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THE SECRETARY OF DEFENSE
WASHINGTON, D. C. 20301

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Chief, Records & Declass Div, WHS
Date: JAN 26 2012

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The Honorable George Shultz
Director, Office of Management
and Budget
Washington, D. C.

Office of the Secretary of Defense
Chief, RDD, ESD, WHS
Date: 26 JAN 2012 Authority: EO 13526
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Dear George:

Thank you for your letter of October 20, 1970 concerning the Defense Department's response to the President's request of May 25, 1970 for areas and programs where additional savings can be made.

I was both shocked and disappointed at the apparent unawareness of the massive cuts which have been made by the Department of Defense since the Nixon Administration took office.

You indicated in your letter that the Department of Defense was late in submitting its response, that its suggestions were of limited usefulness, and that no specific suggestions were made for additional savings.

There is a very simple reason for the fact that no net additional savings were proposed. I have been seeking to communicate that reason to the Congress, to your office, and to other interested offices in the Executive Branch and to the American people. We have already cut Defense to the bone, a point which, as you well know, is of increasing concern to the President.

Any adjustments in Defense outlays that I could foresee from the standpoint of security, the health of the economy and, most importantly, in helping to obtain the President's multiple objectives, would be on the side of net increases rather than further decreases in our "rock-bottom, bare-bones" budget. That is why, with White House approval, I am making a strong reclamation on the additional cuts made by the House on the Fiscal 1971 budget presented by the President. We are going to do everything we can to restore most of these cuts and I would hope we can count on your full support in that vital endeavor.

As to the Fiscal 1972 budget, we are working day and night trying to squeeze our minimal requirements from current estimated

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outlays of \$77.4 billion into the \$74.5 billion fiscal guidance we were given in NSDM 84.

From the standpoint of the concern you expressed in your letter, you seem to be saying that the only useful contribution that Defense could make to the budget problem you face would be to show a net decrease in outlays for Fiscal Year 1972. All the scrubbing in the world of so-called ineffective or low priority programs will not result in a net decrease without jeopardizing national security. In a separate letter, however, I will send you a list of possible decreases combined with a list of possible increases for whatever use this may be to you.

We make no claim, of course, that we are or that we can operate at 100 percent efficiency. As you know, however, the Blue Ribbon Action Committee has been hard at work, under Dave Packard's leadership, seeking to translate the year-long, comprehensive, in-depth study of the Defense Department -- a more comprehensive review of any Department than has been made in this Government in more than a decade -- into increased efficiency. The study itself took a concentrated year of effort, and anything more than a superficial attempt to gain increased efficiency requires similar concentrated attention and time. We are moving ahead as rapidly as possible on the 113 recommendations made by the Fitzhugh panel.

To turn to the central issue that is of concern to you, George, namely a healthy economy, I would like to recall my many discussions this year and last year, including those with the National Security Council and with your predecessor, Bob Mayo, related to the impact on the economy of Defense cuts.

Starting in April 1969, I repeatedly made the point in meeting after meeting that, in my view, a major issue that would occupy the attention of the American people in the Congressional elections would not be (1) the war in Vietnam, (2) the military-industrial complex, or (3) the size of the Defense budget, but that it would clearly be the unemployment levels in the state of the economy. Those forecasts have been borne out but are now past history.

What we now need to do is to look to the next two years and seek to avoid if we can generating additional adverse impacts on the economy.

Needless to say, my primary responsibility has been and will continue to be national security. There can be no compromise on that. But if we are going to insure the President's multiple

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objective, and if we are to have a strong national security posture, I must share the concern of others in the Executive Branch for the state of the American economy.

As the President and I, among others, have stated publicly on numerous occasions, the transition from a war-time economy to a peace-time economy is a difficult problem and inevitably will cause dislocations and turbulence. That transition can be virtually complete by the time the President ends his first term in office. It will be if we follow proper budget and fiscal policies.

The President faces a major deficit in Fiscal 1972, largely as a result of fiscal policy and inflationary pressures he inherited. Now that we have begun to put order back into the Federal fiscal house, we must as a matter of priority discriminate in our selection of programs for cutting or decreasing our Federal outlays so as to strengthen the economy in the next 24 months.

As we face the second half of President Nixon's first term, we have urgent national security needs that argue again selectively for increased outlays. The Federal Government also has an obligation to take those actions necessary to move the economy to full employment at reasonably stable prices.

In the past 15 months, since June 1969, the Department of Defense has been responsible for releasing approximately one million people from Defense-related roles. In that same period, unemployment increased by roughly the same amount. Though there may not be a direct relationship between the large cuts in Defense manpower and large increases in unemployment, there can be no question that there is a co-relation. In the next 12 months, under the budget we submitted to the Congress for Fiscal Year 1971 -- a budget that is not yet fully funded -- we anticipate a similar release of approximately one million Defense-related people, or a total of some two million in about two years. It seems clear to me that any actions we take with regard to Defense spending should be taken with these facts in mind.

Apart from our manpower-related costs, it is clear that Defense spending in the durable goods area will generate more lasting benefits to the health of the economy, to the general employment picture, and thus to the strength of our country than increased spending in many other areas, such as Federal transfer payments. Increased Defense spending in procurement accounts -- particularly of needed items whose purchase was deferred in past years because of the war in Vietnam and which are needed to implement successfully the Nixon Doctrine, both with respect to US forces and forces in allied and friendly nations -- will result in a quicker return of

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tax revenues than similar increased amounts spent for transfer payments. This will impact directly on manufacturing employment which, as you know, is one of the hardest hit areas in the unemployment picture we face in this autumn of 1970.

I have asked Bob Moot and Gardiner Tucker to meet further with your people in continuing attempts to communicate these basic truths and to review in very specific terms what has happened, as predicted, and what we can do for the future to achieve all of the President's top priority objectives in national security matters and in domestic requirements.

Sincerely,



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