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EUROPEAN COMMUNITY: Trade with China

//Members of the European Community are scrambling to profit from China's decision to turn to Western suppliers for technology and equipment. The two-way flow of commodities and cash, however, remains small. Increases in trade implied in recent agreements are on the order of 15 to 20 percent per year through the mid-1980s.//

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//EC exports to China reached $1.4 billion in 1975 but by 1977 had fallen back below $1 billion. Even in 1975, however, exports to China represented less than 0.5 percent of total exports by EC countries and about 1 percent of their sales outside the Community. China's share of imports by EC countries was only about 0.3 percent.//

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//In the first half of 1978, EC shipments to China ran close to the total for all of 1977 and, over the full year, these exports no doubt broke the 1975 record. EC imports from China for 1978 increased roughly 15 percent over 1977.//

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//China's plan for modernization through 1985 could entail a substantial amount of business for all the large EC countries. The plan lists 120 major projects, including 10 steel plant complexes, nine nonferrous metal plants, eight coalfields, 10 new oilfields and gasfields, 30 electric power plants, six major railway networks, and five major ports.//

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//Except for the problems involved in sales of military equipment and nuclear technology, constraints on increased EC-China trade are largely on the Chinese side and are based primarily on China's limited ability to pay for and absorb Western goods. While the Chinese may now be willing to accept conventional foreign credits, they still want to offset imports with exports.//

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//For the Europeans, the key obstacle to meeting trade goals will be finding suitable Chinese products at competitive prices. Soviet displeasure with growing EC-China trade and particularly with the prospect of Chinese arms purchases may affect EC relations with both China and the USSR. The Europeans will consider the Soviet angle, as well as US policy, in responding to Chinese requests for sensitive goods. Although a turning point

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appears to have been reached, long and frustrating negotiations loom for the West Europeans; regardless of the outcome, China will remain a small market for European industry.// [redacted] 25X1

INTERNATIONAL: Cobalt Outlook

A net increase in the global supply of cobalt seems likely this year; the addition will ease but not eliminate the tight supply situation. Demand for cobalt, which is a critical and largely irreplaceable industrial metal, has been rising for the last several years and will probably continue to rise this year. [redacted] 25X1

Cobalt was in tight supply before the invasion in May of Zaire--the leading producer. This scarcity was largely attributable to a shortage in Zaire of spare parts for cobalt production and to the fact that preoccupation with copper production led Zaire to give inadequate attention to cobalt processing. [redacted] 25X1

The invasion did not adversely affect Zaire's cobalt facilities, although it did spark speculative buying, partly in response to inaccurate reports that mines and machinery had been destroyed. The flight of some 400 white technicians also did not constitute as serious a production obstacle as had been forecast by earlier reports. Nevertheless, the Zairians now acknowledge that they face increasing problems. President Mobutu has been forced to try to rehire about 140 foreign technicians who were fired because they fled Zaire after the invasion. Zaire must also replace overaged, defective equipment and acquire spare parts that are currently in short supply. [redacted] 25X1

Even if it could obtain the $100 million necessary to purchase the machinery and parts, Zaire probably would have to wait a year or more for completion of equipment deliveries. In the interim, we anticipate that production problems will accumulate and will reduce recent levels of production. [redacted] 25X1

The shortfall in Zairian cobalt output this year probably will be more than offset, however, by additional output from other producers attempting to cash in on the record prices. Production gains in other countries will probably be at least 5,000 tons. Zambia alone is planning a 2,000-ton increase that will roughly double its current output.

Since the invasion, the official producer price of cobalt has tripled to $20 per pound and undoubtedly will go higher; prices for small-lot sales on the "free" or "gray" market have risen 700 percent to $50 per pound. These stiff increases are easily passed on to consumers because the added cost of cobalt is only a fraction of the final product prices.

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BRIEF

Soviet Meat Buying

The USSR may recently have purchased as much as 40,000 tons of beef from Western suppliers and may be looking for more. This is the first sign of Soviet meat purchases last year; in 1977 the USSR imported more than 200,000 tons from the West. [redacted]

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Because of the tight world meat situation, which has increased prices by 28 percent since last July, Soviet purchases on this scale would probably put upward pressure on prices. [redacted]

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Although the reported purchases would add less than 1 percent to domestic Soviet supplies, the current buying may be explained by the leadership's publicly expressed concern over the effects of continued meat shortages on the mood of the public. [redacted]

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FEATURE ARTICLE

USSR: Compensation Agreements

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The USSR is placing increased emphasis on compensation agreements with Western firms to ensure long-term hard currency earnings. Export earnings guaranteed under the more than 45 agreements signed to date far exceed the $8 billion worth of agreement-related imports from the West. Annual earnings will rise to nearly $4 billion in 1985, softening the impact on Soviet foreign trade of a probable decline in oil exports. Our earlier estimate that the USSR's hard currency import capacity will fall in the early 1980s, however, remains unchanged. [redacted] 25X1

Despite the intense Soviet interest in compensation agreements, problems--notably inept Soviet bureaucracy, inadequate support facilities, and Western difficulties in absorbing large amounts of basic Soviet industrial products--have slowed the pace of new signings. [redacted] 25X1

Compensation agreements essentially allow the Soviets to import Western capital goods on credit and subsequently export to the West a portion of the production from the imported equipment to repay the credits. The major impetus for the USSR has been a desire to acquire and pay for technology and equipment to develop Siberia and to expand certain high priority industries. [redacted] 25X1

The agreements reduce the risk associated with buying Western equipment on credit. In 1975, for example, the Western recession practically halted the growth of Soviet hard currency exports, driving home to Moscow how dependent its exports were on Western economic conditions. Compensation agreements protect the Soviets from developments in the West that would otherwise reduce Soviet export earnings. [redacted] 25X1

Over the past decade, more than 45 compensation agreements have been signed under which nearly $8 billion in Western equipment will be installed in the USSR. The most profitable agreements for the USSR are the gas-for-pipe deals with Western Europe, which call for imports to the USSR of large-diameter gasline pipe in return for delivery of gas to Western Europe for up to 20 years and longer. These agreements will generate revenue several times greater than the $2.8 billion worth of Soviet pipe imports. Rising gas prices will probably earn Moscow $1.2 billion in 1980 and nearly $3 billion in 1985 under current gas delivery schedules. [redacted] 25X1

The Soviet chemical industry, which has been the most aggressive industry seeking foreign help, has ordered more than $3 billion in equipment and technology for fertilizer, petrochemical, and other plants under product-pay-back deals. The chemical deals generally involve just enough exports to cover Soviet payments. In the only major compensation agreement with a US company, Occidental Petroleum last year began to receive ammonia in connection with a deal for four chemical plants at Tolyatti. Other Soviet industries involved in compensation arrangements are timber, coal, and aluminum. [redacted] 25X1

Earnings from compensation deals signed thus far are likely to rise from about $830 million in 1977 to nearly $4 billion in 1985. Revenue from the deals will far exceed costs, yielding Moscow substantial increases in hard currency import capacity in the 1980s to help offset losses from a probable decline in Soviet oil exports. [redacted] 25X1

Internal Soviet problems and Western disenchantment, however, have led to few major agreements since 1974. On the Soviet side, debate continues over the policy of committing raw materials as the price for Western help in developing Soviet resources. The bureaucracy in the USSR, moreover, remains ill-equipped to handle compensation agreements, and ideological attitudes clearly conflict with Western demands for equity participation and management control. Even if agreements can be reached in principle, the primitive level of Siberia's infrastructure and the difficulties involved in taking on several large development projects simultaneously will slow the proliferation of compensation agreements. [redacted] 25X1

On the Western side, companies are reluctant to accept many Soviet products. Unlike their attitude in 1974, when fuel and raw material shortages made long-term supplies of Soviet products attractive to Western firms, these companies now regard compensation agreements as a disagreeable condition for winning Soviet contracts. The

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depressed West European chemical industry is already worried about the chemicals, fertilizers, and petrochemicals that the USSR soon will begin to export under compensation agreements.

Deals involving energy suffer much less from this constraint. Agreements on manufactured goods have not been concluded mainly because the Soviets have been unwilling to meet Western demands for continuing participation and management control to ensure quality.

Despite these problems, the USSR and Western firms are discussing several large deals. If negotiations can be concluded soon, the associated projects would boost Soviet raw material production and exports appreciably by 1985. Deals likely in the near term involve chemicals, wood and wood products, aluminum, and possibly natural gas. Over the longer term, additional compensation agreements could be tied to developing Siberian natural gas deposits in Yakutsk and Urengoy, a major steel complex, copper deposits, and offshore oil reserves.

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FEATURE ARTICLE

RHODESIA: White Emigration

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The number of white Rhodesians who have emigrated from the country has accelerated sharply since mid-1978 as guerrilla activity has increased and as the outlook for an actual turnover of power to a black majority government has loomed closer under the internal settlement plan of Prime Minister Smith. For the year as a whole, a record 13,000 more whites emigrated from the country than entered it--a drain of about 5 percent of the white population. Reports of "extended vacations" indicate that an additional 20,000-30,000 persons may have left on a wait-and-see basis pending the outcome of the struggle.

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We expect another record outflow in 1979, possibly reaching disastrous proportions if the Smith government cannot sell its revised internal settlement. A surge in guerrilla activity--a distinct possibility--could seriously damage already fragile white morale, sparking a large exodus of whites and possibly dealing economic, political, and military institutions an irreparable blow.

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In sharp contrast to net white immigration of 40,000 people in 1966-75, 31,000 more whites left Rhodesia than entered in the last three years. Initially, the dramatic reversal in the migration trend was caused by stepped-up guerrilla activity accompanied by deepening recession. Many young Rhodesians in particular lost all hope in the country's economic and political future. Later, the departures took on a momentum of their own as families saw neighbors, relatives, and coworkers leave or prepare to leave.

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After leveling off somewhat in early 1978, net emigration more than doubled in the second half of the year when it became apparent that the internal settlement would not lead to a cease-fire or an end to UN economic sanctions. The massacre of 14 missionaries and

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their dependents at Elim and the downing of the Air Rhodesia Viscount dealt a further blow to white morale. Successful cross-border raids by Rhodesian security forces in October and November, designed in part to boost morale, did not stem the flow, which reached record heights. The destruction of the fuel depot at Salisbury in December probably added to the out-migration. Even before this, applications for emigration pointed to a surge toward the end of the year. 25X1

Most of those who have left are skilled or white collar workers and professionals. More than half of the white males who left in 1978 were reportedly between the ages of 25 and 45; many of those leaving hold dual citizenship in the UK, South Africa, or other countries. 25X1

Emigration has had a major impact on the economy, contributing to a 20-percent decline in GNP since 1975. A shrinking domestic market--as whites, who represent most of Rhodesia's purchasing power, leave the country--along with tight government economic policies that emphasize large military imports have weakened demand. Demand for consumer durables has fallen off as Rhodesians increasingly put their money into portable valuables such as gold and jewelry. This has contributed to a sizable drop in manufacturing output since 1975. 25X1

//The manpower drain has not made itself felt in the military yet. To some degree, however, the rising emigration already has served indirectly as a check on expanding the white military forces because the government is hesitant to draft more whites into the services for fear of further deflating white morale.// 25X1

The emigrant flow and the possibility that it might become a flood were the key factors that convinced Smith and his black nationalist partners to revise their internal settlement to provide for greater white participation in the government than they originally had agreed to. Smith's plan will be put to the test by the white referendum on the constitution scheduled for 30 January. The potential loss of manpower also was one of the reasons why Smith decided earlier this year to talk with black nationalist leader Joshua Nkomo. 25X1

A substantial hardcore of whites, perhaps 100,000 or more, will nevertheless probably elect to stick it out in Rhodesia through 1979 and longer, unless conditions deteriorate drastically. These whites are typically native born, without dual passports, owners of substantial property in Rhodesia, and attached psychologically to the country. [redacted] 25X1

Loss of 25 percent or more of Rhodesia's European population would bring immediate and irreparable damage to the white war effort and the economy. [redacted] 25X1

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