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With Pentagon Hiding
Billions of Its Outlays****Stealth Bombers and Fighters
Expand Classified Total;
Is It All That Necessary?****How Bidding Can Be Averted**By ROY J. HARRIS JR.
And ROBERT S. GREENBERGER

Staff Reporters of THE WALL STREET JOURNAL

A black hole is growing inside the federal government, and it is pulling in billions of dollars a year.

Like the celestial black holes, this phenomenon can be seen mostly by its effects: Lockheed Corp.'s 7,000 or so employees in Burbank, Calif., busily working on something the company steadfastly refuses to discuss; giant C-5 military transports roaring out of the Hollywood-Burbank airport on late-night secret missions; unexplained gaps in the financial reports of defense contractors, and the recent disappearance of an entire Pentagon agency from the federal budget for research and development.

What's happening is a sudden and enormous rise in military secrecy, particularly of so-called black programs, ones so sensitive that their very existence is known to only a handful of top government and corporate officials.

The government, of course, won't acknowledge how much it is spending on black programs. But those who study the difference between the government's total \$302 billion defense-spending plan and the programs broken out in the complex tangle of budget proposals estimate that between \$10 billion and \$30 billion is being hidden. The Center for Defense Information, an independent research group often critical of administration policies, calculates that the black budget has shot up at least 50% for fiscal 1986, which begins next Tuesday.

Why Total Rises

The size apparently has ballooned lately because of a few huge programs nearing the production stage: especially "Stealth" fighters and bombers—aircraft whose nickname derives from their ability to evade radar. But black programs cover an array of hardware and programs, from spy satellites and futuristic electronic weaponry to the plans for protecting the president in case of war.

Sometimes public efforts become black programs. The research and development budget of the Pentagon's Defense Mapping Agency, which prepares the data that guide bombers and cruise missiles, vanished from this fiscal year's budget. This fast-growing portion of the agency's budget increased from \$70 million in 1983 to a request for \$207 million in 1985 before disappearing into the black budget.

When black programs do show up in the Pentagon budget, they are undefined and unquantified. They often are cloaked in intriguing code names like "Theme Castle" and "Omega," or deceptively familiar ones like "Bernie" and "Leo." Experts piece together information that yields clues about these code names. David Morrison, of the Center for Defense Information, believes that black budget codes begin with "Seek," such as "Seek Axle" or "Seek Spinner," refer to radar systems. Mr. Morrison notes that unclassified Pentagon documents frequently refer to the FPS-117 radar, which is part of the U.S.-Canadian air defense system, as "Seek Igloo."

Pentagon's Position

In an age when weapons technology is developing at breakneck speed, larger numbers of programs must be kept from the public eye, says Britt Snider, the Defense Department's director for counterintelligence and security policy. Black programs are needed because "even acknowledging the existence of a program in some circumstances can provide an adversary with an indication of the direction of U.S. efforts" and allow the enemy to create a countermeasure, he says.

Even most of the nation's elected representatives must be excluded, defenders of black programs say. "Congress is a leaky place. You can't trust them," says Richard DeLauer, former undersecretary of defense for research and engineering.

Some lawmakers aren't impressed by such arguments. "I recognize some things have to be secret. But (the Pentagon is) putting up a serious barrier that's not in the public interest," says Democratic Sen. Paul Simon of Illinois.

In what could be a major challenge to the administration's secrecy effort, Rep. Mike Synar of Oklahoma has sponsored an amendment to the defense authorization bill that would require a report to Congress by next February on the total cost of Stealth bomber development. The Democrat's bill would prohibit procurement funds until Congress receives the report.

Debatable Results

It is debatable whether the secrecy really keeps all that much information from the Russians. Bill Sweetman, a San Francisco journalist writing a book on Stealth technology, describes Lockheed-built Stealth fighters' being sequestered in individual, spy-proof hangars on a corner of Nevada's Nellis Air Force Base. But, he

says, Soviet satellites are hanging overhead all the time—you can see them at night in the desert sky"—presumably watching the planes fly through simulated Russian radar defenses.

The amounts being spent on secret programs, though hidden in the Pentagon budget and in financial reports by contractors, may also be discernable. Benjamin Schemmer, the editor of Armed Forces Journal, a monthly magazine published independently of the military, says that the size of the holes in military arms requests is so apparent that "the Russians can figure it out with third-grade mathematics."

Another worry is that classification may simply be a way to protect the military and contractors from criticism about high costs and abuses. In black programs the military normally picks contractors privately, short-cutting the system of seeking low bids from various competitors, says Melvin Laird, a Nixon administration defense secretary, who believes secrecy has expanded far more than necessary. "You've got to be careful that you're not using the black route to avoid competitive bidding," Mr. Laird says.

Some in the defense industry, however, claim black programs actually tend to be better buys for taxpayers. "There's much less red tape and much more flexibility" in black programs, says Willis Hawkins, a Lockheed senior adviser who recently retired as senior vice president for aircraft. He says Lockheed's "Skunk Works" operation in Burbank, where much of the company's secret work is done, "had a history of turning money back to the customer over and over again," and generally did similar work at costs 25% below Lockheed's other programs.

The claim can't be substantiated, Mr. Hawkins concedes, because of the secrecy of the programs involved. And one official of a Lockheed competitor has some doubts: "If a coffee pot costs \$10,000 on a white aircraft, can you imagine what a contractor charges on a black one?" he asks.

Whatever the costs, however, history illustrates that politics, and sometimes economics, can play as much a role as national security in determining when a program leaves or enters the light.

In the 1960s, for example, President Johnson made Lockheed's top-secret SR-71 spy plane public because "he decided he wanted credit for it," Mr. Hawkins says. (The U-2, another Lockheed-built spy plane, got an embarrassing public debut in 1960 after the Russians shot one down over their territory.)

President Reagan's current Strategic Defense Initiative opened up many formerly black programs—at least temporarily—as a part of his drive to gain public and scientific support for developing the so-called Star Wars technology.

Continued

Particularly instructive is the history of the nation's Stealth bomber program.

Research into reducing the "signature" of an aircraft—the various images that are picked up by radar and other defenses—first slipped into blackness in the early 1970s. That was when well-publicized industry theories began to jell into a plan for building a jet that was "invisible" to the enemy. Only tidbits of information leaked out. Several sources, for example, reported at least one crash in Nevada of an early design by Lockheed (nicknamed Harvey, after the invisible rabbit of fiction). A local newspaper even identified a Lockheed pilot who had gone into a hospital with post-crash injuries, although reporters trying to follow up found the crash report classified.

Secrecy was tightened even more by the Carter administration in 1977. In 1978, a Pentagon official asked Mr. Schemmer, the Armed Forces Journal editor, to kill a major article on the emerging Stealth technology. He obliged, believing the story might do "immense, grave damage" to the nation's security.

Two years later, the editor was amazed when the same Pentagon official, William J. Perry, volunteered an on-the-record interview about Stealth. Shortly thereafter, in October 1980, the defense secretary, Harold Brown, held a press conference announcing that work was under way on an aircraft designed to be undetectable to radar.

Carter officials said the release was prompted by leaks in the news media about Stealth. They noted that they gave out only scant data about technology and the potential for a bomber.

Other Possible Motives

However, critics suggest the announcement was more timed to help President Carter's reelection bid that year and to justify the controversial decision to cancel the B-1 bomber. Mr. Schemmer, a firm believer in the need for black programs, says the government's release of the Stealth information was premature and "compromised security far more" than his original story would have.

The Reagan administration hasn't been immune to outside pressure on Stealth bomber secrecy.

In 1981, Aviation Week, a major trade publication, identified Northrop Corp. as the program's prime contractor and placed the overall value of the bomber work at \$21.9 billion. Over the next several days, Northrop stock surged 15% and was heavily traded. The New York Stock Exchange halted trading until Northrop could make an announcement about the reasons for the activity.

Initially, the company felt it couldn't comment. But when stock trading was halted, the company made an urgent appeal to the military for some kind of announcement, says one person who was close to the matter. Air Force officials resisted. But finally the Air Force and Northrop made a terse announcement saying that Northrop was indeed the prime contractor for research on an advanced-technology bomber and that the program would have "material significance" for the company. After that, the company's stock resumed trading.

Officials involved in that decision insist they didn't compromise security for the sake of securities. "The main thing was to protect the developmental design of the aircraft. The contractor part of it wasn't necessarily as sensitive," says Gen. Richard Abel, at the time the Air Force's chief of public information.

Boon for Northrop

For Northrop, the announcement helped solve an increasing embarrassment of riches. Just a few days later, the company reported a 30% increase in quarterly sales that it couldn't otherwise have explained. "It was like being pregnant," recalls one Northrop executive. "People were starting to notice."

Lockheed, on the other hand, can't talk

about its reported Stealth efforts, including the widely published speculation that it is building Stealth fighters in Burbank and transporting them out at night in C-5s.

Gen. Abel suggests that the Air Force disclosed only the Stealth bomber contractors because that program "had received so much visibility" in 1980. But another factor keeping the fighter hushed may be that the much larger Lockheed—with sales last year more than twice Northrop's \$3.69 billion—is simply better able to conceal secret programs in its financial reports.

An inability to mask secret programs apparently changed one company's future. Little San Diego-based Global Analytics filed in 1983 for an initial public stock offering, describing itself as a specialist in Stealth technology for new and modified weapons systems. But the offering was withdrawn suddenly; a source close to the company says it was because the Air Force feared that sensitive information about the progress of Stealth technology could emerge in Global's required public filings.

Global Analytics later was purchased by Aluminum Co. of America, which lumps the unit's financial results in with a new defense systems division.

Alcoa declines to comment on Global Analytics.

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Securities Firms Hire Experts to Penetrate Pentagon Secrecy

* * *
New Breed of Analyst Studies
Budgets, Contractor Data
For Classified Projects

By ROY J. HARRIS JR.

Staff Reporter of THE WALL STREET JOURNAL

NEW YORK—Joseph Campbell used to be a national security aide in the Reagan White House. Since 1983, however, he has helped outsiders penetrate the mysteries of defense programs.

Mr. Campbell hasn't become a spy. He is a securities analyst who now uses his knowledge of the government's inner workings when he studies defense budgets or contractor financial reports that mask classified work. His employer, Paine Webber Group Inc., has made a special effort to bring to its research staff people who have "relevant experience" in the areas being analyzed, he says. And in the case of aerospace and defense, that means a background of dealing with military secrets.

As the hidden portion of the Pentagon budget has expanded, a community of academics, journalists and others has sprung up to analyze how taxpayer money is being spent by the government or earned by contractors. And several Wall Street firms have hired experts in classified programs to try a hand at figuring out defense-industry financial puzzles.

Lumping Together

"The analytical mind can't deal with jelly like what appears in company financial reports," says David J. Smith, who joined Sanford C. Bernstein & Co. last year after an Air Force career in which he claims to have worked around some secret aircraft programs. Companies tend to lump their secret projects in with unclassified work. So he spends much of his time estimating the size of hidden programs, like Northrop Corp.'s Stealth bomber, and projecting sales and earnings.

"I guess you could say I act almost like an intelligence agent in the work I do," he says. But he maintains that his information doesn't come from secret sources. Instead, it is based on his educated guesses about what the military needs, tidbits of information gleaned from Pentagon budget requests and corporate filings, and reports that appear in trade publications.

For all their expertise, this new breed of defense-industry analyst doesn't seem to be unusually prescient in estimating the earnings of such companies as Northrop and Lockheed Corp., with their heavy concentrations of classified programs.

Mr. Smith recently had to increase his forecast of Northrop's 1985 pre-tax operating profit from the Stealth bomber program by 60%, to \$90 million, based on his review of the latest government defense-spending proposal. The budget request indicated to him that the program has grown far faster than he had anticipated, he says. And a few months before Northrop reported its 1984 net income of \$3.63 a share, Mr. Smith had predicted earnings of \$3.30.

At the same time, Wolfgang Demisch of First Boston Corp., who doesn't have a background working with classified information, was a little closer, at \$3.35 a share.

The Big Picture

By concentrating mainly on classified programs, an analyst "can miss the big picture of how a company is doing," says Mr. Demisch, who concedes that he relies heavily on reports about secret programs that appear in such major trade publications as Aviation Week and Interavia, a European publication that often writes about Stealth technology.

Those press reports rarely are documented and often offer veiled hints about the nature and the size of various secret programs. The reporting technique of Bill Sweetman, whose Interavia stories are filled with colorful detail about Stealth aircraft, offers scant assurance that his information is always accurate.

Mr. Sweetman, based in San Francisco, says a lack of verifiable information often forces him to recount rumors that his Air Force sources won't confirm. His sources probably would tell him if a rumor was erroneous, he says, because "the Air Force doesn't want false reports to get too much credit."