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*A Hypothesis on the Content
of the Soviet Defense Budget*

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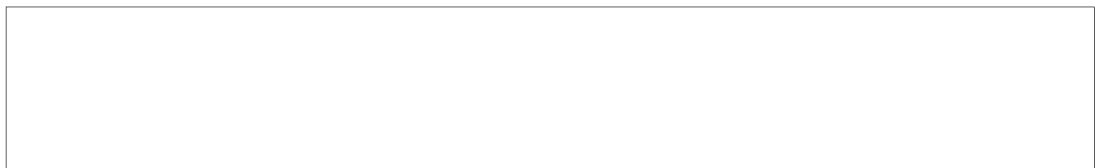
A HYPOTHESIS ON THE CONTENT OF THE SOVIET DEFENSE BUDGET

The Soviet government closely protects information on its defense spending, releasing only one official statistic annually. Moreover, the Soviets have never clearly defined what activities are included in this figure.

Several newly examined Soviet and East European unclassified financial books suggest that the defense budget covers only the maintenance and operating costs of the Soviet military establishment. Other costs, including the large expenditures for major weapons systems, are presumably hidden in nondefense categories of the state budget or financed from nonbudgetary sources. The published defense figure is reasonably close to independently derived CIA estimates for operational costs, although the trends in the two series differ.

The Soviet and CIA defense series are not, however, easily compared. Soviet budget data are expressed in current rubles, which includes the effect of military price increases. CIA estimates, on the other hand, are expressed in constant 1970 rubles, which removes the effect of price changes. When adjusted for inflation, the Soviet defense budget is higher than the CIA estimate for operational expenditures through 1970, and lower after 1970. Also, the CIA data indicate that Soviet military operating costs have been increasing annually since 1960. The Soviet figures show such costs rising prior to 1970 but falling thereafter. The discrepancy may be due to definitional differences, CIA data problems, or may result from the Soviet manipulation of the defense budget for political purposes. In any case, it is unlikely that Soviet operating costs could be falling in the 1970s in light of manpower and pay increases in the Soviet military as well as the increased complexity of Soviet weapons.

We do not have sufficient information at this time to prove our hypothesis that the defense budget is an operational budget. Nevertheless, consideration of this issue improves our overall understanding of Soviet defense expenditures and points out promising areas for future research.



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DISCUSSION

Introduction

The USSR maintains extreme secrecy on its spending for defense and constituent defense programs. Only one official figure on defense expenditures is released annually--the single-line item labeled "Defense" in the Soviet state budget. This number, however, is clearly too low to cover the full range of Soviet military activities. In fact, actual defense outlays are believed to be about three times larger than the Soviets publicly admit. For example, CIA has estimated that actual Soviet 1975 defense expenditures--defined to accord with US budgetary accounts--were 50-55 billion rubles in 1970 prices, while the announced defense number came to 17.4 billion rubles in current prices. Under a broader definition--as the Soviets might account for their defense effort--CIA estimates Moscow's defense spending in 1975 to have been 55-60 billion rubles.

Soviet sources have never clearly defined what activities are included in the published defense budget. It is known that defense expenditures funded by the Ministry of Defense (MOD) are planned on the basis of the MOD estimate, or *Smeta*. Soviet financial writers describe the activities covered by the *Smeta* as including military pay and subsistence, outlays for operations and maintenance, military procurement, and military construction.¹ It is significant, however, that nowhere in the Soviet literature is the MOD "estimate" unequivocally linked to the "Defense" line of the state budget. Nor does the literature contain any quantification of the MOD "estimate."

The uncertainty surrounding the true coverage of the annually published data series has rendered them virtually useless as a barometer of the level of or the trend in total Soviet defense expenditures. As a result, Western analysts have had to devise alternative techniques to estimate such outlays. Uncovering the real basis, if any, for the Soviet announced defense budget would greatly assist in this effort.

New Insights

Several Soviet analyses of the financing of defense expenditures imply that the announced defense budget covers only the operating and maintenance outlays

1. See for example, A. M. Aleksandrov, ed., *Gosudarstvennyi byudzhnet SSSR*, 1965, pp. 382-383 and D.K. Allakhverdyan, et. al., *Finansy SSSR*, Moscow, 1962, p. 310.

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of the Soviet military establishment.² These probably include pay and allowances of military personnel, wages of civilian MOD employees, some current repair, food and nonfood quartermaster supplies, utilities, and the like. Expenditures for the procurement of weapons, construction of facilities, military space programs, R&D, and other defense activities presumably are hidden elsewhere in the state budget or financed from nonbudgetary sources.

In an analysis of state expenditures through 1951, V. P. D'yachenko contrasted the maintenance expenditures of the military with other outlays, such as those for construction of facilities and for materiel supply. He states, for example, "in the nonproductive sphere are carried out expenditures on defense and the ensuring of state security (the construction, maintenance and supplying of the Red Army, the Navy, the frontier guards, and the maintenance of the organs of Soviet intelligence)."³ The author provides a table on the 1949 state budget where *soderzhaniye vooruzhenikh sil*, the maintenance or upkeep of the armed forces, is substituted for the standard budget nomenclature for defense, *oborona*.⁴ The figure he gives for the "maintenance" of the armed forces is identical to the announced defense budget for that year.

D'yachenko does not explain his deviation from conventional Soviet phraseology on the defense budget. He may have intentionally used the concept of "maintenance" to distinguish operational from investment-type outlays. If so, then he is suggesting that the defense budget is an operating budget. This budget would understate total defense spending by the amount expended for military construction, procurement, and other nonoperational costs. On the other hand, D'yachenko could have loosely used the term "maintenance" to mean overall provisions for the military, as in "maintaining the military establishment." This concept would include both operating and investment-type expenses. In any event, the fact remains that D'yachenko's budget nomenclature is unprecedented, and for that reason its implications warrant further testing and evaluation.

2. V.P. D'yachenko, *Tovarno-denezhniye otnosheniya i finansy pri sotsializme*, Moscow, 1974, pp. 322-323, 326, 382. D'yachenko, a corresponding member of the Academy of Sciences, was head of the Department of Pricing at the Academy's Institute of Economics from 1953 until his death in 1971. The 1974 book is a collection of his writings, and was edited by the most prestigious names in Soviet finance, including A. M. Aleksandrov, D. K. Allakhverdyan, and M. S. Atlas.

L. Ya. Berri, ed., *Planirovaniye narodnogo khozyaistvo SSSR*, Moscow, 1973, pp. 451-453.

Support for this interpretation of defense budgets is also provided by an East European writer, Milan Spicak, in *V armade po unoru*, Prague, 1968, pp. 153-156.

3. D'yachenko, *op. cit.*, p. 326.

4. *Ibid.*, p. 382.

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The hypothesis that defense budgets in the early postwar years represented operating expenditures seems to be supported by [redacted] Czechoslovakia, whose financial system is patterned on the Soviet model. To a large extent Czechoslovakia's methods for financing (and concealing) defense outlays may reflect the prevailing Soviet practices. [redacted] weapons procurement and military construction in 1948-49 were financed from investment credits "camouflaged" in the nondefense portions of the state budget.⁵ If true, the announced defense budget was limited to operating and maintenance activities of the armed forces. The data [redacted] imply that total Czechoslovak defense expenditures for 1949 were funded 61 percent from the announced defense budget and 39 percent from other budget lines.

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Support for the hypothesis that the defense budget expenditures are limited to operations and maintenance costs also is found in a 1973 treatise on economic-financial planning by Soviet input-output specialist L. Ya. Berri. He presents a concept of state expenditures in which defense, *raskhodi na oboronu*, explicitly excludes all capital investment and capital repair. Other defense-related activities not included in this definition of defense were increases in state material reserves and social-cultural measures (such as science).⁶ While Berri does not define the "expenditures on defense," the clear inference is that they are limited to operational-type outlays. Although Berri's analysis includes nonbudget expenditures, he demonstrates that Soviet planners employ a concept of defense which excludes many of the costly investment-type activities associated with the total defense program. Moreover, this concept is given the same label used in the state budget.

Testing the Hypothesis

CIA independently estimates Soviet defense outlays using a building block approach, which applies prices to the physical components and activities which would be considered as defense related in the US. The resulting ruble expenditures can be aggregated by principal resource category--investment, operating, and R&D. There are some inherent uncertainties in the CIA estimates due to the lack of precise knowledge of some Soviet defense activities as well as possible variations in coverage resulting from differences in US and Soviet definitions.

CIA's estimates of Soviet operating expenditures can be compared with the defense budget announced by the Soviet Union to test the hypothesis that the

5. Spicak, *op. cit.*, p. 154.

6. Berri, *op. cit.*, p. 542.

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announced budget covers only the operating and maintenance expenditures of the military establishment. This comparison is shown below:

| | Published Defense Budget (Billion Current Rubles) | CIA Operating Cost Estimates ¹ (Billion 1970 Rubles) |
|------|--|--|
| 1960 | 9.3 | 9-10 |
| 1965 | 12.8 | 12-13 |
| 1970 | 17.9 | 15-16 |
| 1975 | 17.4 | 17-18 |
| 1976 | 17.4 | 18-19 |

1. Includes those activities which would be considered as operating expenditures in the US; pay, food, clothing and personal equipment expenditures for military personnel, MOD civilian wages, facility and equipment maintenance costs, POL, utility and transportation costs, and miscellaneous other maintenance costs.

At first blush the expenditure levels of the two series appear to be in the same general range. In fact, the figures are virtually equal in all years except 1970 and 1976. The trends in the two series however, are markedly different.

The two sets of data, nonetheless are not directly comparable because of the effects of inflation. Most Western analysts agree that there has been inflation in the Soviet Union. The pace of that inflation is difficult to measure because of the nature of the Soviet economy as well as the paucity of Soviet price data. Western studies generally place the rate of price increases in the Soviet Union in the range of 2 to 5 percent annually.⁷ Several Soviet economists have privately admitted to a 3- to 4-percent annual increase in prices.

The defense budget published by the Soviet government is expressed in current rubles, which includes the effect of price changes. The CIA estimates, on the other hand, are expressed in constant 1970 rubles, which removes the effects of price change. A strict comparison of the published data and the CIA estimates of operating expenditures requires that the Soviet numbers be adjusted for price changes.

We attempted to estimate the rate of inflation in Soviet defense expenditures by applying statistics on Soviet prices—official Soviet wholesale price indexes and



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wage data, supplemented with Western data on Soviet prices—to the relevant categories of the CIA estimate of Soviet military operating expenditures. An average annual rate of inflation of more than 1.5 percent between 1960 and 1976 was indicated by that exercise.⁸ Assuming an increase in Soviet prices of 2 percent annually, the following comparison results:

| | Soviet Defense Budget | | Billion |
|------|-------------------------------|--|--------------------------------|
| | Published (Current Rubles) | Adjusted ¹ (1970 Rubles) | CIA Estimates (1970 Rubles) |
| 1960 | 9.3 | 11.3 | 9-10 |
| 1965 | 12.8 | 14.1 | 12-13 |
| 1970 | 17.9 | 17.9 | 15-16 |
| 1975 | 17.4 | 15.8 | 17-18 |
| 1976 | 17.4 | 15.5 | 18-19 |

1. For 2-percent inflation.

With the adjustment for inflation, the Soviet published budget is higher than the CIA estimate through 1970 and lower than the CIA estimate after 1970. The CIA figure is 2-3 billion rubles lower than the published number in 1970, the only directly comparable year. Also, the CIA data indicate that Soviet military operating costs have been increasing annually since 1960. The Soviet figures, on the other hand, show such costs rising prior to 1970 but falling thereafter.

Admittedly, there is some uncertainty built into the CIA estimates—they should be regarded as general orders of magnitude rather than point estimates.

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8. Two serious problems raise questions as to the reliability of this test. First, Western analysts generally question the meaningfulness of Soviet price indexes (see, for example, Vladimir Treml and John Hardt (eds) *Soviet Economic Statistics*, Durham, N.C., 1972, p. 103-106.) Second, insufficient information exists to judge whether wholesale price indexes approximate price changes faced by the military. With these uncertainties, our notional judgment is that an arbitrarily assumed rate of inflation of 2 percent is roughly appropriate.

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[redacted] It is unlikely, for example, that Soviet operating costs could be falling in the 1970s as suggested in the Soviet data. Soviet military manpower levels have increased over this period by about 370,000 men, there have been several military pay increases, and operations and maintenance costs have undoubtedly risen due to the increased complexity of Soviet weapons.

Conclusions

On balance, the hypothesis that the USSR's announced defense budget is an operating budget cannot be confirmed on the basis of information currently available to Western observers; neither the magnitudes nor the trends in the Soviet data mesh with CIA estimates of Soviet operating costs. Nevertheless, we cannot rule out a real basis for the Soviet data. Rather, several plausible alternative interpretations of the hypothesis can be made. For example, it is possible that the defense budget may consist solely of operating expenditures, but it may not include all such expenditures because of Soviet accounting practices. Alternatively, the Soviet definition of operating expenditures may change over time. It is also possible that, definitional differences aside, the budget may be manipulated for political purposes. For example, some operating expenditures may have been added to the defense budget in the second half of the 1960s to counter the rapid expansion in US defense budgets. Similarly, some operating expenditures may have been shifted from the defense budget to other budget lines in the 1970s to signal Soviet attitudes about detente.

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