



October 27, 2008

Letter from Washington

If you want to understand what the candidates believe the trend is in the endgame leading up to the November 4th election, just look at where they have been campaigning for the last week. Obama has been concentrating on states that went for George Bush in 2004, hoping to pick off a number of them that should be leaning toward McCain but are very much in play. McCain however, has been focused on trying to maintain what should be safe states for him, and is having to shore up his base with only 8 days to go before the election. Clearly this doesn't bode well for him.

Earlier in the month the McCain campaign made the decision to abandon all efforts and expenditure of money in Michigan, a state that was thought to be within reach as recently as mid-September.

Recall that several weeks ago McCain was drawing close, and in some polls even with Obama, especially after the last debate. Since then however, the combination of the deepening financial crisis and the controversy surrounding Sarah Palin, the Vice-Presidential running mate, have served to derail that up tick in McCain support.

McCain, who has run on his resume rather than a specific platform, has not responded well to the financial turmoil in the markets, and has mercifully ceased issuing new plans daily, but not before considerable damage has been done. Trying to appear on top of things and proactive, instead McCain came across as confused, offering a scatter-gun blitz of not well thought out programs that had the opposite effect on the undecided voters. Obama, always cautious, basically said nothing substantive, and by comparison appeared more thoughtful and Presidential.

McCain's signature issue has always been "who do you want in charge during a crisis". Unfortunately for him, a majority of Americans polled believe Obama and the Democrats are more capable of dealing with the economy and financial issues by a wide margin, which constitute the crisis of the moment --- just not the one McCain had visualized.

McCain's other problem has been Sarah Palin. Initially she was seen as a brilliant strategic choice for McCain, but she has not worn well. Palin has

been well received by the Republican base, where McCain really didn't need any help, but has increasingly been seen as either a divisive partisan or the female equivalent of an empty suit, by the independent and centrist-leaning middle --- the constituency that McCain has to have in his column to win.

All of these things together have added up to a bad October for McCain. Perhaps the worst sign is the growing internal dissension within the Republican party on where to apply the remaining resources. Since declining federal funding for his campaign, despite an earlier promise to accept federal funds with McCain, Obama has out raised the Republicans by a wide margin. Going into the last weeks of the campaign he has enough money to purchase a half hour infomercial on the major networks, as well as outgun McCain in every major market and all of the key states.

The National Republican Campaign Committee, looking at a potential Obama landslide, is attempting triage with the remaining funds, believing that the Presidential race is lost. The basis for an eventual Republican return to power probably lies in the Senate, and the effort is shifting to de-fund the Presidential campaign in those states that are apparently lost, moving those funds to close Congressional and Senate races. Clearly this does not sit well with the McCain brain trust, and the recriminations have already begun.

Barring some massive terrorist event that will shake Americans out of their complacency, or an equally massive occurrence of the "Bradley Effect" on election day, Obama will coast home to a major victory, probably carrying a number of states like North Carolina and Indiana that have been Republican for decades. The so-called "Bradley Effect", named after a black candidate for Governor of California in the early 80's, occurs when voters are polled and claim to support the minority candidate, but actually vote for the white. Even if there is a Bradley phenomenon on November 4th, most pollsters only credit it with a 3-4% shift, still comfortably within Obama's likely margin of victory. At this point the polls suggest that Obama could even lose the "key" electoral states of Pennsylvania, Ohio and Florida, and still win the 270 electoral college votes required for the White House.

In the Congress the Democrats are likely to pick up at least seven and possibly ten Senate seats, and up to 30 seats in the House.

The outlook is so grim for the Republicans that the best argument they can make in this last week is that it would be a major mistake for the American voting public to put both houses of Congress *and* the White House in the hands of one party, effectively removing all of the checks and balances. This will be especially true if the Democrats come close to picking up 60 seats in the Senate, giving them a filibuster-proof majority and allowing them to shut off debate, depriving the minority party of its most effective parliamentary tactic. While there is a great deal of truth in the no-checks-and-balances argument, it reveals the sense of desperation that has enveloped the Republicans for them to be using it in the first place.

Meanwhile, back at the Pentagon the Office of the Secretary of Defense has put the finishing touches on the FY-10 POM and subsequent FYDP. The plan calls for an almost US\$60B boost in FY-10 and across each year of the FYDP. These increases are intended to allow the Navy to get its shipbuilding programs in order and attain the 313 ship goal several years earlier than planned. The Air Force is taking the opposite tack and cutting almost 300 F-15 and F-16 aircraft, retiring them early to get aging aircraft off the flight line while receiving the financial benefit of taking them off the books. The Air Force plan calls for increased investment in C4ISR and other force multiplying technologies that will allow the remaining force to operate more effectively. Both Navy and Air Force will receive substantial procurement boosts to accelerate Joint Strike Fighter buys. The Army meanwhile intends to use the Abrams and Bradley programs as bill-payers for the FCS, focusing now on getting FCS technology out of the heavy vehicles and into the hands of the troops first.

OSD's attempt to enshrine these priorities before the incoming administration has a chance to tinker with them will likely be unsuccessful. Unlike most of the past administration changes that were effectively hostile takeovers, in this case the new President's party will also control the Congress, and can essentially rewrite the defense priorities on their own schedule. While it is highly likely that we will see huge spending increases with a Democrat-run administration, defense will more likely become the bill-payer for social programs such as health care, not even taking into account the trillions that have yet to be spent in shoring up the financial, banking and credit systems.

Finally, in what is at first look a big boost for Boeing, the FY-09 Defense Appropriation, which the President signed in early October, gives the Secretary of Defense the authority to take US industrial base considerations into account in major procurements. This language was inserted as a direct result of the failed tanker competition, and was sponsored by the Congressional delegations in Boeing states. The language does not tell the SECDEF what to do, but merely gives him the authority to consider the base in shaping acquisition policy. The effect, other than for the constituents back home, is unlikely to be significant.