Impact of Trade Embargo with USSR on U.S. Economy

Background

The balance of trade with USSR is heavily in the U.S. favor -- with exports at least 3-4 times greater than imports consistently over the last four years.

United States exports to the USSR (which are dominated by agricultural products) declined sharply in 1980 due to the sanctions imposed by the Carter Administration following the Soviet invasion of Afghanistan. In 1981, exports rose sharply, mainly as a result of the lifting of the grain embargo. In the absence of USG restraints, it is expected that exports (particularly grains) would expand further, by a large amount in 1982. In the manufacturing sector, exports are concentrated in a few product categories (e.g. tractors, phosphate fertilizer, pressure sensitive tape), and a few U.S. companies (e.g. Occidential, International Harvester, Caterpillar).

The patterns of U.S. exports to the USSR contrasts sharply with those of our major Western allies -- for whom steel and machinery are the major export items. Thus, our allies are a much more important source of manufactures for the USSR and their manufacturing sectors have a much larger stake in the Soviet market.

United States imports from the USSR have been primarily minerals and metals, although in recent years ammonia and refined petroleum products have accounted for a substantially larger share. Imports have dropped significantly in volume in 1980 and 1981 largely due to a decline in gold purchases.

The attached tables provide data on recent U.S. trade with the USSR.

Impact of Total Embargo

The impact of an embargo on trade with the USSR is summarized by sector on the attached chart.

In total, we estimate that about $10 billion in export sales would be lost in 1982-83, with an accompanying loss of about 160,000 jobs. The impact on certain companies (e.g. Occidental and International Harvester) would be quite substantial.

Federal budget outlays for existing agricultural programs would increase by at least $6-8 billion and there would be pressure for additional or enhanced programs. Federal budget outlays and revenues would also be adversely affected by higher levels of unemployment. The Export-Import Bank would probably suffer a $180 million loss due to default on the Occidential contract.

Over the longer term, an embargo would cause loss of significant potential sales to the Soviet Union and to other countries and would encourage the spread of long term supply agreements in agricultural trade.

The attached paper by USDA describes the effects of an embargo in agriculture in detail.

Attachments

U.S. EXPORTS TO USSR
(Million dollars)

	1978	1979	1980	First Half 1981
Agricultural				
Yellow corn	1,053	1,402	602	387
Unmilled wheat	356	812	336	334
Inedible tallow	19	58	28	40
Soybeans	200	489	45	NA
Shelled almonds	NA	8	17	15
Sugar beets or cane	NA	NA	NA	11
Hops	NA	5	10	10
Subtotal of above	1,628	2,774	1,038	797
(as % of total)	72%	77%	69%	75%
Mineral				
Alumina	NA	NA	NA	8
Molybdenum ore	26	41	NA	8
Petroelum coke, calcined	18	14	20	21
Manufactures				
Tracklaying tractors & parts	NA	43	90	58
Other tractor parts	NA	2	10	15
Phosphoric acid	NA	93	17	14
Pressure sensitive tape	37	50	42	13
Parts for oil/gas drilling	28	28	NA	NA
Metal working machines, gear	NA	NA	NA	8
Belting & belts for machines	NA	2	13	8
Subtotal of above	65	218	172	116
(as % of total)	3%	6%	11%	11%
Total Exports	2,249	3,604	1,510	1,066
(above items as % of total)	77%	85%	81%	89%

U.S. IMPORTS FROM USSR
(Million dollars)

	1978	1979	1980	First Half 1981
Agricultural				
Sable furskins	8	9	6	3
Vodka	NA	NA	NA	3
Minerals/Metals				
Gold	286	548	86	18
Nickel	16	29	21	34
Palladium	28	62	54	18
Platinum metals	3	16	6	1
Chrome ore	7	11	4	2
Rhodium	8	9	6	2
Aluminum scrap	30	9	2	2
Metal coins	6	25	18	NA
Subtotal of above	384	709	197	77
(as % of total)	72%	81%	46%	35%
Manufactures				
Ammonia	27	56	95	40
Light fuel oils	NA	NA	NA	50
Napthas	NA	--	5	17
Total Imports	530	873	430	219
(above items as % of total)	79%	89%	70%	87%

SUMMARY OF IMPACT OF USSR TRADE EMBARGO
ON U.S. ECONOMY

SECTOR	IMPACT IN 1982-1983	LONGER TERM IMPACT
AGRICULTURE 1/	1 - Loss of $7 billion in export sales. 2 - Loss of over 100,000 jobs (and associated increased costs and revenue loss in federal budget). 3 - Increase in U.S. agricultural budget outlays by $6-8 billion. 4 - Higher costs for ammonia fertilizer, lower for phosphates. 5 - Depressed commodity price levels (to or below loan levels).	1 - Spread of long term trade arrangements. 2 - Foreign buyers will diversify away from U.S. sources due to loss of credibility of U.S. as supplier.
MANUFACTURES	1 - Loss of $3 billion in export sales and 60,000 jobs (and associated increased costs and revenue loss in federal budget). 2 - May well cause International Harvester to go bankrupt. 3 - Caterpillar would lose $200 million in sales and 1,000 jobs. 4 - Occidental would lose 1,600 jobs in phosphate industry and write off of possibly $60 million. 5 - Cut off of imports of mineral would cause increased costs to consuming industries (e.g. auto, specialty steel) seeking alternative supplies. 6 - Positive impact on U.S. ammonia industry. 7 - Loss to Export-Import Bank of $180 million (Occidental deal).	1 - Loss of substantial potential business (e.(pipelayers. 2 - Loss of reliability of U.S. as supplier would discourage other purchasers. 3 - Loss of $400 million/year for remaining 15 years of Occidental market.
SERVICES	1 - Loss of $50-80 million in revenues to shippers. 2 - Potential adverse effect of U.S. banks holding credits to Soviets.	

1/ Assumes embargo would apply to Eastern Europe and USSR and no new government programs to aid farmers (which could add several billion dollars in budget outlays).

SECRET

SOVIET/EASTERN BLOC EMBARGO - ISSUES AND IMPACTS

Summary

The potential gains to be derived from a trade embargo with the Soviet Union and the Eastern Bloc countries appear small relative to the costs the United States would suffer. Such efforts in the past have not influenced Soviet foreign policy, but have hurt our agricultural trade, disrupted commodity markets, depressed commodity prices, and cost the Treasury large sums. A trade embargo with the Soviet/Bloc countries should not even be considered without first imposing a full embargo on credit from the West.

While in years of poor harvests the Soviets account for a large share of the world's wheat and coarse grain imports (nearly a fifth in 1981/82), their overall imports (nonagricultural and agricultural) make up only 3.3 percent of their GNP. Because half the Soviet's overall imports come from the Eastern European countries, any trade embargo action taken by the United States and its allies would have to also include Eastern Europe to prevent transshipment. Such an action would depress prices for farm commodities in this country because over 70 percent of our exports to the Soviet Union and Eastern Europe are agricultural products.

Our agricultural export sales to the USSR and Eastern Europe are projected to total about $4.8 billion in 1981/82. If the action were imposed immediately and across the board, agricultural export earnings would fall by over $2 billion in fiscal 1982, further aggravating the U.S. trade deficit and the position of the dollar internationally. We estimate it would cost the federal government $2-3 billion for 1981/82 to absorb the commodities that would otherwise have been exported. The reduction in exports would also mean the loss of over 100,000 jobs throughout the economy. In addition to making commodity loans to farmers, we would have to subsidize their storage and interest costs. Thus, the export-based underpinning of American farm income would be seriously weakened by an embargo. To compensate, it would cost the U.S. government more in price support and related outlays than the value of the exports lost due to the embargo. The whole structure of farm prices--including agricultural commodities not now exported to the Soviet Union and the Eastern Bloc--would shift downward.

The impact of continuing an embargo into 1982/83 is even more damaging to agriculture and related industries. We project agricultural exports would decline by over $5 billion in 1982/83. Commodity prices would fall at or below loan levels, increasing deficiency payments for grains and raising loan and reserve outlays sharply. Budget outlays for grains alone in 1982/83 would total $4-5 billion above levels expected in the absence of an embargo.

To limit taxpayer sacrifices in continuing to absorb the surpluses, the U.S. government would be forced into massive and costly acreage reduction programs. These programs would disrupt markets and impact on nearly all sectors of the U.S. economy: employment in industries supplying farm inputs would fall; rural communities would suffer as the volume of U.S. farm output declined; and gross farm income would fall. The longer the embargo were to continue, the more severe would become the dislocations.

U.S. agriculture's ability to produce would also be impaired by a total trade embargo. The Soviet Union and Eastern Europe account for 30 percent of

the world's nitrogen fertilizer production capacity. In 1980/81, the Soviet Union alone supplied the United States with half of its imported ammonia.

Coverage

If an embargo of only agricultural products were imposed, the Agriculture and Food Act of 1981 would require that the Secretary take steps to assure farmers of 100 percent of parity. It is important to note that in addition to grains, the U.S. also exports oilseeds, tallow, sugar, cattle hides, meats, animals, tobacco, etc. to the USSR and Bloc countries. Hence, there would be tremendous economic disruptions.

Implementation

In order to minimize disruptions to farm commodity markets, we recommend that exporters be allowed to deliver on contracts already written for shipment in 1981/82. Thus, about half of the grain and other agricultural products projected to be exported to the USSR and EE would still move. This would still imply about a 10-15 percent reduction in total U.S. grain exports for 1981/82.

Impacts on Agriculture and the Budget

With farm prices and incomes already depressed, an embargo would have a devastating effect in agriculture and related industries. The reduction in exports would mean the loss of over 100,000 jobs throughout the economy. The embargo would eliminate any opportunity for price strengthening in 1981/82 and would lead to a tremendous increase in loan and inventory outlays as well as a significant buildup in reserves. Unless offsetting actions were taken, corn prices would drop and average for the season near loan rate levels, about 10-15 cents per bushel below earlier expectations. Wheat prices would also be pushed near loan rate levels, about 50 to 60 cents per bushel below earlier projections. This would result in large additional movements of grain under government loan and into the farmer-owned reserve with additional budget outlays around $2 billion for these commodities alone.

A continuation of the embargo into 1982/83 would mean a reduction of nearly 25 percent in grain exports, with farm prices for grain averaging at or below the reserve loan rates. Soybean exports and prices would be similarly affected. Movement of this volume of grain into loan and reserve programs would result in twice as much grain in the reserve than earlier expected and budget outlays of about $4 to $5 billion. These increased outlays do not include the costs of any additional offsetting actions, such as contract purchases, direct grain purchases, paid land diversion programs, or higher support rates designed to minimize impacts on the sector as a whole.

Effectiveness of an Embargo

It is very difficult to get exporters to cooperate in a trade embargo. It would be particularly difficult in this case because of the linkage between Western Europe and the Eastern Bloc countries. West Germany is a major supplier, particularly of credit, to the Bloc. Moreover, our experience in managing embargoes has not been good. Mechanisms do not exist for making such actions effective. Reports by GAO and USDA's Inspector General conclude that the 1980 embargo with the USSR was virtually ineffective.

Longer Term Impacts

The longer an embargo is allowed to stay in effect, the greater the problems that would emerge. Pressure for the government to take compensating actions on agricultural commodity prices would rise. Even then, any further actions to help farmers would have to be coordinated with the other supplying nations. The longer the embargo remains in effect, the more the exporters would be tempted to circumvent the embargo and thereby undermine the intent of the action. Irrespective of the duration of the embargo, the United States would find its foreign markets seriously eroded. Other suppliers and the Soviets would attempt to write bilateral agreements in order to tie up future trade to their advantage. Other importing countries, including our major trading partners, would also try to tie up and diversify the sources of their future requirements in formal agreements. Following the 1980 embargo, roughly 30 percent of the world's grain trade was estimated to be locked up by other exporting countries in the form of bilateral agreements, a sharp increase from the pre-embargo level.