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# Reducing the Risks of Depending upon Foreign Industries

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James F. Miskel

**A** COMMON VIEW AMONG NATIONAL SECURITY strategists is that the United States is courting trouble by importing too many defense-related components and technologies from Europe and Asia. According to this view, the United States has allowed itself to become so dependent upon imported components, subsystems, and materials that the success of future military operations may very well hinge upon continued access to and cooperation by foreign suppliers.<sup>1</sup> Adherents of this view acknowledge that an interruption in the flow of defense-related imports would obviously have less dire consequences today than it might have had during the Cold War, when national survival and the global balance of power could have been at stake. Even so, they hold, the consequences might still be substantial.

For example, during the Persian Gulf War of 1991 the United States depended upon foreign industries for a number of essential goods and services. Industries in Western Europe were important sources of the munitions and heavy-duty trucks that were employed by the Desert Storm coalition. Asian industries provided essential electronic components. Merchant marines of Europe and Asia provided nearly half of the sealift ships required by Desert Shield and Storm.<sup>2</sup> Speculation aside as to what could have happened on the battlefield had these imports been unavailable, suffice it to say that the preparations for the Gulf War would have been greatly complicated and perhaps considerably slowed if foreign industries had not continued to export to the United States.

Because the consequences of an interruption in the flow of defense-related imports could indeed be severe, a number of strategies have been proposed in recent years to reduce the risks associated with dependence upon foreign

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A fuller treatment of the foreign dependence issue is found in the author's *Buying Trouble? National Security and Reliance on Foreign Industry* (Lanham, Md.: University Press of America, 1993).

industries. Many of these strategies reflect assumptions that are at odds with the industrial and political realities of the post-Cold War era and thus are not likely to be effective risk-reduction strategies. This does not mean that the problem should be ignored as beyond repair. As will be discussed, new policies for the foreign dependence issue need to be developed, and this article concludes by identifying approaches that seem worthy of further study.

The strategies that have been proposed for reducing the national security risks of foreign dependency generally fall into two categories. One would mitigate risk by limiting the amount of defense-related goods and services that the United States would import during wartime, typically through "buy American" restrictions on military acquisitions or through subsidies for domestic industries. The other would adopt trade and acquisition policies that permit dependencies to develop only upon those foreign industries that Washington expects to be reliable in the future; at the same time, dependence on all other foreign suppliers of defense-related goods and services would be limited through deliberate government actions.

Before discussing these approaches, two preliminary observations are warranted. First, effectiveness is often in the eye of the beholder. The managers and workers at an ammunition factory would naturally regard as highly effective any policy that enabled their factory to keep its financial head above water. Yet for a variety of reasons, staying the closure of that particular plant may not materially reduce the overall damage that an interruption in imports could cause. The focus of this article will be on national, macro-level effectiveness, not on possible impact on individual facilities.

A second observation is that the foreign dependence issue has itself two dimensions: reliability and capacity. Both are important in that wartime shortages can result when unreliable foreign industries stop exporting to the United States or when reliable foreign industries lack the capacity to increase production quickly. Although the battlefield effects are identical (e.g., insufficient supplies of munitions for artillery or of spare parts for aircraft, too few chemical protective suits to replace units that have reached their expiration dates), production capacity and reliability are different issues. With respect to reliability, the issue is whether foreign industries can be counted upon to export defense-related goods and services to the United States during wartime. Capacity is a matter of the speed with which the foreign industries exporting to the United States can increase their output. Furthermore, capacity is a consideration for both foreign and domestic industries, whereas reliability is an issue only for foreign industries.

A foreign industry may be reliable in that it would not deliberately interrupt production of defense-related exports to the United States; practical obstacles, however, could nevertheless prevent it from increasing production quickly enough to meet American military requirements. Indeed, foreign industries are

## 42 Naval War College Review

affected by many of the same problems that might impede domestic manufacturers. Examples of the factors unrelated to reliability that could constrain production increases are shortages of raw materials, lack of capital, insufficient time to train new workers properly, environmental regulations delaying the construction of new factories, and restrictions on the disposal of waste that accelerated production in existing plants would produce.

Capacity problems could also develop during coalition wars if industries located in allied nations are unable to meet the combined production demands of the Pentagon and their own ministries of defense. If that were to occur, the industries would understandably give precedence to orders from their own national governments, leaving American demand at least temporarily unsatisfied. Some observers believe this possibility to be one of the risks associated with reliance upon foreign industry.<sup>3</sup> To an extent it is—but the risk derives from the industry's capacity, not its reliability.

Because many discussions of foreign dependence treat reliability and capacity as if they were two sides of the same coin, it is often assumed that policies addressing reliability will have complementary effects on capacity, or that reliability and capacity problems can be resolved with a single stroke. Unfortunately, some measures that have been proposed to mitigate reliability risks would actually make capacity problems worse; this would be particularly troublesome as the United States, Western Europe, and the former Soviet Union all downsize their defense industrial bases. In the discussion that follows of various approaches to reliability risks, an eye will be kept on their probable effects on capacity.

### Protecting Domestic Suppliers

Many recommended approaches to the reliability problem call for indirect financial incentives to protect domestic industries from foreign competition. Examples include “buy American” restrictions on defense-related goods and services, tariffs or quotas on imports, and voluntary restraint agreements under which exporting nations agree (under pressure from Washington) to limit “voluntarily” the amount of goods and services they export to the United States.

“Buy American” rules have been in existence for years, and a significant number of items are already restricted to domestic industry. Some, but not all, of the rules provide exceptions for industries in nations whose markets are relatively open to American defense exports. These *quid pro quo* arrangements are designed to facilitate peacetime trade and promote the interoperability of equipment among Nato armed forces. They do not reflect explicit judgments about the wartime reliability of the “excepted” industries.

Among the products that have been reserved for domestic contractors are periscopes, casings for various munitions, land mine components, rocket motors, night-vision goggles, "Meals Ready to Eat," fabric for chemical protection suits, and cold-weather boots.<sup>4</sup> In the transportation sector, similar rules bar foreign shippers from trade routes in American coastal and inland waters and reserve most international government cargo (e.g., food aid shipments and military supplies for overseas bases) to domestic merchant marine carriers.

Industries shielded from international competition are able to charge higher prices than those that must compete against overseas producers having lower cost bases or heavy subsidies. From the reliability perspective, these higher prices are wise investments if the right industries benefit and the higher prices induce domestic industries to continue "stateside" production and spend money on maintenance and modernization. However, from the capacity perspective, "buy American" restrictions and direct subsidies can be counterproductive. Because the rules discriminate against all foreign industries, reliable foreign industries—however few or many these may be—lose peacetime access to what is still the world's largest and most valuable defense market. Thus, reliable foreign industries may be forced to leave the defense trade or to defer investment in maintenance and modernization. In either case their ability to increase production quickly in response to wartime demand from the United States, from American-led coalitions, or from their own national governments, would suffer.

Whereas "buy American" restrictions and domestic subsidies seek to prevent future erosion of the U.S. industrial base, a primary purpose of various stockpiling and war reserve programs is compensation for *past* erosion. Stockpiles of raw materials and reserves of finished products and components reduce the volume of goods and services that would have to be imported during wartime; they thereby greatly diminish the impact that an embargo on wartime exports to the United States might have. Stockpiles and war reserves can also reduce the amounts that would have to be produced by domestic or reliable foreign industries during a crisis. Thus, stockpile and war reserve programs tend to have compatible effects on reliability and capacity, unlike programs that protect domestic industries from foreign competition.

War reserve programs include the multibillion-dollar inventories of military supplies and equipment that the Defense Department prepositions in depots in the United States and overseas, the Ready Reserve Force fleet of cargo ships, and the Civil Reserve Air Fleet for commercial air carriers. The latter programs were activated for the first time during the Gulf War to supplement military sea and airlift. Had the United States been unable to call upon these programs during Desert Shield, significant capacity constraints in transportation would have resulted, as would have greater dependence upon foreign merchant marines and air transport.

The Strategic and Critical Materials Stockpile is a similar program, under which raw materials worth about \$9 billion are kept in storage to eliminate “dangerous and costly dependence by the United States upon foreign sources of supply.”<sup>5</sup> It has also been used to remediate capacity constraints. For example, throughout the 1980s stockpiled ferroalloy ore was refined to meet purity specifications; the process was financed through the sale of tin from the stockpile. The refining was performed by domestic industries, and the refined product was

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then returned to the stockpile for possible wartime use. This arrangement addressed capacity problems in two ways: the amount of refining that might have been necessary during wartime was reduced, and domestic refineries were given extra business during peacetime—with, accordingly, incentive to stay in that business longer.

Eliminating reliability risks by building a vast array of industrial subsidies, expanding war reserves, and stockpiling great quantities of materials would certainly cost far more than the nation will be willing to spend in the 1990s. Even the Defense Department, which presumably would have the most to lose from unreliable foreign sources, will oppose major expansions of these programs, because they would draw funds away from higher-priority accounts like research and military readiness.

Conceivably the costs could be limited by targeting a select group of industries or facilities rather than by attempting to cover the entire industrial base. The drawback to this approach to the reliability issue is that the federal government does not know enough about the extent of the nation’s current dependence upon foreign industries. This point has been repeatedly affirmed by experts since the mid-1980s, and as recently as March 1993 the General Accounting Office reminded Congress that “DOD generally does not know whether and to what extent it relies upon foreign technology and products to meet its critical needs.”<sup>6</sup> Attempting to reduce reliability risks without first evaluating current dependence on foreign sources would be analogous to closing the barn door without first looking to see if any horses are inside.

If a defense industry or facility is already dependent upon a continuous flow of imported raw materials or components, reliability risks will not be reduced by protecting that industry or facility from foreign competition. Similarly, if only one of several imported components for a particular weapon is stockpiled, wartime production of the weapon can still be interrupted if the suppliers of the

other components prove unreliable. Moreover, subsidies may not even prevent a bad situation from getting worse—the recipient of subsidies might develop further foreign dependence if its domestic suppliers fail to match the quality and cost of imports.

The point here is not that subsidies and “buy American” programs are ineffective tools, but rather that the nation does not know enough about the defense industrial base and its relationships with foreign industries to use such tools properly to reduce reliability risks, or to do so without creating capacity problems. Defense industries in the United States are highly complex enterprises, and it is hardly surprising that the relationships among the prime contractors, subcontractors, and suppliers are not fully grasped by the federal government. Precisely because the entire production chain is imperfectly understood, however, it is virtually impossible to guarantee that protecting any one link (or stockpiling any one component or raw material) would have more than a marginal effect on wartime procurement reliability. Acquiring a thorough knowledge of the defense industrial base—i.e., the insights that would be necessary for a serious effort to reduce reliability risks—is a task that would require substantial amounts of time, money, and professional expertise; it does not appear achievable in the current budget climate.

Moreover, defining essential industries as those facilities that produce essential products or components overlooks the fact that essentiality is situational, a function of more than the inherent characteristics of the particular end-product, component, or service. A factory that produces an important component, for example, may itself become unessential once an ample supply of that component is produced, or when additional manufacturers in the United States or reliable foreign nations come on-line, or if technological breakthroughs enable the introduction of substitute components.

Finally, the process of deciding which prime contractors, subcontractors, and suppliers merit protection or subsidization is inescapably political. Perhaps even more so is the process of terminating existing protections and subsidies. By their very nature such programs favor vested interests, the existing industries that employ constituents and pay local taxes, at the expense of emerging industries whose potential contributions to national security are necessarily less well appreciated. Favoring existing industries may have been appropriate when the threat was near-term, as was arguably the case in the Cold War; but the Cold War is over, and it is the emerging industries that may be the most important in the future.

### **Predicting Which Foreign Sources Will Be Reliable**

The second general approach to the reliability issue assumes that at least some foreign industries can be counted upon during wartime. A corollary assumption

is that Washington will have the foresight to formulate and administer effectively policies that allow dependence to develop only on reliable sources, while simultaneously preventing wartime dependence upon unreliable ones. These assumptions are, in fact, embodied in recent legislation. For example, the 1992 amendments to the Defense Production Act direct the executive branch to evaluate the reliability of foreign sources and to reduce dependence upon foreign industries that do not measure up to minimum standards.<sup>7</sup> Obviously, the criteria for evaluating reliability are crucial; yet the legislation is silent on the subject. While there is no unanimity, most students of the issue have advocated criteria that treat reliability as a reflection of the strength of political-military relations between the United States and the nation in which the exporting industry is located.

For example, in 1991 the Office of Technology Assessment, a research agency of the Congress, proposed a "co-belligerency" standard for reliability. Using this measure, the only reliable foreign sources would be defense industries in nations that are expected to deploy forces to fight alongside American soldiers.<sup>8</sup> Industries in neutral or allied-but-nonbelligerent nations (e.g., our Nato allies during the Vietnam War) would be considered unreliable under this standard.

During the Gulf War, however, there were no significant interruptions in the flow of imports from neutrals or nonbelligerents to the United States or other coalition members.<sup>9</sup> Thus the only contemporary empirical evidence suggests that the Office of Technology Assessment's co-belligerency standard is too rigorous. The Gulf War also demonstrated that a policy of depending only on imports from co-belligerents may be virtually impossible to administer. In order for such a policy to succeed, the United States must be able to predict accurately whether other nations will deploy their armed forces in future conflicts. Apart from Cold War confidence that the European Nato members would fight against a Soviet invasion, it has never been easy to guarantee predictions about co-belligerency. Even during the Cold War, there were substantial doubts about the willingness of Nato nations to participate in out-of-area conflicts; now that the Cold War is over, crises are more likely than ever to be outside the traditional Nato arena. The Gulf War offers an instructive example of the difficulty of foretelling the military policies even of close allies. For some time after Kuwait had been invaded there was considerable doubt about which Western European nations could be counted upon actually to commit forces to a ground war against Iraq. A strict application of the co-belligerency criterion during the early days of the Gulf crisis would have classified virtually all major European industries as unreliable.

A related but more pragmatic approach would be to base reliability determinations on current alliance relationships. The Center for Strategic and International Studies argued in a 1991 report that defense industries in all Nato



countries should be considered reliable as long as “the Atlantic Alliance remains strong.”<sup>10</sup> According to this view, the underlying strength of the Alliance is such that defense industries in Western Europe should be relied upon to export to the United States even when their national governments refuse to put military forces in harm’s way. By inference, defense industries in nations with equally strong political relationships with the United States would also be reliable; but as long as Nato is unique, defense industries in other nations would presumably be considered unreliable under this standard.

A clear benefit of this approach is that it finesses the uncertainties inherent in predicting the military policies of the individual nations from which the United States imports defense-related products. The drawback is that it is based on the untested and ultimately untestable assumption that defense industries in Western Europe will be reliable trading partners in 2000 and 2001 because Nato as a whole is strong in 1995 and 1996.

While the Warsaw Pact remained a threat, it made eminent sense for the United States to assume that Nato would remain strong as a political-military

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alliance. But how long will Nato retain the same kind of strength now that the Soviet threat—the *raison d’être* for the alliance—has evaporated and trade frictions increasingly dominate dialogue between Europe and North America? At the very least it is likely that Nato will gradually weaken as a military alliance. If that happens, there would be less reason to regard a nation’s membership in Nato as sufficient assurance that its industries will be reliable wartime trading partners.

There could as well be turnover in Nato, which would reflect both that the nature of the Alliance was changing and that difficulties could flow from a policy equating industrial reliability with Nato membership. Many Eastern European nations have expressed strong interest in joining, and it is possible that the Czech Republic, Poland, and even Ukraine might eventually be admitted through the Partnership for Peace. If that were to happen, should Czech, Polish, or Ukrainian industries be considered reliable wartime suppliers?

Conversely, under some circumstances longstanding members could leave the Alliance. For example, it is not inconceivable Turkey might someday decide to withdraw in response to a territorial dispute with another Nato member, as a protest over the treatment of Turkish emigrant workers in a northern European Nato state, if its industries were denied free access to the single European market, or if the United States pursued accords with Russia that frustrated Turkish ambitions in the Central Asian republics of the former Soviet Union. To provide

## 48 Naval War College Review

another example, Greek opposition to the newly recognized Former Yugoslav Republic of Macedonia could result in the eventual estrangement of Greece from the rest of Nato. If wartime reliability were equated with Nato membership, Turkish and Greek industries would cease to be considered reliable if and when Ankara or Athens decided to leave the Alliance. Assuming that Washington wanted to maintain amicable relations with lapsed members (or wished to bring them back into the flock), it obviously would be counterproductive for the United States to adopt trade policies that discriminated against defense-related imports from Turkish or Greek industries.

Predictions about the long-range future and composition of the Nato alliance and about the military policies of other nations in as-yet-unforeseen crises are not merely academic exercises. Unreliable sources need to be identified years before a crisis arises in which access to imports could be militarily significant. According to the Defense Department it can take a year or longer for existing facilities to manufacture major pieces of military hardware, and this time frame is likely to grow as defense industries respond to military spending cuts by consolidating operations and liquidating assets.<sup>11</sup> Clearly, building new plants to replace unreliable foreign producers, shaking down the new facilities and then refilling the military hardware pipelines could add many months to the process. Thus if Nato is destined to weaken over the next several years, the time to start taking industrial action to reduce dependence upon defense industries in Western Europe is now, not in 1998 or 1999. If Japan or France, for example, are considered unlikely co-belligerents in whatever crises may erupt at the turn of the century, efforts should be initiated in 1995 or 1996 to reduce dependence upon those nations' defense industries.

If distinguishing between reliable and unreliable foreign industries is to be a meaningful exercise, political consequences must flow from predictions of another nation's unreliability in future crises. But there is a fundamental dilemma: designating industries in neutral, friendly, or even allied countries as unreliable would obviously be inimical to day-to-day diplomatic relations and would be stoutly resisted by the foreign policy establishment. Moreover, as long as there are no serious threats on the immediate horizon, taking action to reduce dependence upon unreliable foreign industries would be seen as having higher diplomatic costs than military benefits.

Another policy recommendation for reducing reliability risks is diversification. This approach recognizes that many foreign industries will be reliable suppliers but concedes the impossibility of identifying exactly which foreign sources can be relied upon and which should not be taken for granted. Under the diversification strategy, the risks of relying upon unreliable sources would be minimized by importing from multiple suppliers and avoiding heavy dependence upon foreign industries that dominate their respective markets.<sup>12</sup> Rather than buying large quantities of imports from one or two industries in a single

country, the United States would reduce its reliability risk by apportioning orders among manufacturers in several countries, the theory obviously being that the shortages caused by a supply interruption will be more manageable if the affected supplier is only one of many sources. As sensible as diversification sounds, however, it too confronts serious practical limitations.

One is that for an increasing number of defense products multiple sources simply may not be readily available. As defense industries in the United States, Europe, and Asia consolidate and “convert” to commercial activities or go out of business entirely, pools of second, third, and fourth suppliers will shrink like puddles in the hot sun. Indeed in some product lines the pool has already shrunk to the point where the first and second manufacturers have merged, the third is phasing out of the defense business, and the fourth has declared bankruptcy. A second limitation is that budgetary pressures will almost certainly prevent the Defense Department from spending what would be required to identify, develop, and qualify second, third, and fourth suppliers and to provide enough business for these companies.

Even when it can be implemented, diversification could negatively affect capacity in the same way that during the nineteenth century Irish inheritance laws diminished the capacity of peasant families to make a living from their farms. The Irish laws prevented land from being passed on to a single heir; thus farms were continuously broken up into smaller and smaller plots, and successive inheritors became progressively less able to feed themselves and their families. Aggressively pursuing diversification during an era of reduced defense spending could result in a similar vicious cycle of progressively smaller contracts being distributed each year among progressively weaker industries. All other things being equal, higher levels of investment in maintenance and modernization are more likely when there are one or two suppliers than when there are four or five. With respect to capacity, as the overall level of defense business decreases, one or two high-volume suppliers may be in a better position to meet crisis production goals than four or five low-volume suppliers.

**M**ost recommendations made in recent years to reduce the reliability risks associated with dependence upon foreign industry suffer from insufficient knowledge. In particular, proposals to protect or subsidize selected industries and facilities suffer from insufficient data about existing dependencies and trends in the global industrial base. This lack of knowledge ultimately means there is no way to ensure that whatever actions the government does take will have more than a marginal effect on reliability risks. Subsidies to a domestic gear manufacturer may, for example, enable that particular manufacturer to stay in

## 50 Naval War College Review

business; but they do not ensure that the raw materials or additional production machinery the firm needs will be available during wartime, or that all of the other components that join with those gears in a weapon system or military vehicle will be available in sufficient quantity.

Imperfect knowledge about the political and military policies that other nations will adopt in future crises raises doubts about the efficacy of proposals to allow dependence to develop only with allies or co-belligerents. Also, lack of both funding and knowledge about industrial developments overseas makes problematic any recommendation to diversify foreign sources.

There are, however, more promising and less expensive alternatives that deserve further consideration. One is to make anti-American trade embargoes more difficult to administer. This aim could be accomplished as a by-product of free trade agreements with neighboring nations, for example the North American Free Trade Agreement, or an arrangement that included some or all Central and South American nations. In order for an anti-American embargo to have a tangible effect, the embargoing nation would have to prevent its exports from reaching any of the participants in the free trade arrangement. Another approach worth study is to base reliability predictions on the strength of a nation's economic ties to the United States rather than traditional political-military relations. The assumption here is that some nations cannot afford to be unreliable. Japan and some other nations rely heavily upon access to the American market and have substantial economic investments in the United States. In the post-Cold War era, protecting that access and those investments could be more likely than political and military ties to motivate industrial cooperation.

In the end, however, the outlook with regard to foreign dependence may be much more reassuring than it has seemed to be, and thus the urgency of "doing something about it" may be rather less than has been thought. That becomes apparent when, as the post-Cold War regime requires, we view the world and its future through a lens that is principally economic, not exclusively political or ideological. We see then that the risks of a major trading partner proving unreliable during a crisis may be lower now than at any time in recent years. With the collapse of the Soviet Union there is no superpower that could pressure our trading partners into embargoing exports to the United States. Nations like Iraq and Iran that might, for their own purposes, wish to embargo the United States do not manufacture products essential to the American military. Their only essential export, oil, is a raw material that can be obtained from other sources or purchased through middlemen in Europe or South America. Thus, the ability of potentially unreliable sources to damage this nation materially is not what it once was; their exports must be sold somewhere, and, in the absence of a competing superpower, must ultimately become available to the United States.

That the true implications of reduced self-sufficiency are now uncertain ties the issue of reliability to that of protecting domestic suppliers. Of course, it stands to reason that a defense electronics factory in California buying semiconductors from a plant in Texas should be a more reliable military supplier than an equivalent firm in Korea that imports components from Malaysia. But the real question is whether the increased reliability that the California and Texas facilities offer—so important during the Cold War—remains as vital in its aftermath. Finally, then, is that greater reliability worth the high prices that the nation would have to pay (and in fact is now paying) to keep these domestic manufacturers in business? Or would the money be better spent keeping modern and diversified defense firms competitive, or in promoting research and development?

It may well be that neither “globalizing” the nation’s defense industrial base nor “right-sizing” its present domestic one will create a significant vulnerability, even in the dangerous new world. If so, any actions the United States might take to hedge against those processes will inevitably siphon scarce resources away from more important national priorities.

### Notes

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## 52 Naval War College Review

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Let us learn our lessons. Never, never, never believe any war will be smooth and easy, or that anyone who embarks on the strange voyage can measure the tides and hurricanes he will encounter. . . . Antiquated War Offices, weak, incompetent or arrogant Commanders, untrustworthy allies, hostile neutrals, malignant Fortune, ugly surprises, awful miscalculations—all take their seats at the Council Board on the morrow of a declaration of war. Always remember, however sure you are that you can easily win, that there would not be a war if the other man did not think he also had a chance.

Winston Churchill  
*A Roving Commission*

The end of the short-lived distraction of the Cold War means that the Royal Navy can now get back to its proper business—fighting the French!

Rear-Admiral Guy F. Liardet, C.B., C.B.E., Royal Navy  
(From "After Dinner Speech: Trend and Change," in  
James Goldrick and John B. Hattendorf, eds., *Mahan Is Not  
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