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PROSPECTS FOR CLOSER YUGOSLAV ECONOMIC RELATIONS
WITH THE USSR



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PROSPECTS FOR CLOSER YUGOSLAV ECONOMIC RELATIONS
WITH THE USSR

Summary and Conclusions

The recent rapprochement between Yugoslavia and the USSR has entailed Soviet recognition of the respectability of the Yugoslav brand of socialism and agreements calling for a substantial increase in Soviet-Yugoslav trade. Both sides appear to be playing down ideological differences. At the same time, neither the USSR nor the Yugoslavs have taken any important steps to reduce the actual differences in their economic systems. The new Yugoslav trade agreement with the USSR, if implemented, would bring trade well above the depressed level of the past 2 years, but there are no firm indications that the USSR has extended new credits to Yugoslavia, and Yugoslavia has not as yet gained association with the Council for Mutual Economic Assistance (CEMA).

The Yugoslav regime undoubtedly favors increased economic relations with the USSR to derive economic benefits and to protect the country against the uncertain prospects for Western trade and aid. The regime, however, would be reluctant to increase these relations to the point of threatening Yugoslav independence; the uniqueness of the Yugoslav economic system; the benefits of good economic relations with the West, including credits and a better quality and greater diversity of imports; and the special advantages of a "nonaligned" status in relations with underdeveloped Free World countries. Moreover, the decentralized economic system of Yugoslavia makes it difficult for the government to increase greatly imports from the Soviet Bloc even if it so wishes, because of the preference of Yugoslav producers and consumers for Western manufactured goods.

Tito no doubt hopes that closer Soviet-Yugoslav relations can be achieved without endangering the US aid program under Public Law 480 and Western European credits. If his actions should provoke suspension of US aid and

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supporting measures in Western Europe, he faces a serious short-term problem of maintaining food consumption at a satisfactory level, for the Bloc is in a weak position to help him in this respect. Over the longer term, loss or curtailment of Western assistance could be expected to lower significantly the rate of Yugoslav economic growth unless compensating credits are obtained from Bloc countries.

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1. Recent Developments

a. Trade and Aid

Recent indications of improvements in Yugoslav relations with the USSR -- such as the exchange of visits by Presidents Brezhnev and Tito and subsequent statements by Khrushchev and Tito suggesting a broadened area of agreement -- raise the possibility of a closer economic relationship between the two countries. Such a change presumably would involve a substantial increase in trade between the two countries -- possibly with the stimulus of Soviet credits and technical assistance for Yugoslav industrial development. The USSR might also offer Yugoslavia some form of participation in CEMA.

Yugoslav trade with the USSR has recently declined to only 5 or 6 percent of its total turnover compared with a share of 9 percent in 1959, and trade with the European Satellites has declined moderately, to about 16 percent of Yugoslav turnover (see Tables 1 and 2). Expectations of increased Yugoslav trade with the USSR and the Satellites rest largely on new trade agreements for the next several years. A new agreement with the USSR, covering 1963-65, projects a trade turnover of \$750 million during the 3 years compared with the old agreement for 1961-65 that scheduled a turnover of \$800 million during the 5 years and was not being fulfilled. The Soviet-Yugoslav trade protocol for 1963 schedules a turnover of about \$180 million -- an amount about three-fifths larger than turnover in 1960 (a more normal year than 1961) and much larger than turnover in 1962, judging from data for 9 months. Whether or not any such growth of trade with the USSR will actually take place remains to be seen, for earlier agreements specifying large increases in Soviet-Yugoslav trade sometimes were not realized. Yugoslav complaints that the USSR would not deliver the desired types and qualities of goods have been common. Even if both governments agree that a much larger volume of exchanges is desirable, the carrying out of the policy may be hampered by the freedom that Yugoslav producing and trading enterprises have in deciding what to produce and where to market it most profitably.

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There is little firm evidence so far that the USSR has extended or soon plans to extend credits to Yugoslavia. Since the suspension in 1958 of Soviet and other Bloc credits extended during the preceding period of rapprochement, Yugoslavia has received no new credits from these countries except possibly for one credit from Poland. The efforts last July of a Yugoslav economic delegation in Moscow to arrange reinstatement of the suspended Soviet credit do not appear so far to have been successful.

The Yugoslav regime has been interested for some time in gaining observer status in CEMA, apparently believing that such an association would further the country's development and would be accepted by Western countries without a violent reaction if it were accompanied by efforts to obtain some form of association with the European Common Market. So far as can be determined, however, Yugoslav participation in CEMA has not yet been approved.

b. Economic Systems and Ideologies

The recent Soviet-Yugoslav rapprochement has involved Soviet recognition of the respectability of the Yugoslav brand of socialism and the playing down of ideological differences by both sides. The Soviet regime once again has formally recognized Yugoslavia's status as a socialist state in spite of the differences in approach and in economic systems. The USSR has strengthened Yugoslavia's ideological position in agricultural policy by accepting a similar deviation in Poland. Finally, by greatly widening the area of acceptable discussion in the USSR and the European Satellites on possible ways of reforming the economic system (for example, the discussion of the "Liberian proposal," which would give greater freedom of action to enterprise managers), the USSR has made the unique aspects of Yugoslav socialism outside agriculture more respectable within the Bloc. For its part the Yugoslav regime appears to be willing to deemphasize its ideological differences with the Bloc but without retreating from its established ideological line.

The main ideological differences between the USSR and Yugoslavia, however, still exist. Moreover, recent institutional changes in the two countries have done little to make the two systems more

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similar, and a sharp contrast remains between Yugoslav decentralization and workers' management and the strong central control and detailed planning of the Soviet system. In the USSR, recent changes have been wholly administrative in character and, if anything, have tightened central controls over the economy. The Liberman proposal and other liberal proposals, if adopted, would indeed bring the Soviet system closer to the Yugoslav, although none of the proposals would go so far as to allow the market to regulate an important part of economic activity as in Yugoslavia. These proposals, however, have not been implemented, and the prospects for any drastic changes in the Soviet economic system in the near future are small.

The Yugoslav system, which had been further liberalized in 1961 with the adoption of a uniform foreign exchange rate and a reduction of controls over the expenditures of enterprises, appears to have weathered a period of faltering industrial growth and stagnation of exports in 1961 and the first half of 1962 without any major damage, and the economic situation, except in agriculture, has improved considerably in the past few months. Some restrictions over enterprise activities and foreign exchange spending were reimposed, but the regime apparently relied mainly on indirect methods of control such as a tightening of bank credit, resisting the temptation to attack current economic problems through direct intervention by the state. In agriculture, however, economic pressure on private farmers to enter into some form of association with cooperatives increased considerably, although there was only a small increase in the area under socialized farming.

2. Prospects

a. Motivating Factors

The Yugoslav regime has both ideological and economic reasons for seeking closer relations with the Bloc. Communist ideology fosters a desire on the part of the Yugoslav leaders to have the "socialist" status of their country accepted by other Communist countries. It is probable that profitable opportunities exist for increased trade and other forms of economic cooperation with the Bloc that have been slighted in

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the past for political reasons. Finally, increased economic relations with the Bloc are also sought because of the uncertainties of Western policies concerning trade and aid. Prospects for aid from the US must seem uncertain to the Tito regime. Whether or not the loss of most-favored-nation status for Yugoslav exports to the US can be reversed in the near future is also uncertain. Boycotts and demonstrations in some US communities against goods from Communist countries have caused concern in Yugoslavia. The Common Market seems certain to have adverse effects eventually on Yugoslav trade with Western Europe unless some special status such as associate membership can be arranged -- a step that West Germany, for example, at present seems to oppose.

b. Limiting Factors

Although the Yugoslav regime wants to expand its economic relations and improve its ideological relations with the Bloc, it is apparently as determined as ever to maintain Yugoslavia's full independence and the distinctive economic system evolved over the last decade. Moreover, the regime would be reluctant to forego the economic benefits which have resulted from "nonaligned" status and from extensive trade with the West -- US and other Western aid, a wider variety and better quality of imported goods, a good bargaining position for trade with the Bloc, and the ability to sell "socialism" and expand trade in underdeveloped countries without the onus attached to membership in a "bloc."

It seems unlikely that Tito is willing to make any substantial changes in the Yugoslav economic system to accommodate the Russians, and he is deeply committed to an independent Yugoslav approach to Communism. Neither is it likely, however, that a Yugoslav retreat in these areas would be made a condition of closer relations with the USSR. Acceptance of the respectability of the Yugoslav approach by the Soviet Bloc and the avoidance of ideological attacks by both sides seem to constitute an adequate basis for closer economic relations.

Yugoslavia probably could increase substantially the share of the Soviet Bloc in its foreign trade above the relatively low level of recent years without risking its independence but not without some economic cost. If the increase in trade with the Bloc occurred at the expense of

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trade with the West, Yugoslavia would suffer a loss in the quality and diversity of its imports. The rapid expansion of trade with the West, as well as Western credits, has been an important stimulus to Yugoslav economic growth, which averaged 10 percent annually during 1957-61.

Moreover, a large expansion of trade with the Bloc would be difficult to achieve -- even if the regime wished it -- with present institutions, which permit Yugoslav enterprises to choose their markets. The preferences of Yugoslav buyers usually are for Western goods, at least with respect to manufactured goods. Bloc countries can promote trade with Yugoslavia by making more attractive goods available, but in many instances they are not in a good position to compete. Bloc exports of raw materials, however, generally do not suffer from a disadvantage. The Yugoslav regime can arrange for the equipment for centrally planned investment projects to come from the Bloc, even though Western equipment might be more profitable. Such an arrangement was made to expand the Zenica steel mill. The regime could also discriminate in favor of the Bloc by means of tariffs, quotas, or multiple exchange rates, but by so doing it would be retreating from the reforms of early 1961 and thus impairing its chances of receiving favorable treatment in the West.

In seeking a rapprochement with the Soviet Bloc, the Yugoslav regime probably will try to retain the influence its nonaligned status gives it among the underdeveloped countries of the Free World. So long as Yugoslavia is not regarded as an instrument of Soviet power, its influence, bolstered by a program of trade and aid for these underdeveloped countries, seems unlikely to be much affected by a rapprochement with the USSR.

3. Influence of Western Aid on Yugoslav Policy

The effects of possible expansion of Yugoslav economic relations with the USSR depend not only on the nature and extent of the measures taken but also on the reaction of Western countries, especially the reaction of those that have been sources of grants and credits. Tito no doubt realizes that at some point his foreign policy -- which increasingly seems like nonalignment against the West -- may lead the US to discontinue its aid

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program and to urge supporting action by Western European countries. An important volume of aid is at stake, including not only US deliveries of surplus wheat under Public Law 480 (valued at about \$90 million for the 1962/63 crop year), but sizable credits from Western Europe, including a \$78 million credit obtained from Italy last summer, another \$78 million credit obtained from a British consortium last November for construction of a steel works in Macedonia, and a \$30 million French commodity credit covering 1963-65. Yugoslavia's trade deficit with the US -- a rough measure of total US aid -- rose from \$50 million in 1960 (when US aid reached its low point) to \$145 million in 1961. The deficit during the first 9 months of 1962 was \$130 million.

Suspension of US aid at this time probably would soon have a serious effect on the level of Yugoslav food consumption. What the continuing effect might be is difficult to foresee, as it would depend on future harvests and Yugoslav success in importing grain from other sources. It is clear, however, that Bloc countries are in a poor position to replace Yugoslav imports of wheat from the US. US deliveries of grain to Yugoslavia under Public Law 480 -- the most important element of US aid -- declined substantially several years ago but have again become large. The grain deliveries scheduled for 1962/63 make up an estimated one-fourth of the average daily Yugoslav food consumption of about 2,900 calories per capita. The Yugoslav regime has wanted to dispense with these deliveries for some time and did succeed in reducing them to a low level in 1960 after the excellent harvest of 1959. Reduced grain harvests since 1959, however, have again impelled the regime to request large deliveries, as shown in the following tabulation:

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	<u>1958/59</u>	<u>1959/60</u>	<u>1960/61</u>	<u>1961/62</u>	<u>1962/63*</u>
Yugoslav production (thousand metric tons)					
Wheat, rye, and corn	6,641	11,065	9,963	7,910	8,000
Wheat and rye only	2,691	4,395	3,803	3,360	3,200
US deliveries of wheat under Public Law 480 (thousand metric tons)	838	241	148	942	1,400
US deliveries of wheat as a percent of Yugo- slav production					
Wheat, rye, and corn	13	2	1	12	18
Wheat and rye only	31	5	4	28	44

Unless grain production in 1963 recovers to something like the 1959 level, cancellation of US deliveries could cause an extremely difficult temporary situation for Tito. The weather so far during the 1962/63 crop year has not been particularly favorable, but much depends on crop conditions next spring and summer.

Western grants and credits to Yugoslavia have increasingly become a factor supporting an unusually high rate of investment and economic growth rather than emergency assistance facilitating the estrangement of Yugoslavia from the Soviet Bloc. The main long-term effect of loss or reduction of US assistance probably would be a significant lowering of the rate of growth unless substantial credits were obtained from Bloc countries.

* Preliminary figures for production and scheduled amount of US deliveries.

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Table 1

Yugoslav Foreign Trade with the USSR
1958-62

	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>Jan-Sep 1962</u>
Value of trade (million US \$)					
Turnover with the USSR <u>a/</u>	94	105	109	83	59
Imports from the USSR	58	58	57	32	38
Exports to the USSR	36	47	53	51	22
Deficit with the USSR <u>a/</u>	-21	-10	-4	<u>b/</u>	-16
Share of Yugoslav totals (percent)					
Turnover with the USSR	8.4	9.0	7.9	5.6	5.2
Imports from the USSR	8.4	8.4	6.9	3.5	5.6
Exports to the USSR	8.2	9.9	9.3	8.9	4.6
Deficit with the USSR	8.8	4.9	1.6	<u>b/</u>	7.8

a. Because of rounding, components may not add to the totals shown.

b. Yugoslavia had a trade surplus of \$19 million with the USSR but an over-all trade deficit of \$341 million.

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Table 2

Yugoslav Foreign Trade with the European Satellites
1958-62

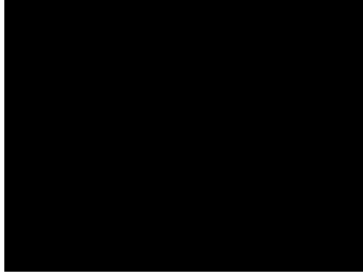
	<u>1958</u>	<u>1959</u>	<u>1960</u>	<u>1961</u>	<u>Jan-Sep 1962</u>
Value of trade (million US \$)					
Turnover with the European Satellites <u>a/</u>	221	212	283	262	183
Imports from the European Satellites	135	112	154	137	93
Exports to the European Satellites	86	99	129	125	90
Deficit with the European Satellites <u>a/</u>	-49	-12	-25	-12	-3
Share of Yugoslav totals (percent)					
Turnover with the European Satellites	19.6	18.2	20.3	17.7	15.9
Imports from the European Satellites	19.7	16.3	18.7	15.1	13.7
Exports to the European Satellites	19.5	20.9	22.8	21.9	19.0
Deficit with the European Satellites	2.0	5.9	9.6	3.7	1.5

a. Because of rounding, components may not add to the totals shown.

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