

ECONOMIC INTELLIGENCE REPORT

ECONOMIC RELATIONS
BETWEEN COMMUNIST CHINA
AND THE EUROPEAN SATELLITES
1950-58



CIA/RR 59-29
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CENTRAL INTELLIGENCE AGENCY
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FOREWORD

This report has been reviewed and approved by the Subcommittee on International Trade and Finance of the Economic Intelligence Committee (EIC). The Subcommittee consists of representatives of the Departments of State, Commerce, Treasury, Navy, Army, and the Air Force; the Office of the Secretary of Defense; the Federal Reserve Board; and CIA. The Subcommittee considers that this report fills a priority deficiency in economic intelligence research as identified by the EIC.

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ECONOMIC RELATIONS BETWEEN COMMUNIST CHINA
AND THE EUROPEAN SATELLITES*
1950-58

Summary and Conclusions

Since 1950, Eastern European countries with which Communist China historically has had virtually no economic contact have assumed considerable importance in China's economic relations. This change has taken place largely because of the ideological affinity between the leaders of the European Satellites** and those of China. A rational economic basis for trade between the relatively underdeveloped economy of China and the industrialized economies of Eastern Europe also exists. The magnitude of such trade and the breadth of the economic contacts, however, are clear indications of a calculated policy of promoting Soviet Bloc unity by economic means. Furthermore, the unique position that China occupies in the Communist world, a position much more independent of Moscow than is that of the Satellites, has enabled China to give particular support to efforts for unification within the Bloc.

The primary economic link between Communist China and the Satellites is foreign trade, based on a mutually advantageous exchange of Chinese raw materials and foodstuffs for Satellite industrial products. The level of Sino-Satellite trade rose from \$20 million*** in 1950 to \$655 million in 1958. The rate of growth of this trade since 1952 has been about 13 percent annually, about the same as that of China's total foreign trade, and the relative importance of Sino-Satellite trade has consequently remained fairly stable at about one-sixth of China's total foreign trade.

Through 1953, Communist China had a substantial export surplus in trade and consequently accumulated credit balances of nearly \$100 million in its financial account with the Satellites. Beginning in 1954,

* The estimates and conclusions in this report represent the best judgment of this Office as of 1 June 1959.

** The terms European Satellites and Satellites in this report refer to the Communist-controlled countries of Eastern Europe, as follows: East Germany, Czechoslovakia, Poland, Hungary, Rumania, Bulgaria, and Albania.

*** Unless otherwise specified, all dollar values in this report are in terms of current US dollars.

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China has had debit balances in the clearing accounts that have offset the credit balances of previous years. For the period 1951-57 as a whole, Sino-Satellite clearing accounts were approximately in balance. Future imbalances are expected to be small.

Mutual trade provides both Communist China and the European Satellites with the types of commodities that are required by their economies. The complementary basis of this trade is illustrated by the fact that about 60 percent of Sino-Satellite trade has been between China and East Germany and Czechoslovakia, the two most industrialized Satellite countries. Complete industrial installations currently account for more than one-third of China's imports from the Satellites, and their proportion is increasing yearly. During China's First Five Year Plan (1953-57) the Satellites supplied the equipment for 64 projects that were under construction. By the end of 1957, 27 of the projects were completed and at least in partial operation. Some of the more important completed plants supplied by the Satellites included 18 thermal electric power stations and a large telecommunications complex.

Communist China's exports to the Satellites have been almost wholly raw materials and foodstuffs. Vegetable oils, oilseeds, and mineral and chemical products have been major specific export items. China's exports have added notably to the available raw materials and foodstuffs in the European Satellites, all of which have experienced chronic shortages of these goods. The Satellites, however, have frequently taken advantage of the ready market in Western Europe for many Chinese products to resell Chinese exports in order to obtain foreign exchange to purchase non-Communist goods. Satellite reexports of Chinese products have been significant since the beginning of the Sino-Satellite trade and in some years may have been as high as \$50 million. There are indications, however, that Chinese exports of the type usually reexported by the Satellites have been declining since 1957, and thus Satellite reexports may have diminishing significance.

A number of additional economic relationships with the Satellites link Communist China to the Soviet Bloc. For some time, China has been a member of intra-Bloc economic organizations such as the administrative agency for the Bloc agreement on railroads. A joint Sino-Polish shipping organization (Chipolbrok -- Chinese-Polish Shipbrokers, Ltd.) was formed in 1951 to facilitate the movement of goods between China and the Satellites. The majority of the vessels identified with the company in 1956 and 1957 appear to have been contributed by the Chinese, and China probably has earned a small amount of foreign exchange through the company's operations.

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Communist China has established Western currency accounts in Satellite banks. Originally, these were established to avoid the blocking of Chinese accounts by Free World governments. Although China no longer fears the seizure of funds held in Western banks, it has opened additional Western currency accounts and has broadened its use of the international services of Satellite banks. The Bank of China also has acted on a small scale as a short-term financier for some of the European Satellites' imports of Western goods.

Although limiting its official position to observer status, Communist China has actively participated in those activities of the Council for Mutual Economic Assistance (CEMA) which have coincided with China's interests to such an extent that the Chinese have claimed that their economic cooperation with member countries is as great as that among the members themselves. Those CEMA activities in which China has not participated have involved projects of no direct concern to the Chinese; such as the oil pipeline to be built between the USSR and the European Satellites or problems connected with Eastern European economic integration and specialization. Given the present state of economic development in China, industrial specialization and integration with Eastern Europe is not a matter with which the Chinese can be seriously involved. Furthermore, in view of the size and natural endowments of China, which make feasible its expressed intention of achieving industrial self-sufficiency, China is not likely to participate in the industrial integration programs of CEMA in the foreseeable future.

Sino-Satellite economic relations have reflected Communist China's policy of supporting Sino-Soviet Bloc unity as forcefully as its limited resources and its other national goals would permit. Following the uprisings in East Germany, Poland, and Hungary, China provided these countries with advance deliveries and additional quantities of raw materials and foodstuffs. In addition, China offered Hungary grants and credits amounting to \$57.5 million and agreed to pay Poland in Western currency for some Polish exports to alleviate Poland's critical shortage of foreign exchange. Although this Chinese assistance has not been large, it has entailed the subordination of other Chinese interests.

The economic relations between China and the European Satellites have been mutually advantageous, and trade between the two areas probably will continue to expand, although the Satellite share in the total trade of China probably will not increase. Both China and the Satellites appear to be equally interested in the further development of their relations and in the benefits to be derived; hence the permanence in scope and scale of the relationships that have been established seems assured.

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I. Introduction

In the decade since the Communist victory in the Chinese civil war the foreign relations and economic policy of China have been oriented primarily toward the Soviet Bloc. China's approach to foreign relations has been dominated by the belief that its armed forces should be supported by a close political and economic alliance with other Communist nations and that its role in world affairs should be strengthened by rapid industrialization. China's entrance into the Korean War destroyed whatever chance existed that it would receive assistance in industrializing from Western capitalist countries and at the same time strengthened the conviction of the Communist Party hierarchy that its interest lay in expanding economic relations with other Communist countries. China has formed strong economic bonds with the USSR and the European Satellites in order not only to buttress its own ideological ties with the Communist orbit but also to strengthen those existing among other members as well. Adoption of an economic policy in which rapid industrialization and military preparedness have been given the highest priority has led inexorably to initial reliance on Bloc sources of supply for large amounts of military goods, capital equipment, and other industrial items. Bloc markets in turn have become the major foreign outlets for the products of China.

The wide variety of Sino-Satellite relationships in the fields of foreign trade, transportation, finance, technology, planning, and economic policy reflects the development of this interdependence. This report is an analysis of the more important of these relationships. It shows that in several instances and in a number of ways Communist China has been willing to sacrifice its own economic interests in dealing with the European Satellites in order to further the strength and cohesiveness of the Sino-Soviet Bloc as a unit.

II. Level and Balance of Trade

The primary link between Communist China and Eastern Europe is commodity trade based upon the exchange of Chinese raw materials and foodstuffs for Satellite industrial products, an essentially complementary trade. With the consolidation of Communist power in Eastern Europe and China, a dramatic increase in trade between China and the Satellites has occurred, rising from a level of \$20 million in 1950 to \$655 million in 1958. The Satellites as a result have accounted for about 17 percent of the total foreign trade of China in recent years.

Both Communist China and the European Satellites have followed policies of orienting their foreign trade toward the rest of the Sino-Soviet Bloc. Although the expansion of Sino-Satellite trade has buttressed intra-Bloc political relations, it also has served as a highly

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satisfactory approach to key economic problems in both China and the European Satellites. The trade potential between the two areas was considerably improved by the economic policies and particularly by the investments in heavy industry which followed the installation of Communist governments in the countries of Eastern Europe and in China. Thus many of the import requirements for machinery and equipment for the industrialization program of China have been supplied by the Satellites. The Satellites, on the other hand, have been able to sell to China industrial products which have been difficult to dispose of in other markets. Goods which were relatively unmarketable within Eastern Europe because of the similarity in the development programs of the Satellites or in Western countries because of the high costs of production and the less advanced designs have been marketed in China. The goods received in exchange from China have supplied a significant proportion of Satellite import requirements for consumer foodstuffs and industrial raw materials.

A. Level of Trade, 1950-58

The reorientation of Chinese trade toward the Soviet Bloc moved rapidly during the first 2 years following the consolidation of Communist power in China. The accompanying chart, Figure 1, shows the geographic distribution of China's foreign trade in 1950 and 1958. By

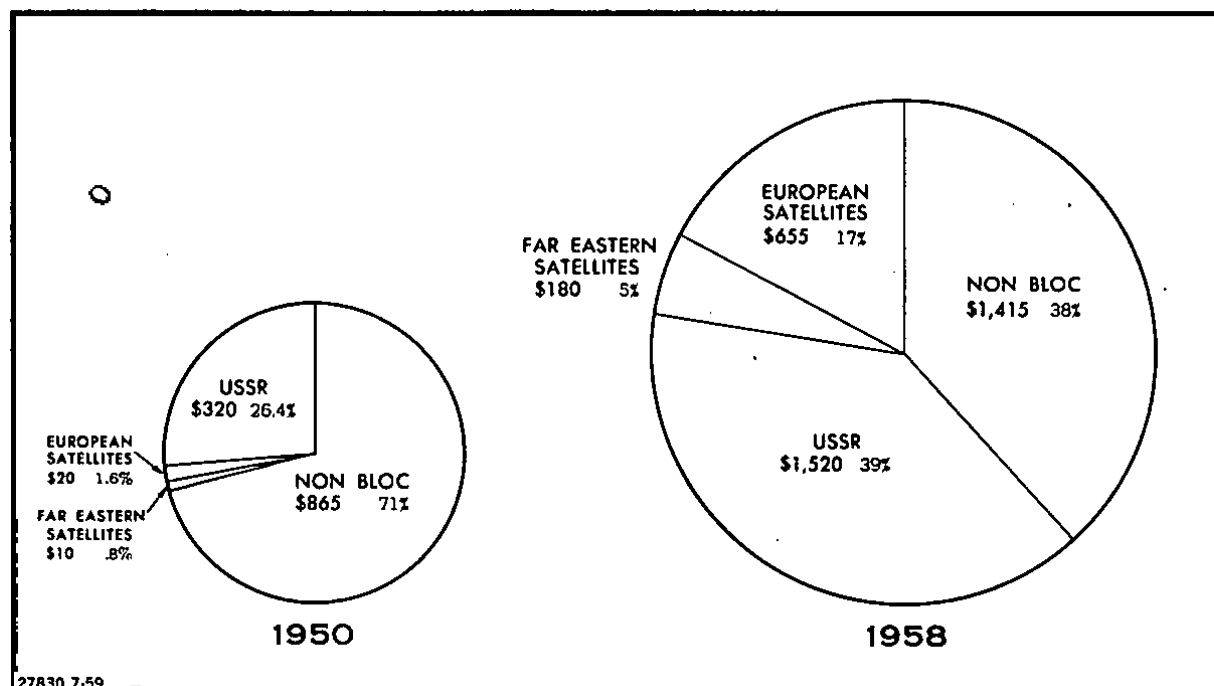


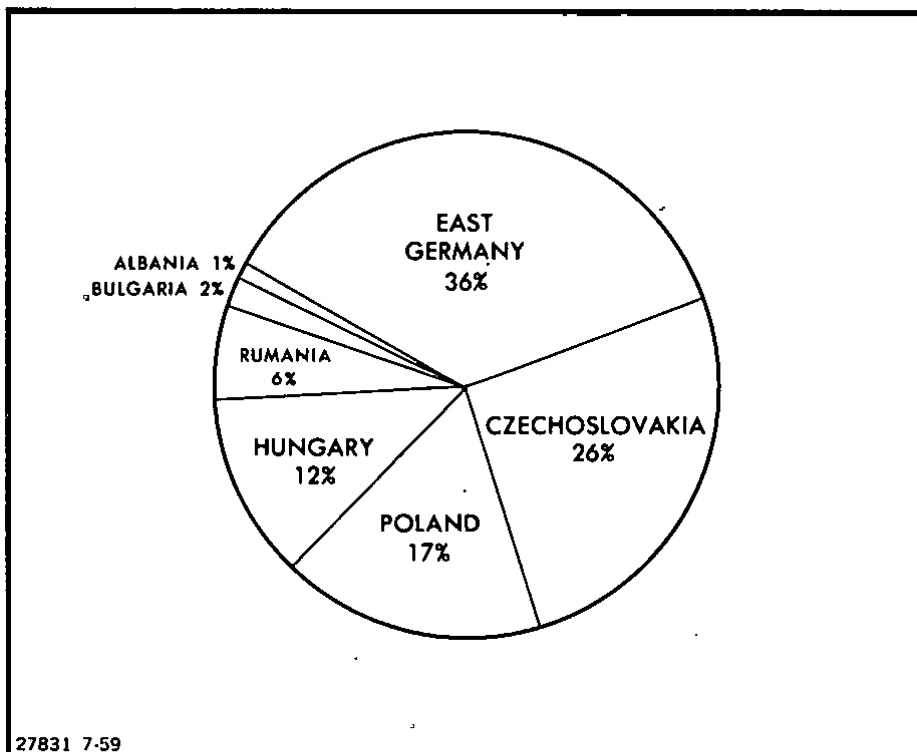
Figure 1. Communist China: Geographic distribution of foreign trade, by percentage and by dollar value, 1950 and 1958.

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1952, Chinese trade with the European Satellites had increased to 16 times the level of 1950 (see Table 1*). Since then, Sino-Satellite trade has continued to grow but at a more modest pace, averaging about 13 percent per year between 1952 and 1957. The rate of growth of Chinese trade with the European Satellites since 1952 has been nearly the same as the rate of growth of China's total foreign trade. Hence the relative importance of Sino-Satellite trade has remained comparatively stable, averaging about one-sixth of the total trade of China.

Communist China's trade with the individual countries of Eastern Europe has been directed primarily toward the more mature industrial nations (see Table 2** and the accompanying chart, Figure 2, for the estimated distribution of this trade in 1956). Thus East



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Figure 2. Communist China: Percentage distribution of trade with European Satellites, by country, 1956.

Germany and Czechoslovakia alone accounted for about 60 percent of Sino-Satellite trade. The order of importance of the individual Satellites remained stable between 1951 and 1957, with only minor changes. Czechoslovakia, for example, had a larger share of Sino-Satellite trade in earlier years than in more recent years.

* Table 1 follows on p. 7.

** Table 2 follows on p. 8.

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Table 1
Foreign Trade of Communist China a/
1950-58

	Million Current US \$								
Area	1950	1951	1952	1953	1954	1955	1956	1957	1958
With the Free World	<u>865</u>	<u>920</u>	<u>580</u>	<u>750</u>	<u>625</u>	<u>800</u>	<u>1,090</u>	<u>1,135</u>	<u>1,415</u>
With the Sino-Soviet Bloc b/									
USSR	320	750	965	1,170	1,275	1,705	1,460	1,290	1,520
European Satellites	20	205	320	345	375	430	465	490	655
Far Eastern Satellites	5	20	30	50	90	125	120	145	180
Subtotal	<u>350</u>	<u>970</u>	<u>1,315</u>	<u>1,565</u>	<u>1,740</u>	<u>2,265</u>	<u>2,045</u>	<u>1,925</u>	<u>2,350</u>
Total trade	<u>1,215</u>	<u>1,890</u>	<u>1,895</u>	<u>2,315</u>	<u>2,365</u>	<u>3,065</u>	<u>3,135</u>	<u>3,060</u>	<u>3,765</u>

a. Estimates are based on data available through May 1959. Dollar values in the table have been converted from yuan values derived from Chinese Communist announcements. Conversion from yuan to dollars was made at 2.46 yuan per dollar for non-Bloc trade and 4 yuan per dollar for Bloc trade (see Appendix A, Part 1). Statistics published by the European Satellites on their trade with China (nearly complete data are available for 1953-56) show a somewhat higher level of total Sino-Satellite trade than is shown in this table. There is no adequate explanation for the continual and rather stable discrepancy in the same direction, but this difference has not been greater than 10 percent.

b. All data are rounded to the nearest number divisible by five. Totals are derived from unrounded data and may not agree with the sum of their rounded components.

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Table 2

Trade of Communist China
with the European Satellites, by Country a/
1956

<u>Country</u>	<u>Value (Million US \$)</u>	<u>Percent</u>
East Germany	167	36
Czechoslovakia	121	26
Poland	79	17
Hungary	56	12
Rumania	28	6
Bulgaria	9	2
Albania	5	1
Total	<u>465</u>	<u>100</u>

a. The percentages have been derived from the relationship of figures published by each Satellite on its trade with China to the sum of the published figures for all the Satellites. Sino-Albanian trade, for which no official data are available, has been estimated to be \$5 million, or 1 percent of total Sino-Satellite trade. Because the Satellite figures on Sino-Satellite trade are somewhat higher than the Chinese yuan values converted to dollars, the percentages have been applied to the 1956 dollar values shown in Table 1 (p. 7, above). Therefore the values in Table 2 are slightly lower than the figures published by the Satellites.

The growth of Sino-Satellite trade has been based on yearly negotiations. Trade agreements were signed with the four major Satellite countries -- Czechoslovakia, East Germany, Poland, and Hungary -- in 1950 and with Rumania and Bulgaria in 1952. Sino-Albanian trade was initiated in 1955 under a trade and long-term credit agreement. A number of European Satellites have negotiated long-term trade agreements with Communist China, beginning in 1956, when Czechoslovakia and probably East Germany signed such pacts. In 1957-58, China negotiated similar agreements with all the other European Satellites. The long-term agreements provide a framework within which annual pacts are negotiated specifying types, volumes, and prices of goods to be traded.

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(See III, B,* for a further discussion of the development of long-term trade agreements.)

B. Commercial and Settlement Transactions

Most Sino-Satellite commodity transactions and payments for services are financed through bilateral clearing accounts.** Both payments and receipts are entered by both trading partners into the appropriate clearing accounts, and the difference between payments and receipts is computed periodically. Differences that exist (net balances) may be settled by transfers of gold or acceptable foreign exchange, or they may be carried over for future settlement in commodities. When net balances are carried over, they are in effect advances of credit, which, when unplanned or persistent, may represent potential sources of friction.

1. Bilateral Clearing Accounts

Annual trade balances between Communist China and the European Satellites have been subject to rather wide swings since 1950. Through 1953, Communist China accumulated substantial credit balances in its clearing accounts -- balances which resulted largely from the failure of the Satellites to fulfill export contracts on schedule. Since 1954, however, China has had debit balances with almost all of the Satellites and an aggregate debit balance for each year. For the period 1951-57 as a whole, however, Sino-Satellite clearing accounts were approximately in balance (see Table 3***).

A high level of trade between China on the one hand and Czechoslovakia, East Germany, Hungary, and Poland on the other -- probably involving a Chinese import surplus -- was planned in trade agreements for 1951. The Sino - East German trade agreement, for example, called for China to import goods valued at \$130 million and to export

* P. 13, below.

** Sino-Satellite clearing procedures distinguish between "commercial" and "noncommercial" transactions. Payments on commercial accounts include both goods transactions and probably such noncommodity transactions as the services of technicians, ship repairs, and possibly some freight services. The noncommercial accounts appear to be used for remitting funds to fellow nationals (such as personnel in embassies and delegations) for services obtained within another country (such as rent, food, and utilities). The principal items excluded from the Sino-Satellite bilateral clearing processes appear to have been Satellite purchases of Western goods for China and probably most shipping transactions.

*** Table 3 follows on p. 10.

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Table 3

Estimated Balances on Clearing Accounts
Between Communist China and the European Satellites
1951-57

<u>Year</u>	<u>Million US \$</u> <u>Estimated</u> <u>Clearing</u> <u>Balance a/</u>
1951	80
1952	10
1953	10
1954	-50
1955	-5
1956	-20
1957	-30
Net total	-5

a. A positive figure denotes an excess and a negative figure a deficiency of Chinese earnings (primarily from exports and other monetary receipts) over payments (primarily for imports and other monetary remittances). The net balances are estimates based largely upon reported trade. See Appendix A, Part 2, for sources and methodology. All data are rounded to the nearest number divisible by five.

goods valued at \$98 million, with the difference probably to be settled by China in a convertible currency. 1/* Actual Sino - East German trade, however, fell considerably below the targets, and China developed an export surplus. China's exports to East Germany in 1951 were \$62 million, somewhat below the planned goal, but its imports from East Germany were only about \$22 million, far less than the planned level.** The imbalance would have been even larger if China had not canceled several export contracts. 2/ China similarly had a \$40 million surplus in its clearing account with Czechoslovakia and a similar but much smaller surplus with Hungary. The unexpected

*** [redacted] see Appendix A, Part 2,
for [redacted] methodology concerning clearing balances.

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failure of the Satellites to meet their export commitments thus forced China into a position of creditor on clearing accounts for about \$80 million in 1951.

Communist China continued to accumulate surpluses in its clearing accounts with the Satellites through 1952 and 1953, although the imbalances were much smaller than in 1951. Greatly increased Czechoslovak exports were largely responsible for limiting the Sino-Satellite imbalance to a total of \$20 million for the 2-year period 1952-53. Although China had deficits in its trade with Czechoslovakia probably amounting to about \$30 million during the 2 years, its clearing account surpluses with the other Satellites persisted. Thus the Sino-East German imbalance increased by about \$30 million in the 2-year period 1952-53, and the Sino-Polish and Sino-Hungarian imbalances amounted to about \$10 million each during the same period. The inability of the Satellites to meet their export commitments was clearly a major restricting factor on the development of Sino-Satellite trade during the first few years.

Satellite exports to Communist China, however, were rising continuously and, inasmuch as Chinese exports to the Satellites were relatively constant, China's surplus on clearing accounts declined yearly. By 1954, China's imports from the Satellites considerably exceeded its exports to these countries, and consequently China had a clearing account deficit estimated to be about \$50 million. Debit balances, although of smaller magnitude, have continued since 1954.

The Sino-Satellite clearing balance in 1958 and subsequent years is expected to be small. Planning under recent Sino-Satellite trade agreements has aimed at balanced trade, as illustrated in the Chinese efforts in 1957 to reduce imports to the level of exports. Improved planning and contracting procedures, particularly under long-term trade agreements, and increased ability of the Satellites to meet export commitments indicate that imbalances on current account in the future also will be small.

2. Settlement Transactions

Balances in Sino-Satellite clearing accounts are generally carried over for settlement by the shipment of goods in subsequent years rather than by net currency or gold flows as an imbalance develops. Thus the surpluses of Communist China during the first 3 years of formalized Sino-Satellite trade represented a cumulative credit to the Satellites totaling nearly \$100 million which the Chinese neither anticipated nor desired. On the contrary, it was probably planned in each year that the accumulated clearing account surplus would be eliminated. The fact that China's surplus in clearing accounts continued to accumulate

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appears to be indicative of a series of serious planning failures in the European Satellites.

Satellite exports were not sufficiently large to begin repayment of clearing credits until 1954, although Chinese Communist exports remained at about the same level from 1952 through 1954. By the end of 1957 the cumulative imbalances of the clearing accounts had been eliminated.

The development of the large clearing imbalances in the first years of Sino-Satellite trade suggests that limitations, such as swing limits, were not applied. Settlement of clearing imbalances in hard currency probably was provided for in the Sino-Satellite trade agreements, but it has not been used, probably because of the shortage of Western foreign exchange reserves in Satellite countries and the preference of Bloc countries to settle imbalances with merchandise shipments rather than with gold or transfers of foreign exchange. Minor shipments of gold and precious metals have been treated in Sino-Satellite trade as commodity transactions rather than as financial settlements.

Payments on some Sino-Satellite transactions, however, have involved transfers of Western currencies. Some of these transactions have been within the framework of the clearing procedures and therefore have been included in the estimate of the balance of the clearing accounts. The major Western currency transactions, however, probably have been outside of Sino-Satellite clearing procedures and have involved the purchase of Western goods by Satellite firms for delivery to China. It is estimated that 10 to 15 percent of the Western goods entering China by way of the European Satellites during 1951-57 were purchased by Satellite firms. Thus China probably transferred about \$40 million to \$50 million in convertible currency to the Satellites in payment for Western goods.

III. Factors Influencing the Level and Balance of Trade

A. Pricing Practices

The pricing procedures employed in Sino-Satellite trade have generally involved negotiating individual prices, using world market quotations during a base period as the point of reference. A typical Chinese Communist agreement with a Satellite country, for example, calls for the trading firms of the two countries to negotiate a ruble price based on the average world market price in the principal market for each article, generally during the 12 months preceding the beginning of negotiations for the trade agreement. In determining the average world market price for each commodity, quotations must be supported

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by specific types of representative documents, and apparently data from trade journals may be used only for information purposes. Each side probably submits price documentation favorable to itself, and thus a crucial point in the negotiations probably consists of the scrutiny and selection of agreed documentation. The agreed-on world market price for the article is converted into rubles on the basis of the appropriate exchange rate quoted by the Soviet State Bank for the pertinent time period. Occasionally, deliveries are necessary before final prices have been determined, and in such cases a provisional price, such as the previous year's price, is agreed to for accounting purposes until the final price is negotiated.

Neither party -- Communist China or the Satellites -- appears to derive any special advantage from the negotiated prices of Sino-Satellite trade. Prices for individual commodities may seem out of line, but the price distortions are not in one direction and are claimed to balance out in the aggregate. For example, China pays excessive prices for one or several types of imported items, but it also pays below-world-market prices for other types of imports or charges above-world-market prices for some of its exports. ^{3/} Satellite trade representatives in China have acknowledged the keen awareness of market conditions which the Chinese have shown in price negotiations.

B. Long-Term Trade Agreements

A major factor that has restricted the development of Sino-Satellite trade has been the failure of the Satellites to meet their export commitments. The Satellites have been consistently late in meeting contractual delivery dates and also were unable to export the full amount of their yearly quotas between 1951 and 1953. This failure in turn has resulted partly from Communist China's slowness in drafting its long-term import requirements. Moreover, the Chinese have changed specifications on a number of orders, prolonging manufacturing periods beyond the scheduled delivery dates.

As early as 1950 and 1951, some Satellites wanted long-term trade agreements in order better to incorporate Chinese Communist requirements into their production plans, but, until 1956, Chinese requirements were probably provided only on an annual basis. In late 1955, China and the Satellite countries began discussing long-range requirements, and in mid-1956 the first long-term trade agreements were signed with Czechoslovakia and probably with East Germany. ^{4/} The unrest in the Satellites and the Chinese review of their development program probably caused the postponement of long-term trade agreements with the remaining Satellites until late 1957 and early 1958. ^{5/}

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The long-term agreements should largely overcome the past problems of incorporating Chinese Communist orders into Satellite production plans on short notice. These agreements should also permit the investment in Satellite production facilities necessary to handle Chinese orders in an orderly fashion. The long-term trade agreements constitute a strong link between the economies of China and the European Satellites, and as such represent a major step toward consolidating China's relations with the Communist Bloc.

C. Economic Support for Eastern Europe

Communist China on several occasions has provided emergency economic support to the European Satellites, in particular to those experiencing economic problems associated with domestic political difficulties. The Chinese aid programs to the Communist countries of Asia and the Chinese participation in the Bloc economic programs in the underdeveloped nations of the Free World are well known and outside the scope of this report. Chinese assistance to the European Satellites is less well known, partly because of its small scale and partly because it frequently has been given in forms other than identifiable grants or credits.

All three instances of major unrest in the Satellites prompted Communist China to offer economic assistance to help alleviate the economic difficulties that had played an important role in the developing crises. After the June 1953 riots in East Germany, China agreed to ship additional foodstuffs worth about \$13 million, although the Chinese clearing credit to East Germany amounted to more than \$60 million at the time. 6/ The Chinese agreed after the Polish uprising in 1956 to pay for Polish iron and steel products in Western currency in order to alleviate the shortage of foreign exchange in Poland, a policy which was probably continued in 1957. 7/ While China was providing Poland with Western exchange, the Chinese were limiting their purchases of Western goods because of a shortage of such currencies. Thus the help China gave to Poland entailed some sacrifice of its own economic interests. Furthermore, the unusual 50-percent increase envisaged for 1958 in Sino-Polish trade contracts involved acceptance by China of several Polish exports, which it previously had been reluctant to purchase, and provision to Poland of a larger volume of Chinese raw materials and foodstuffs.

Chinese Communist aid to Hungary after the revolt in 1956 was the largest extended to a European Satellite. China provided an initial \$7.5 million gift early in November 1956. In January 1957 the Chinese announced the offer of a \$50 million long-term credit to Hungary, consisting of \$25 million in commodities and \$25 million in Western exchange. 8/ The foreign exchange credit of \$25 million was formalized

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in an agreement in May 1957. 9/ This credit, too, was made at a time when China was limiting its imports from Western countries because of a shortage of foreign exchange. China also responded to Hungarian requests to assist industrial recovery by providing additional goods and by making deliveries ahead of schedule.

Credits and grants have been a basic part of Communist China's relations with Albania since the first economic agreements were signed in October 1954. The value of these credits and grants is not known but is believed to be small. More recently, however, China has granted a \$14 million long-term loan for the period 1961-65. Albania will use the loan to purchase from China equipment for a cotton mill, a flax mill, and a glassworks and for other Chinese commodities. Albania is to repay the loan with commodities between 1981 and 1990.

In indirect ways the Chinese Communists have aided many Satellite countries in coping with shortages of Western currencies. China has imported Asian rubber, principally from Ceylon, and has reexported part of it to several Satellite countries. China probably followed a similar policy with respect to Canadian wheat and Egyptian cotton. China used Western currencies (although sometimes in a limited form, as in the Sino-Ceylonese rubber-rice agreement) to obtain the goods and probably received clearing rubles from the Satellites for the re-exports. This Chinese practice contrasts sharply with the Satellite policy which requires China to remit the necessary Western exchange when the Satellite countries purchase Western goods for China. Moreover, Communist China has continued to permit the Satellites to resell its products in Western Europe, although the Satellite marketing procedures have made it more difficult for China to market its own products in the area.

IV. Commodity Trade

A. Chinese Communist Exports

Agricultural products dominate the exports of Communist China, amounting to about 75 percent of total exports in value, and minerals and metal products constitute most of the remainder. The composition of Chinese exports to the European Satellites approximates this pattern.

Seaborne cargo data appear to provide nearly complete information concerning the volume of Chinese Communist exports to the Satellites. Table 4* presents tonnage estimates and the accompanying chart, Figure 3,** presents estimates by tonnage and by value for Chinese

* Table 4 follows on p. 17.

** Figure 3 follows on p. 16.

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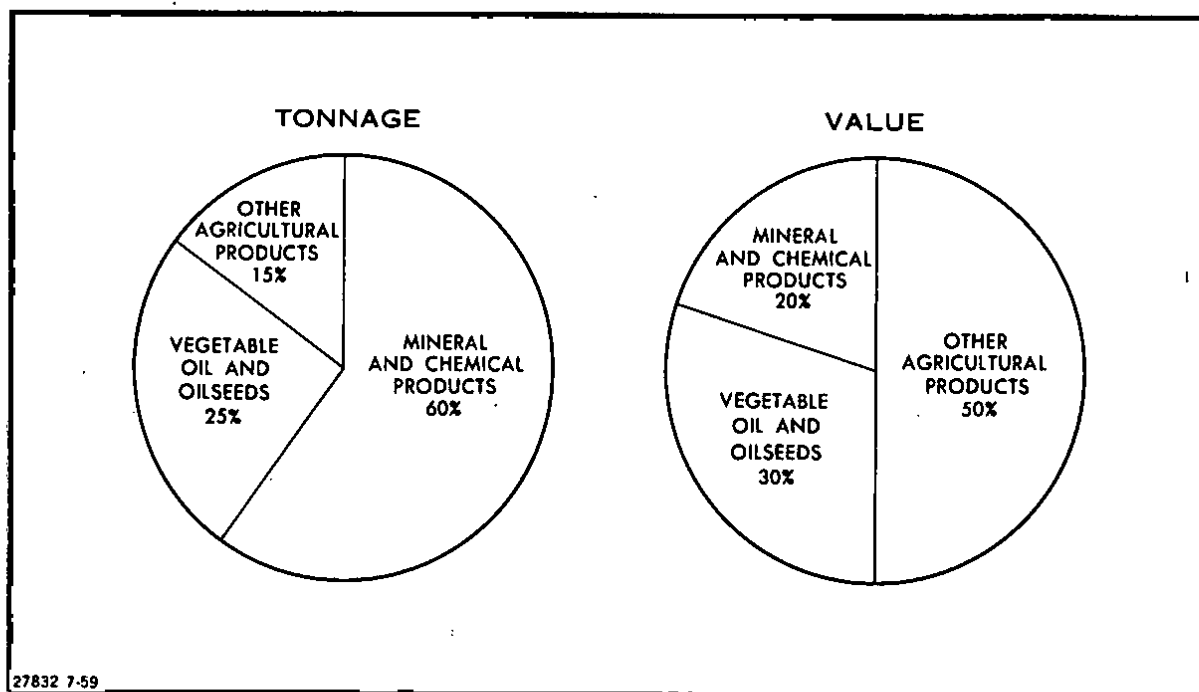


Figure 3. Communist China: Estimated seaborne exports to the European Satellites, by tonnage and by value, 1956.

exports to the Satellites in 1956 for important commodities. Chemical and mineral products -- predominantly iron ore -- amounted to about three-fifths of the total tonnage, but their value is believed to be about one-fifth of the total value of Chinese exports to the Satellites. Oilseeds and vegetable oils constituted about one-fourth of the tonnage, with soybean exports the most important. The value of these oilseeds and vegetable oils probably amounted to about one-third of the total value of Chinese exports to the Satellites. The remaining 15 percent of the tonnage was made up of a wide range of other agricultural commodities such as meats, bristles, hog-casings, feathers, and eggs. Because of the very high unit price of these commodities, it is believed that they constituted nearly one-half of the value of Chinese exports to Eastern Europe.

Communist China's exports to the European Satellites appear to include some reexported Free World goods such as cotton, wheat, and rubber. The latter, however, is the only commodity that has been consistently reexported. A significant portion of Chinese exports to the Satellites is resold by the Satellites, primarily to Western Europe, to alleviate the chronic shortage of Western currencies held by the European Satellites (see VI*).

* P. 25, below.

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Table 4

Estimated Seaborne Exports
from Communist China to the European Satellites a/
1956

Thousand Metric Tons	
Commodities	Estimated Volume <u>b/</u>
Iron ore	483
Pig iron	50
Other minerals and chemicals	32
Soybeans	225
Peanuts	78
Vegetable oils and other oilseeds	35
Meat	33
Rice	36
Other agricultural products	76
Unidentified <u>c/</u>	262
Total	<u>1,310</u>

a. 10/

b. Tonnage is estimated from cargo data and probably includes nearly all reexports.

c. The bulk of the unidentified cargo probably was iron ore. For the estimates in the text (see p. 16), 200,000 tons of the unidentified cargo were assumed to be iron ore.

A recent interesting development is the emerging Chinese Communist capability to export industrial goods. Under its 1958 trade agreements, China has contracted to supply to Eastern Europe a number of industrial commodities that formerly had been imported in sizable quantities from the European Satellites. The new Chinese exports include tires, electronic parts, machine tools, textile machinery, and other industrial products. Exports of these new commodities, however, are still small in value, and agricultural products may be expected to continue to dominate Chinese exports to the Satellites for several years.

B. Chinese Communist Imports

Chinese Communist imports from the European Satellites have been predominantly industrial products, in particular machinery and

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equipment. Reports indicate that imports from the Satellites have consisted of about 75 percent investment goods, 13 percent raw materials, and 12 percent consumer goods. Approximately 70 percent of the investment goods, or more than one-half of total imports, have consisted of machinery and equipment, such as machine tools, motors, vehicles, and construction equipment. ^{11/} The composition of imports appears to have remained essentially unchanged in recent years, with perhaps a slight decline in imports of consumer goods and raw materials and a corresponding increase in investment goods as Satellite exports of complete installations* have assumed greater importance. The pattern of Chinese imports from the Satellites during 1952-58 is shown in the accompanying chart, Figure 4.

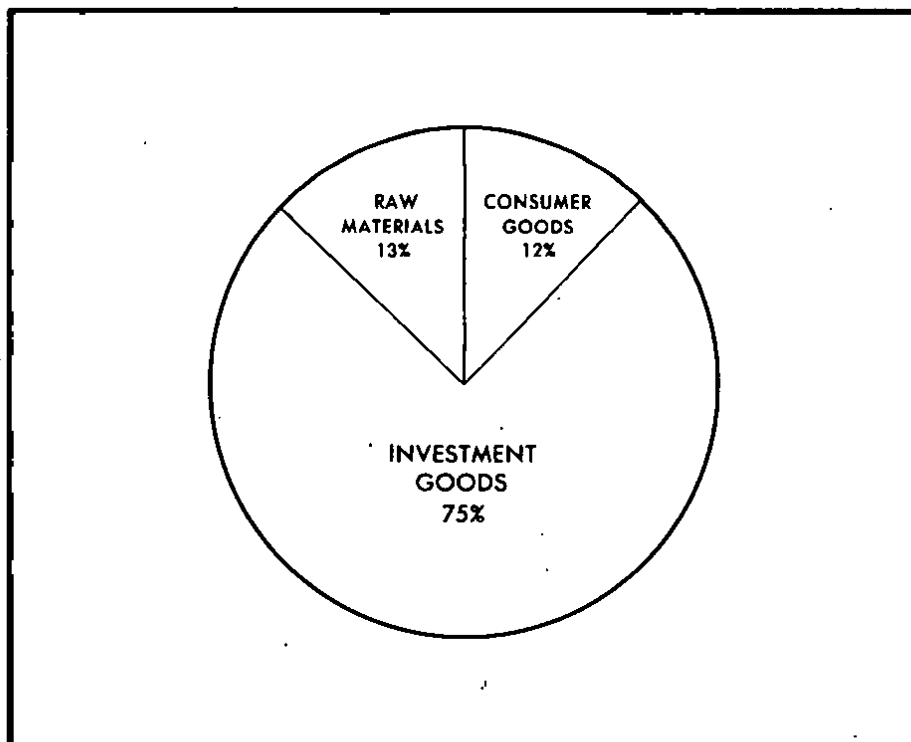


Figure 4. Communist China: Estimated pattern of imports from the European Satellites, by major commodity groups, 1952-58.

The principal consumer goods imported by Communist China from the Satellites have been kerosine, pharmaceuticals, sugar, and textiles. Imports of raw materials have consisted largely of petroleum products, chemicals, dyes, fertilizers, and newsprint. Imports of investment goods have included many types of machinery and equipment and various ferrous and nonferrous metal products. Since 1955, complete installations have probably accounted for more than 30 percent of total imports from the Satellites and imports of transportation and agricultural equipment for at least another 20 percent.

* For a definition of the term complete installations, see the footnote, p. 21, below.

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Detailed commodity statistics for Chinese Communist imports from East Germany (see Table 5* and the accompanying chart, Figure 5)

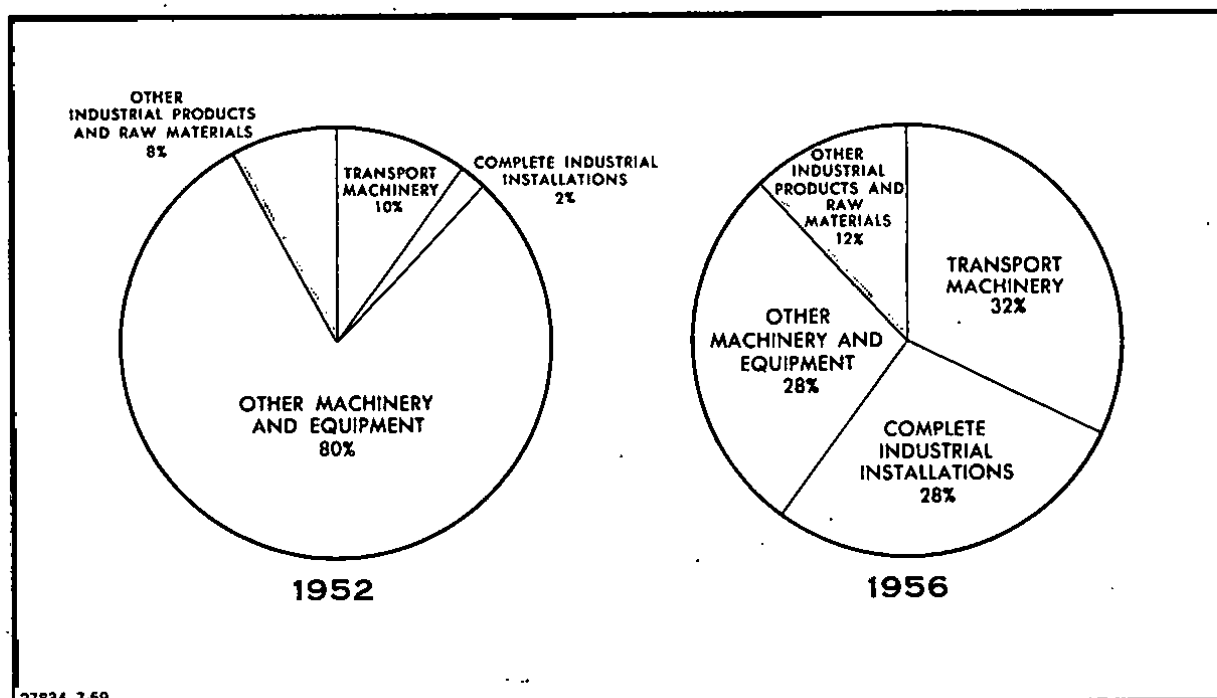


Figure 5. Communist China Imports from East Germany, 1952 and 1956.

indicate that electrical goods as well as precision machinery and optical equipment were the leading imports from East Germany in 1952. In contrast, transport equipment and complete installations were the most important commodity groups in 1956. The decline in importance between 1952 and 1956 of such categories as machinery and electrical equipment, however, primarily reflected the aggregation and export of these products as part of complete installations. East German exports of complete installations to China have been gaining in importance, amounting to 42 percent of East Germany's exports to China in 1957 and 58 percent of planned exports in 1958. 12/

The commodity composition of Chinese Communist imports from the remaining European Satellites differs somewhat from the pattern of imports from East Germany. Complete installations have been the leading commodity group in Czechoslovakia's exports to China in recent years, comprising nearly 50 percent of the total. 13/ The planned composition of Polish exports to China for 1957 was 44 percent for transportation equipment (primarily oceangoing vessels), 20 percent for complete installations, and 17 percent for iron and steel products. 14/

* Table 5 follows on p. 20.

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Table 5

Imports into Communist China from East Germany
 1952 and 1956

Commodity Group	1952		1956	
	Percent of Total <u>a/</u>	Value (Million Current US \$) <u>b/</u>	Percent of Total <u>a/</u>	Value (Million Current US \$) <u>b/</u>
Machinery and equipment				
General machinery	14	4.2	8	7.6
Transportation machinery	10	3.0	32	30.4
Chemical industry equipment	8	2.4	3	2.8
Machine tools and metal goods	13	3.9	4	3.8
Electrical goods	24	7.2	6	5.7
Precision machinery and optical equipment	21	6.3	7	6.6
Complete industrial installations	2	0.6	28	26.6
Subtotal	<u>92</u>	<u>27.6</u>	<u>88</u>	<u>83.5</u>
Other industrial products and raw materials				
Minerals and chemicals	4	1.2	9	8.6
Light industrial products	4	1.2	2	1.9
Products of the printing industry	0	0	1	1.0
Subtotal	<u>8</u>	<u>2.4</u>	<u>12</u>	<u>11.5</u>
Total	<u>100</u>	<u>30.0</u>	<u>100</u>	<u>95.0</u>

a. 15/

b. Computed by applying the percentage given here to the value of East German exports to Communist China as shown in Appendix A, Table 8 (p. 36, below).

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About 25 percent of Hungarian exports to China between 1953 and 1957 were vehicles, but deliveries of complete installations and electronic equipment have been significant also. 16/ Rumanian exports have been mainly petroleum products and equipment, although complete installations appear to be increasing in importance. Important Bulgarian exports to China have been tractors, fertilizers, pharmaceuticals, and nonferrous metals. Albanian exports have been mainly textiles.

Satellite exports have contributed to the development of the Chinese Communist military establishment, [redacted]

[redacted] Very probably a portion of the Chinese imports of such commodities as vehicles and communications equipment has been for military organizations. [redacted]

[redacted] In any event, Satellite exports of military end items to Communist China are believed to be small and probably are included in the Satellite trade data.

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V. Technical Assistance from the European Satellites to Communist China

Industrialization requires an abundance of technical equipment and skills, and the extreme shortage of producer goods and of engineers and technicians in Communist China, accordingly, has led it to rely on foreign sources for these things. China has recognized that the European Satellites possess a pool of engineering skills and can be relied upon as a source of industrial equipment. China began to draw on the Satellites' technical capabilities as early as 1950 and since that time has continuously utilized Satellite specialists and has imported an increasing volume of plant and equipment produced by the Satellites. Most frequently, in recent years China has imported technical services and industrial equipment combined into complete installations. Satellite technical assistance has also served as a method of training -- in particular on-the-job training -- of Chinese specialists. Thus China has improved its own technical capabilities and has already reduced in some measure its dependence upon foreign technical services.

A. Complete Installations*

Communist China showed considerable interest in importing complete installations from the European Satellites as early as 1950, but

* The term complete installations is a commodity category which is employed in Sino-Soviet Bloc foreign trade reporting and which covers the import and export of technical services and equipment combined in a single unit. Complete installations vary from [footnote continued on p. 22]

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few plants were imported before 1954. The early development of this type of import was inhibited by the lack of Chinese long-range plans and by the Satellite failures to meet their export commitments. By 1953, however, China had formulated its plans for development clearly enough to expand its requests for complete installations. Then, during 1954, most of the Satellites established firms specifically to handle the export of complete installations, a move which considerably improved the contracting procedures. By 1955 the deliveries of equipment for complete installations had become a significant element in China's imports from the Satellites. In 1956 and 1957, such imports comprised at least 30 percent of total imports from the Satellites, a proportion that is expected to rise in 1958 and subsequent years.

During the Chinese Communist First Five Year Plan (1953-57) the Satellites supplied equipment for 64 complete installations. By the end of 1957, 27 projects were completed and at least in partial operation, 17/ The USSR, in comparison, had provided 57 completed projects by the end of 1957. Many of the Soviet projects, however, were probably larger and more costly than the Satellite projects. About 67 percent, or 18, of the completed Satellite plants were electric power stations, 18/ and they accounted for about 18 percent of the increase of power-generating capacity installed by China during the First Five Year Plan (see Table 6*). China has contracted to import large numbers of electric powerplants from the Satellites during its Second Five Year Plan.

Czechoslovakia's exports of complete installations to Communist China have been predominantly electric powerplants but have included a fertilizer plant as well as a number of other smaller installations. East Germany's most important project has been a radio parts combine consisting of some 25 plants, nearly all of which have been completed. Among the other East German projects are an abrasive plant, two synthetic fiber plants, two glass plants, a precision measuring instruments plant, and a number of cement plants and electric power stations. Polish projects include two sugar refineries, one large sugar combine near Canton, and two coal processing plants. Hungary's main projects have been small electric power stations. Rumanian projects have also been largely electric power stations, although a number of cement plants have been contracted for China's Second Five Year Plan. Bulgaria has agreed to supply small electric power stations and ore flotation plants.

small units such as air-conditioning equipment designed for specific use in a textile mill to very large units such as an industrial complex consisting of many separate plants. The common ingredient in complete installations is the technical services involved in design, manufacture, and installation of equipment as a complete unit.

* Table 6 follows on p. 23.

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Table 6

Increase in Installed Power-Generating Capacity
in Communist China
Supplied by the European Satellites a/
1953-57

<u>Country</u>	<u>Megawatts</u>	<u>Percent</u>
Czechoslovakia	231	10
East Germany	108	5
Rumania	21	1
Hungary	39	2
Total	<u>399</u>	<u>18.</u>

a. 19/

Communist China's purchases of complete installations have been on current account and have involved no extension of long-term credits by the Satellites. The trade agreements generally call for a quota for estimated deliveries of technical services and equipment for the year. 20/ The Satellites appear to forward monthly invoices for designing costs and invoices for equipment at the time of each shipment. 21/ China pays the technicians' salaries to the responsible Satellite firm, probably monthly, and pays a per diem allowance directly to the technician. China pays in the required Western currency for sub-units or parts for the installations that have to be purchased from Western countries, apparently in advance of each purchase. 22/

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European Satellite firms have shown great interest in selling complete installations to Communist China, and some competition for these contracts has been evident.

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the initial planning and delivery schedules previously had been arranged during the course of more than a year of negotiations with East Germany. 23/ Thus, although Western suppliers have been largely eliminated from the Chinese market, competition among Bloc countries has permitted China to select from among Bloc suppliers several types of complete installations.

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B. Technicians

Some specialists from the European Satellites have been sent to Communist China to assemble and service machinery and equipment imported under regular commercial contracts from Satellite countries. In other cases, instructors have been sent to explain the operation of complicated or unusual equipment. Satellite personnel have been employed, for the most part, directly in production. There is no evidence, for example, that Satellite experts have filled advisory posts in ministries, as Soviet experts have done.

Communist China also has imported the services of many technicians through the purchase of complete installations. These technical services have been included in the cost of the complete units. The majority of the technical services have been performed in the various Satellite design bureaus where designs, blueprints, and other necessary technical data have been drawn up. Satellite specialists usually have been sent to China early in the designing stage of a project to obtain planning data and toward the end of a project to supervise the assembly, installation, and test operation of the project.

Training of Chinese Communist technicians has been provided by the Satellites, thus increasing China's pool of technical capabilities. Much of the training has been on-the-job training in China, but Chinese specialists have been sent to the Satellite countries to learn particular skills. As a result, Chinese technicians have been assigned to certain subordinate positions or functions formerly filled by Satellite specialists. Freedom from reliance on foreign technicians, however, appears to be still many years in the future.

The pay scale of foreign specialists in Communist China is high in comparison with the scale of Chinese workers, a phenomenon common to most underdeveloped countries. The per diem alone of foreign technicians is nearly twice the salary of comparable Chinese workers. The total payment (salary plus per diem) to a foreign engineer is probably 10 to 15 times that of his Chinese counterpart. China probably pays the per diem directly to the Satellite technician and his salary to his home company on the basis of monthly invoices. China must also pay a number of additional charges for specialists, including the specialist's transportation, housing, and insurance and a fee amounting to 50 percent of the specialist's salary to defray the administrative expenses of his home firm. The services of foreign technicians in China are costly and, although China has employed many Satellite technicians, the Chinese keep this number to a minimum by requiring the Satellite exporter to justify the need of each technician's work in China.

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C. Technical and Scientific Cooperation

Communist China also has obtained important technical assistance through the operation of intra-Bloc Scientific and Technical Cooperation Agreements. ^{24/} Under the agreements that China has signed with the Satellites it has obtained considerable technical data on industrial processes and on the use of various types of equipment, and it has received factory blueprints and designs for equipment. Chinese specialists have been trained in Satellite plants in general operations, in particular production processes, in utilizing special equipment, and in other technical and scientific endeavors.

Although Communist China has only limited ability to provide scientific and technical data, it has supplied some assistance to other Soviet Bloc countries, primarily in the agricultural field. It also has supplied technical data for the design of surgical instruments, for tung oil manufacture, for Chinese lacquer formulas, and for the cultivation and processing of herbs.

The countries of the Sino-Soviet Bloc usually claim that the Scientific and Technical Cooperation program involves no costs, but it seems probable that incidental costs such as reproduction costs for documents and traveling expenses are paid by the receiving country. It is believed that Communist China probably pays the traveling expenses and perhaps a per diem for Satellite technicians who come to the country for short periods under the Scientific and Technical Cooperation Agreements as well as perhaps also the salaries of those staying for several months. Conversely, Chinese technicians probably receive similar benefits when providing services to the Satellite countries, but China probably pays the expenses of Chinese sent to study industrial processes in Satellite countries.

VI. Reexports and Transshipments in Sino-Satellite Trade

A significant portion of Sino-Satellite trade involves transactions with third countries, but only the following two types of transactions have been important: those involving Satellite resales of Chinese Communist exports and those involving Chinese imports of Western goods via the European Satellites. Satellite reexports to China of goods produced in the Bloc appear to have been small. China has reexported some Satellite commodities, but the volume also appears to have been small. China has reexported small quantities of Western products, primarily rubber, to the European Satellites under the trade agreements.

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A. Resale of Chinese Communist Exports

Considerable quantities of the exports of Communist China to the European Satellites have been reexported, largely to countries of Western Europe, enabling the Satellites to supplement their scant holdings of Western currencies.* This practice began with the initial development of Sino-Satellite trade and has involved a significant portion of Chinese exports to the Satellites. Thus it is probable that, until 1957, Satellite resales of Chinese products were above \$30 million and possibly were as high as \$50 million yearly. Since 1957, resales appear to have been of less importance than in previous years. Hungary's resales amounted to nearly \$20 million annually during 1954-56 and represented between 50 and 70 percent of China's exports to Hungary. 25/ East Germany's resales amounted to about \$35 million in 1951

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In subsequent years, China exported directly to West Germany, and it seems certain that East German resales were sharply reduced after 1951.

For the remainder of the Satellites, there have been many resale transactions but no indications of over-all volume. In the Czechoslovak-French trade agreement for 1955-56, for example, the commodity list of Czechoslovak exports included the category "reexports of Chinese products," but the amount was less than \$1 million. 27/ Other Czechoslovak trade agreements have included such obviously Chinese products as tung oil as well as other commodities probably of Chinese origin such as antimony, tea, oilseeds, furs, and casings. Austria received Chinese products worth about \$1 million through trade agreements with several of the Satellites in 1953. 28/ Other Western countries, particularly West Germany, reportedly have received larger quantities of goods reexported from China.

The practice of reexporting goods from Communist China, particularly when sales are made at prices lower than those set by the Chinese, has had an unsettling effect upon the normal marketing of China's exports. Western European merchants of Chinese goods, many with a long tradition of handling Chinese products, have found Satellite offers at lower prices particularly disruptive. 29/ China has been aware of the Satellite marketing practices and of the disruptive

* European Satellite resales of Chinese Communist exports introduce a bias into Western trade statistics because most Western countries record imports on the basis of the country of origin wherever possible. This bias may reach significant proportions, as in West German statistics on trade with East Germany in 1951, when West Germany recorded approximately \$35 million of East German reexports as imports from China.

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effect on China's direct exports to Western Europe. China's reasons for allowing such sizable resales are uncertain, but the effect of past Chinese practice has been to permit the Satellites to adjust the volume of their resales to their immediate requirements for Western currency.

B. Imports of Western Goods via the European Satellites

Communist China has received significant quantities of Western goods via the European Satellites. Most of such goods have been purchased by Satellite firms acting as agents for Chinese firms or have been merely transshipped through Satellite ports. In both of these types of transactions, the goods and the associated payments probably do not enter the Sino-Satellite trade figures or the bilateral clearing accounts. There also has been a small volume of Free World goods reexported by the Satellites to China under the bilateral trade and accounting procedures, but these transactions were significant only in 1951. Evasion of Free World controls on strategic exports to Communist China has not been the only factor affecting the movement of Western goods to China via the European Satellites, and consequently the relaxation of controls in 1957 has not eliminated this pattern of trade.

Purchases by Satellite firms acting as agents probably have consisted largely of controlled goods. The largest series of known transactions of this nature occurred in 1956, when Satellite agencies purchased Western copper

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By far the greatest volume of Western goods has reached China through transshipments, primarily through the Polish ports of Gdynia/Gdansk. Many shipments have been carried by the Polish shuttle service from Western European ports to Poland and transshipped to the oceangoing vessels loading for China.

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Western strategic controls have served as a stimulus to these transshipments, but some of these goods would move to Polish ports for transshipment under normal commercial practice. Moreover, the Chinese have been able to exercise greater control over loading by having a large proportion of their sea cargo assembled in the Gdynia/Gdansk area.

VII. Other Economic Relations

A. Transportation

Because of the great distance separating Communist China from the European Satellites, transportation is an important factor in

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Sino-Satellite trade. China has entered into various relationships with Soviet Bloc countries to facilitate the movement of goods. Because lower ocean freight costs have caused the major portion of Sino-Satellite trade to be moved by sea, the more important of these bilateral relationships are in the field of ocean shipping.

Communist China's most important shipping associate is Poland, with which it has formed a joint company, Chinese-Polish Shipbrokers, Ltd. (Chipolbrok). The company was formed in 1951 with the head office in Tientsin and a large branch office in Gdynia. The management consists of both Chinese, associated with the Ministry of Communications, and Poles, associated with the Ministry of Navigation and the Polish Ocean Lines. The several million dollars in annual earnings of Chipolbrok may be shared equally, as the early announcements concerning the company indicated equal partnership. A large part of the earnings are probably in Western currency, as Chipolbrok requires a large percentage of the freight charges to be paid in Western exchange.

Chipolbrok functions as a ship and freight broker rather than as a shipowner. Ownership of the vessels under Chipolbrok control has been concealed because of the Free World embargo and bunkering controls and, in particular, because of the threat of seizure of vessels by Nationalist China. A tabulation of Polish-flag vessels at the end of 1956, however, included seven Polish-owned vessels which were not controlled by Polish organizations and nine foreign-owned vessels. The size of the vessels and the length of their voyages indicated that these vessels were employed on the Far East run and therefore were probably the Polish and Chinese contributions, respectively, to Chipolbrok. 31/ Four more vessels apparently were added to the China-owned fleet during 1957, but no additions from Poland have yet been identified.* The contribution of Poland to the company probably also includes technical services such as training Chinese seamen.

Other Polish-flag vessels as well as some chartered vessels, apart from the vessels assigned to Chipolbrok, are employed by the Polish Ocean Lines on the run to Communist China. Polish Ocean Lines employs Chipolbrok as the agent for these vessels when they are operating in Asian waters.

Czechoslovakia also operates a shipping line to ports in Communist China. Among the vessels of Czechoslovak registry are two which are probably owned by China. The use of Chinese-owned vessels

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suggests that China and Czechoslovakia may have an unpublicized joint shipping arrangement similar to Chipolbrok.

East Germany inaugurated a shipping line to Communist China in 1957 to supplement its charter arrangements. To date, the line has operated a very small fleet consisting primarily of East German-built ships.

The Czechoslovak- and Polish-flag vessels carry a large proportion of the seaborne cargo between Communist China and the European Satellites. In 1956, for example, Czechoslovak-flag and Polish-flag vessels are estimated to have carried more than 70 percent of the Satellite seaborne exports to China (including part of the Western goods transshipped at Gdynia) and about 25 percent of the tonnage from China to Eastern Europe. ^{32/} It has been necessary, however, to charter additional cargo space, and the Chinese and Satellite freight-forwarding and chartering companies have exchanged information and have coordinated plans informally while engaged in these shipping activities.

In rail transport, Communist China participates in the Bloc-wide agreements covering international freight and passenger traffic. The purpose of these agreements is to facilitate the movement of goods and passengers across national boundaries. Several measures have been established to this effect, such as a uniform rate schedule for goods transiting third countries. A central organization administers the agreements and acts as a clearing house for disseminating information. Communist China's adherence to these Bloc-wide agreements was probably motivated by the desire for simplification by the use of standardized procedures. Its participation probably has not appreciably affected the volume of rail shipments between China and the European Satellites. Nearly all of the Sino-Satellite rail shipments appear to be Chinese imports of Satellite goods, and the general criterion for selecting rail transport probably is based upon the required time of arrival of the goods in China. China has frequently selected the more expensive rail transport rather than ocean transport because the items were required at an early date. Adherence to the pacts is a convenience for China, although some economic benefits are probably derived from the uniform transit rates.

B. Financial Cooperation

Communist China has developed diverse financial relationships with the state banks of various European Satellites in addition to the bilateral relationships necessary for financing Sino-Satellite foreign trade. These financial relationships are further examples of the broad participation of China in Soviet Bloc economic activities and illustrate the comprehensive cooperation which links China to the Bloc.

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The Chinese State Bank has acted on a small scale as a short-term financier for some of the Satellites' imports of Western goods, thus tempering the problems of the Satellites in dealing with Western Europe with inadequate currency reserves. The arrangements appear to have been in the nature of revolving lines of credit in convertible Western currency on which a maximum volume of trade bills could be drawn. China has placed at least \$10 million at the disposal of the Satellites for short-term financing of imports from Western countries.

The Chinese State Bank also has established Western currency accounts in several Satellite banks for handling trading operations in Western Europe. ^{33/} The original motivation was probably the Chinese fear of sequestration of funds held in Western banks after Chinese troops entered the Korean War. More recent reports, however, indicate that China has enlarged the number of Satellite banks in which Chinese funds are deposited and also has called upon Satellite banks to an increasing extent for other international banking services.

The nationalized insurance company in China has participated in reinsurance treaties of other Bloc countries, probably on the basis of reciprocity. All known reinsurance treaties in which China has participated have involved Western currency liabilities, apparently the only type of risk that the Bloc insurance companies regard as calling for reinsurance coverage. Most of the reinsurance treaties in which China has participated appear to have covered marine risks.

C. The Role of Communist China in CEMA

The Council for Mutual Economic Assistance (CEMA) was established in 1949 as the mechanism for Soviet Bloc-wide coordination of economic activity and mutual economic aid. The extent of CEMA's activities has increased since its inception, but it has suffered from chronic inability to make its decisions binding upon member countries. Thus CEMA's effectiveness to date has rested primarily upon the hortatory influence it can exert within the Bloc.

Although Communist China's role in CEMA has been limited to that of observer, the Chinese have asserted that their economic cooperation with member countries has been as great as the cooperation among the members themselves. ^{34/} China probably has been as active as full members regarding CEMA decisions when these decisions have been in harmony with Chinese interests, which is the same approach to CEMA recommendations as that employed by the member countries. The Chinese have been active in such CEMA activities as promoting long-term trade agreements and technical and scientific exchanges. They have signed long-term trade agreements and Scientific and Technical Cooperation Agreements with nearly all members of CEMA. They have participated aggressively in discussions regarding pricing problems in intra-Bloc trade. Thus, in those

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CEMA matters affecting China's international trade with Communist nations and its internal development, China has cooperated as thoroughly as have the full CEMA members.

Many questions before CEMA, however, have involved detailed discussions of particular industries and have been of primary concern to the industrialized countries of Eastern Europe. Accordingly, China and the other Bloc countries in Asia probably have believed that they had little to gain from active participation. China, for example, had little direct interest in the technical discussions regarding the petroleum pipeline to be laid from the USSR to the European Satellites and so has not taken part in these sessions. Also, China has not participated in the decisions regarding industrial integration. Although China may ultimately benefit from the gains in efficiency resulting from economic integration within the Soviet Bloc area, active participation in industrial specialization and economic integration is not a matter with which the Chinese can be seriously involved, given the present state of economic development in China. It is unlikely, moreover, that China in the foreseeable future will become very much involved in the integration plans of CEMA. With its vast and varied internal resources, China will derive far more advantage from pursuing a policy leading to self-sufficiency on a broad basis, a policy which the Chinese have expressly avowed they intend to follow.

Limited participation as an observer in the CEMA organization is probably sufficient for Communist China to protect its economic interests and at the same time to display sympathy for the general principle of intra-Bloc cooperation without becoming involved in specific and undesirable commitments regarding economic integration. So far, CEMA's efforts have been largely directed to areas of interest to China and, as a consequence, China has been as active as the full members. If in the future the integration decisions are more closely adhered to by the full members, China may participate in this sphere of activity in order to protect its immediate economic interests. Their apparent intention to develop their economy on a basis encompassing virtually all fields of industry, however, suggests that the Chinese will remain apprehensive about active participation in the integration decisions of CEMA and about full membership.

VIII. Prospects for Future Sino-Satellite Economic Relations

The mutual advantages of Sino-Satellite trade indicate a continued expansion of this trade during the next few years. A major part of this expansion will undoubtedly consist of greater Satellite exports of machinery and equipment, largely in the form of complete plants, to further the increased tempo of Communist China's industrialization. Pacts covering future trade with several Satellites have been signed, generally calling for increased trade. Thus a continually rising

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level of trade between China and the European Satellites is virtually assured.

The relative importance of Sino-Satellite trade in the future, however, is uncertain. The Chinese Communist practice of favoring trade with the Satellites in order to consolidate Bloc relations and to preserve an economic confederation of ideologically united nations may well stimulate the future development of Sino-Satellite trade at a faster rate than the growth of China's total foreign trade. On the other hand, economic factors may play a more important role in determining the relative position of Sino-Satellite trade. The development of Chinese export capabilities in some types of industrial goods such as iron and steel products, textiles, and other light industrial goods points to an expansion of China's trade with Asian and African countries. The relaxation of trade controls suggests that China's trade with developed Free World countries may also become increasingly important. Sino-Soviet trade is expected to maintain its relative position in China's future trade, and Chinese export surpluses will be necessary to cover Chinese credits and grants as well as debt service.

Some aspects of Sino-Satellite trade also suggest that it will not rise as rapidly as Communist China's trade with other regions. The difficulties encountered by the Chinese with late, defective, and incomplete deliveries from the Satellites have appeared important enough to restrict future orders, particularly since the relaxation of the trade control program provides the alternative of Western suppliers. Moreover, the recent attempts by the Chinese to include more industrial products in their exports to the Satellites at the expense of the preferred raw materials and foodstuffs have probably made Chinese exports less desirable to the Satellites. Thus the growing problems arising from the type and volume of Chinese export resources appear to restrict the possibilities for future trade with the European Satellites and suggest perhaps a slight decline in the relative importance of Sino-Satellite trade to China.

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APPENDIX A

METHODOLOGY FOR THE LEVEL AND BALANCE OF TRADE
BETWEEN COMMUNIST CHINA AND THE EUROPEAN SATELLITES

1. Estimates of the Level of Trade

Data recently published by the Chinese Communists provide a reliable series of statistics for the annual yuan values of China's total foreign trade and for a breakdown by the following geographical areas: the USSR, the European Satellites, the Asian Satellites, and non-Communist countries. Comparison of these yuan values with other foreign trade data published by other countries and in other currencies suggests that China has been using a system of multiple exchange ratios. Thus the implicit cross rates between yuan and dollars for the various segments of China's foreign trade have been derived from trade data, as follows: 2.46 yuan per dollar for Sino-Western trade, 4 yuan per dollar for Sino-Soviet trade, approximately 3.7 yuan per dollar for Sino - European Satellite trade, and probably 4 yuan per dollar for Sino - Asian Satellite trade.*

The relevant data on Sino-Satellite trade are shown in Table 7,** but a comparison can be made only for 1953-56, when relatively complete Satellite trade figures were available. Although the average implicit exchange rate for this period, which can be computed from available evidence, is 3.70 yuan per dollar, it is probable that Communist China actually uses a dual conversion system, with one set of internally consistent rates for Bloc trade and one for non-Bloc trade. Thus the Chinese probably convert Sino-Satellite trade into yuan values at the equivalent of 4 yuan per dollar, the same conversion factor as that found in Sino-Soviet trade, and the apparent ratio determined by comparing the Satellite data (in dollars) with the Chinese data (in yuan) may be lower because of differences in Satellite and Chinese recording techniques. Available information regarding methods of recording and valuing foreign trade in China is inadequate, however, to explain the discrepancy between the derived rates for Sino-Satellite trade and those for trade between China and other Bloc countries. Thus the estimated

* [redacted] a preliminary approach to Chinese exchange ratios. 50X1
The yuan values [redacted] have been slightly refined in the present report. Additional information used in this report also considerably altered the derived Sino-Satellite exchange ratio from that found in the above source.

** Table 7 follows on p. 34.

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Table 7

Implicit Foreign Exchange Rate for Trade
Between Communist China and the European Satellites
1950-58

	1950	1951	1952	1953	1954	1955	1956	1957	1958 (Preliminary)
European Satellite data (million US \$) a/									
East Germany	N.A.	N.A.	N.A.	113	165	184	181	194	238
Czechoslovakia	N.A.	N.A.	N.A.	116	120	118	131	147	200
Poland	8	49	55	57	67	66	85	82	108
Hungary	0	45	48	63	58	66	59	58	91
Bulgaria	Negligible	Negligible	3	10	8	9	10	N.A.	N.A.
Rumania	Negligible	N.A.	N.A.	10	15 b/	20 b/	28	N.A.	N.A.
Albania b/	0	0	0	0	0	4	6	N.A.	N.A.
Total	N.A.	N.A.	N.A.	369	433	467	500	N.A.	N.A.
Chinese Communist data (million yuan) c/									
Derived ratio of ex- change (yuan per dollar)	83	814	1,283	1,376	1,496	1,728	1,869	1,960	2,615
Estimated Sino-Satellite trade (million US \$ d/)	N.A.	N.A.	N.A.	3.73	3.45	3.70	3.74	N.A.	N.A.
	20	205	320	345	375	430	465	490	655

a. Data are from European Satellite statistical publications and have been converted from Bloc currencies at the official exchange rates for current US dollars. Totals were derived from unrounded data and may not agree with the sum of their rounded components.

b. Estimated.

c. Data are [] with minor refinements for 1954 and 1955 based on recent Chinese publications.

d. Converted at 4 yuan per dollar and rounded to the nearest number divisible by five.

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dollar values for Sino-Satellite trade shown in the text have been derived for 1950-58 by converting the Chinese yuan values into dollars at the average conversion rate of 4 yuan per dollar.

2. Estimates of the Balances on Clearing Accounts

The balances of the Sino-Satellite clearing accounts presented in Table 3* are estimates of the approximate net total of the end-of-year imbalances in the individual Sino-Satellite clearing accounts. The basic data employed have been the published trade data of the Satellite countries supplemented by available information on some financial transactions. The quantitative data employed in the estimates are shown in Table 8.**

The use of trade data as a basis for estimating Sino-Satellite clearing balances is believed to be justified by the reasoning below. Commodity trade is the dominant element in the clearing accounts and is the part of the accounts where significant imbalances are most likely to occur. Service items are the minor part of the Sino-Satellite clearings and are probably approximately in balance each year. The payments associated with Satellite personnel in China (such as delegations, students, and embassies) are probably about the same as the payments associated with Chinese personnel in Satellite countries. Imbalances in the flow of such payments are minor in magnitude and are insignificant when compared with payments for commodity trade.

Payment of transportation costs is the major remaining service item which might be included in clearing transactions but not in trade statistics. It is doubtful, however, whether many of the transportation charges are included in the Sino-Satellite clearing procedures. All known goods in Sino-Satellite trade are sold either f.o.b. the border or a nearby port, and thus, for railroad shipments, nearly all transportation payments would be settled with the USSR as the country providing most of the transportation services.

Payments for ocean shipping are more involved. Most of the transportation charges for Chinese Communist exports are probably paid by the Satellite countries to either Poland or the Western country supplying the charter ships or freight services from China. A large proportion of Satellite exports is carried to China in Polish vessels, but, considering the joint Chinese-Polish shipping company, in which profits are probably shared equally, it seems unlikely that China has a significant net indebtedness -- on the contrary, China probably realizes a small net income from shipping services because of this company. China also uses ships of several Western countries to transport Satellite goods to China, but payments for these services would not enter Sino-Satellite clearing.

* P. 10, above.

** Table 8 follows on p. 36.

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Table 8

Derivation of Estimated Balances on Clearing Accounts
Between Communist China and the European Satellites
1951-57

	1951			1952			1953			1954			1955			1956			1957			Cumu- lative Bal- ance
	Pay- ments a/	Re- ceipts a/	Bal- ance	Pay- ments a/	Re- ceipts a/	Bal- ance	Pay- ments a/	Re- ceipts a/	Bal- ance	Pay- ments a/	Re- ceipts a/	Bal- ance	Pay- ments a/	Re- ceipts a/	Bal- ance	Pay- ments a/	Re- ceipts a/	Bal- ance	Pay- ments a/	Re- ceipts a/	Bal- ance	
East Germany	22 b/	62 b/	40	30 c/	35 c/	5	45 c/	68 c/	23	98	67	-31	97	87	-10	95	86	-9	106	89	-17	1
Czecho- slovakia	N.A.	N.A.	40 d/	N.A.	N.A.	-15 e/	N.A.	N.A.	-15 e/	N.A.	N.A.	-10 e/	58	61	3	65	66	1	80	67	-13	-9
Poland	26	23	-3	21 f/	34 f/	13	30	27	-3	37	30	-7	30 f/	36 f/	6	50	45 g/	-5	45	45 g/	0	1
Hungary	21	25	4	21	27	6	30	33	3	31	27	-4	37	29	-8	31	28	-3	30	27	-5	-5
Bulgaria	Negli- gible	Negli- gible	Negli- gible	1	2	1	5	5	0	4	4	0	5	4	-1	5	5	0	4	4	0	0
Rumania	Negli- gible	Negli- gible	Negli- gible	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	N.A.	6 h/	17	11	-6	N.A.	N.A.	N.A.	0 h/
Albania	0	0	0	0	0	0	0	0	0	0	0	0	0	N.A.	N.A.	1 i/	N.A.	N.A.	2 i/	N.A.	N.A.	4 j/ 7 j/
Net total j/			80			10			10			-20			-5			-20				-30 -2

a. Payments are the monetary flows associated primarily with Chinese imports, and receipts are the monetary flows associated primarily with Chinese exports. Payment information has been used wherever available, but primarily reliance has been on commodity trade data. The figures are import-export data from Satellite statistical publications, unless a specific source is cited. Figures in Bloc currencies are converted to dollars at the official exchange rates.

b. 37/

c. 39/. These figures are from data on bank payments rather than on commodity trade.

d. 39/

e. Assumed to be the rate of repayment for the Czechoslovak debit balance in 1951.

f. 40/. There are two series of Polish trade figures for trade with China which differ only for the years 1952 and 1955. This series appears to be the more accurate.

g. The sum of \$10 million has been added to the 1956 Polish trade statistics because of Chinese payments of Western currency for Polish iron and steel. 41/. Such payments are estimated to have been \$7 million to \$8 million in 1957.

h. A balance is assumed because of the Chinese policy of maintaining balanced trade.

i. Trade is assumed to balance. Balances shown are estimated Chinese deliveries to Albania under the long-term credit agreement.

j. Totals are rounded to the nearest figure divisible by 5.

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