

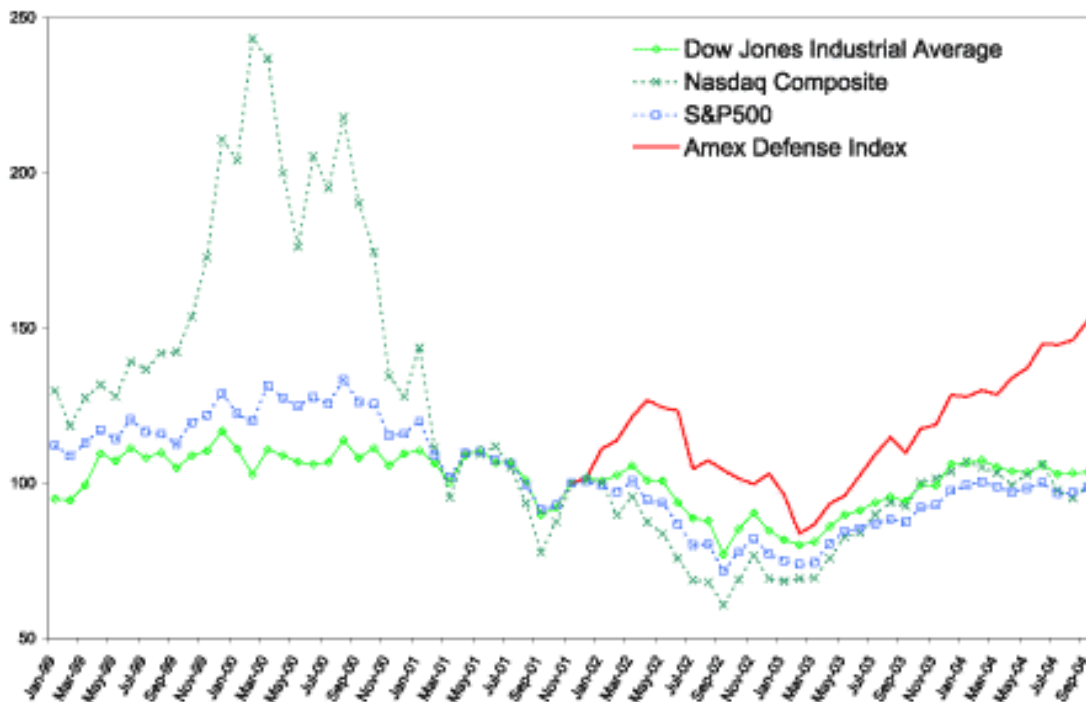
Boom Times for War Inc.

by James K. Galbraith

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On Sept. 21, 2001, the American Stock Exchange created the Amex Defense Index, a measure of the stock prices of 15 corporations that together account for about 80 percent of procurement and research contracting by the Department of Defense. The index, of course, includes the five largest military contractors: Boeing, General Dynamics, Lockheed Martin, Northrop Grumman and Raytheon.

The chart below, presented at a conference in Paris by economists Luc Mampaey and Claude Serfati, shows what has happened since then. With the Afghan war the arms index surged, gaining over 25 percent by April 2002. Then it slumped, along with the rest of the market. If you had invested \$1,000 in a defense portfolio at the peak of the Taliban boomlet, by March 2003 you would have lost a third of your stake.



But then came Iraq. And it's been clover for contractors ever since. Total gains since March 2003 are above 80 percent. Even if you'd put your money in at the beginning, in September 2001, you'd be up over 50 percent. That isn't bad, considering.

This is no scandal, of course. War is naturally good for the arms business. The companies involved are public -- anyone can buy their stocks. Suppose that back in 2001 you'd had unlimited access to bank credit. And suppose you'd also had the certain knowledge that George W. Bush would take out Saddam Hussein, come what may. Well then you, too, could have made billions over the past three years.

The really big scandal lies elsewhere. It isn't in the fact that a small group of political insiders made big money from the Iraq war. The big scandal is in all those other numbers: the Dow Jones industrial average. The Standard and Poor's 500. The NASDAQ composite index. Look at them -- they haven't budged in three years.

Some people get concerned when the stock market goes up. They fret over bubbles, which must pop, and over the

inequality of wealth that naturally rises with a rising market, given that only a few Americans own most of the corporate stock. These are real problems. But count me in the group that tends to see the bright side. A rising stock market means that businesses see the possibility of future profit, which spurs them to invest. And that, above all, is what creates the new jobs so lacking in the past four years.

If you want a one-picture analysis of the American economic problem, this chart is as good as any you will find. Much has been made of the fact that the Bush administration's tax cuts went overwhelmingly to the top 1 percent of the income distribution. But if those tax cuts had succeeded in setting off a strong and widespread economic expansion -- as Ronald Reagan's did, 20 years ago -- who would object? Not me, frankly. The problem is that they failed to do this.

Part of the reason lies in the poor design of the tax cuts. And part of the reason, surely, lies in the fact that the Iraq war is a huge question mark overshadowing the future of the American economy, and hence a deterrent to business investment.

Business isn't stupid. It knows that Iraq took us away from the "war on terror." It knows we're less safe now than if we'd pursued al-Qaida to the bitter end. It knows that energy markets are unsettled and that we may be heading toward a long period of expensive oil. It knows, perhaps above all, that the war in Iraq is far from over. None of this has inspired confidence.

Back in 1919, in the wake of the Great War, John Maynard Keynes wrote of the effects of war on business: "The war has disclosed the possibility of consumption to all and the vanity of abstinence to many." Something like this happened after September 2001. Households borrowed and kept up their spending even as incomes shrank. But businesses, forward-looking and unsettled by the prospects ahead, curtailed investment. As Keynes also wrote, "no longer confident of the future, [capitalists] seek to enjoy more fully their liberties of consumption so long as they last." But they don't invest, and they don't create jobs.

The big scandal isn't who made money. It's who didn't. It isn't the handful who got good jobs working for defense firms. (It isn't the brave truck drivers risking their lives on the roads of Iraq.) It's the millions who got nothing at all.

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