatly increased Vietnam engagement has caused a number of military projects to be postponed which in view of the world-wide commitments of the USA brook no further delay. As Presidential adviser, Arthur Burns pointed out a year ago already that "we've been fighting the war to a significant degree by reducing our inventory of military equipment and by not pushing research and development as vigorously as it should have been"⁵.

Even if, however, additional defence budget economies should be possible on account of the substantial troops cuts ahead—the Pentagon figures that it costs an average of \$ 10,000 a year to keep a man in uniform—a recession threat can be discounted because of the considerable arrears of infrastructure and social welfare spending to be made good, provided this expenditure is politically practicable.

Greater Economic Efficacy of Military Spending

As appears from Mr Burns' remarks, a reduction of the Vietnam engagement will lead to substantial structural changes in the defence budget. When the predominantly conventional Vietnam expenditure ceases, a higher proportion of military spending will be for the purpose of nuclear deterrence which is commonly held to be decisive in the cold war. There will consequently be a much greater impact than hitherto on the sections of the armament industry which employ the most sophisticated technologies in the widest sense of the term.

A recently published Department of Labour survey showed that "at the peak of Vietnam hiring 20 p.c. of the nation's engineers and nearly 10 p.c. of its skilled and semi-skilled workers were employed in defence-related jobs. Defence projects took 59 p.c. of all aeronautical engineers, 22 p.c. of the electrical engineers, 20 p.c. of the mechanical engineers and 16 p.c. of the industrial engineers. Nearly 40 p.c. of the nation's physicists, excluding professors, held defence jobs, and so did 10 p.c. of all chemical engineers⁶." There is much evidence to suggest that restructuring of military expenditure will increase the proportion of highly-skilled personnel employed on military objects.

Considering how important is the influence of military spending on the promotion of technical progress, especially in the American economy, it is to be expected that the pending restructuring of the defence budget will impart additional impulses to growth. Without dealing in detail with the connection between military and civil technical progress⁷, it may be stated that the Amer-

ican economy owes a large part of its know-how to military impulses. To what extent the international competitiveness of the American economy has been enhanced by these particular influences—over wide areas of atomic, aviation and electrical engineering it enjoys an absolute superiority—is illustrated by the fact that German industry is given extensive State subsidies in promotion of civil atomic energy and data processing projects in order to help offset the competitive advantage which has undeniably accrued to American industry on its civilian side as a by-product of military research and development tasks.

Improvement of the Balance of Payments

As the Vietnam war in the past contributed greatly to the worsening of the US balance of payments situation, positive effects may conversely be expected to result from reduced spending in this respect.

The direct foreign exchange cost alone has been estimated at \$ 1.5 bn a year. Besides, a fillip was given to imports of materials and intermediates into the USA. At the same time the war weakened the competitiveness of American goods at home and in overseas markets because the Vietnam spending made for inflation inside the USA. In studies made, the second of these three factors has been quantified at between \$ 600 and 1,100 mn and the third one at about \$ 1,350 mn a year. The three factors together add up to between \$ 3.5 and 4 bn a year, a figure roughly equal to the entire deterioration in the US balance between 1965 and 1968⁸.

Although full relief of the US balance of payments cannot be expected owing to the foreshadowed support for South Vietnam, it may be anticipated that the future trend will be favourably influenced. There will however be concomitant, in part substantial, losses of international liquidity on the part of the Far East Asian countries which have hitherto shared in the American dollar disbursements.

⁷ Cf. H. Regling, *Militärausgaben und wirtschaftliche Entwicklung*, Hamburg, 1970.

⁸ The economics of Vietnam, *Ibid.*, p. 57.

⁶ How peace will cut employment, *Ibid.*, p. 130.



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