

'Peace dividend' wrecks California

Silicon Valley fantasizes that trade with Gorbachov will bail it out after defense cuts. Part I by Brian Lantz.

On the night of June 3, Mikhail and Raisa Gorbachov arrived in San Francisco. On June 4, Mikhail met with former President Reagan, held a summit with South Korean President Noh Tae Woo, lunched with West Coast business and financial leaders, and met with the region's "brain trust" at the Hoover Institute and Stanford University. Simultaneously, top Soviet and U.S. high-technology industry leaders were meeting in a week-long "Soviet-Silicon Summit" on joint ventures, licensing of technologies, design development, and trade.

The Gorbachov visit to San Francisco was the work of former Secretary of State George Shultz, now a Hoover Institute senior fellow, and Harry Orbelian, son of a KGB general. Orbelian is the longtime head of the International Affairs department of the San Francisco Chamber of Commerce. Shultz's former employer, Bechtel Group, Inc., has announced an agreement with the Soviet government to do a feasibility study to build a Soviet version of California's "Silicon Valley," as the state's electronics and high-technology industrial corridor is called. During Gorbachov's U.S. tour, Chevron Corp., also based in San Francisco, signed a pact to explore development of the strategic Tenghiz oilfield, near the Caspian Sea.

There is no question that Gorbachov desperately needs Western help. The Russian leader's wants, however, are almost equaled by those of his West Coast hosts. With the collapse of the "Sun Belt" and New England industrial economies, and now, their real estate markets, it is now California's turn in the barrel. Desperate circumstances make for wishful thinking.

The crash of the aerospace-defense sector

There is irony in the desperate efforts of California's captains of industry and finance to woo the current President of the Union of Soviet Socialist Republics. Since World War II, the industrial core of California's economy has been the aerospace, defense, and electronics sectors. Here we will consider the crash of the aerospace and defense industry, the largest such production capabilities in the nation.

Twenty-six percent of all Americans engaged in military

and aerospace production are—or were—working in California: some 760,000 scientists, engineers, and skilled workers. Lockheed Corp. has produced every submarine-launched ballistic missile (SLBM) since the advent of the Polaris submarine. Lockheed is producing the MX missile as well. Rockwell and Northrop produce the Stealth (B-2) and B-1 bombers. McDonnell-Douglas has been one of the five largest producers of commercial transport aircraft in the world, with 20% of the existing market.

Southern California, whose defense industry has received more of the U.S. defense budget than any other region of the country, is now being hit by cuts in defense spending that began "upstream," in 1985. The famous corridor along the Interstate-405 highway, stretching south of Los Angeles Airport, has been hit with waves of defense budget cuts.

- In late April, McDonnell-Douglas Aircraft Co. announced plans to lay off 3,000 aerospace workers involved in commercial and military production lines from its aircraft division in Los Angeles. More bad news followed. Defense Secretary Richard Cheney announced that the Pentagon was slashing orders for McDonnell-Douglas's C-17 aircraft. McDonnell-Douglas suffered an \$84 million loss in the first quarter, including non-military projects.

- Hughes Aircraft eliminated 6,000 jobs in the second half of 1989, most of them in southern California. As just one consequence, the city of El Segundo raised its per employee business tax from \$40, to \$60, to \$120 as a means of offsetting the impact of Hughes Aircraft layoffs. More layoffs are expected. Hughes is the largest single private employer in California.

- On May 8, Lockheed Corp. announced layoffs of 2-4,000 southern California workers. It will close its Burbank, California operations, including the famous "Skunkworks." There will be 9,000 workers laid off over the next two years. The Burbank facility represents 5.5 million square feet of factory space, where 35,000 aircraft have been produced, including the famous "Blackbird" spy plane, the fastest plane in the world, which has just been retired.

Thousands of additional layoffs have occurred at Northrop, General Dynamics, Litton Industries, TRW, and the

Sacramento-based Aerojet Corp., over the last 12 months. Lockheed just fought a costly junk bond takeover attempt. In April, the American Electronics Association canceled a planned defense industry trade show in Silicon Valley, due to lack of interest. Already-proposed military base closings will mean a loss of an additional \$5-10 billion to the California economy.

What California state budget analysts have quietly spoken of since 1988—the loss of 100,000 aerospace and defense-related jobs by 1990—is fast becoming fact. The combination of increasing defense budget cuts and growing corporate indebtedness means that the hemorrhage of defense and aerospace layoffs will reach at least two or three times the 1988 projected figure.

Shared delusions

Steven E. Hall, economist and fellow at Stanford University's Hoover Institute, recently dismissed defense sector cuts as "not a big deal." His comments, mirrored in remarks made by Bank of America chief economist Robert O. Wilson, poorly disguise the state of the California economy. A precipitous decline in state tax revenues, personal and corporate, doesn't lie.

And then there is real estate.

On the occasion of a recent medical conference, called to explore the meaning of composer Richard Wagner's hallucinatory "Ring" opera cycle, Dr. Leonard Zegans of the

Langley Porter Psychiatric Institute observed that Wagner's gods had much in common with San Franciscans: They are always overdressing and getting caught up in disastrous real estate deals. Dr. Zegan's comments may be applied more broadly.

The spiraling cost of California's commercial and residential real estate has left financial institutions vulnerable to the layoffs that are occurring. In April, Federal Deposit Insurance Corp. (FDIC) chairman L. William Seidman warned that California's real estate markets might be overheating and should come under "increased scrutiny." The booming Anaheim and San Jose, California markets were named as potential flashpoints. On May 14, Standard and Poor's downgraded the debt portfolio of California's prosperous Wells Fargo Bank because it heavily relied on real estate loans and junk bond investments. Then on June 13, Moody's Investors Service lowered its ratings on Wells Fargo of San Francisco and Security Pacific Corp. of Los Angeles, citing the softening real estate market.

Putting the abundant advice of "free enterprise" and "market forces" to one side, the hosts of Mikhail and Raisa Gorbachov were in no position to provide a "quick fix" for the disintegrating Russian empire. It is certain that Soviet officials are likely to be of little help to their California friends.

Next: The decline of the 'New Age': California's Silicon Valley.



CORRECTION

Our June 8 issue, on page 23, mistakenly identified the person on the left-hand side of the photo above as Dr. Richard Wilson. Wilson, a nuclear physicist, is on the right. With him at Chernobyl in this 1987 photo is Bob Sheer, a reporter from the Los Angeles Times. Sheer's photo is the one that appeared with Wilson's interview by mistake.