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It is an honor for me to be here before you tonight as a substitute for Bill Casey who sends his regrets and who cannot be here because of the press of business which keeps him in Washington tonight.

An important cause of Bill's absence is the change that is taking place in the leadership of several key nations. In an age in which bureaucracies seem to have taken over, the personalities of leaders are still important. We recognize this in our selection of presidents and it is true elsewhere. And foreign leaders have been changing rapidly: Andropov has replaced Brezhnev, Kohl has succeeded Schmidt; someone will replace Suzuki.

The most important of these leadership changes is that in the Soviet Union. This change has long been anticipated, yet because of the absence of an organized procedure for the devolution of power in that society, the transfer of political power there is an uncertain business. It seems to have been accomplished this time, however, with remarkable speed and assuredness. It is likely to produce a strong leadership.

This outcome, if it in fact sticks, will offer both challenges and opportunities. These will derive from the underlying realities that face the new Soviet leader and that face us as well.

The most salient of these facts is first the success of the Soviet Union in carrying out the greatest military buildup in history and the projection of this power abroad directly or through proxies throughout Africa, to the edges of Asia, and to the Western Hemisphere. Second, and equally important, is the fact that this power rests on an economic system which is in deep -- and deepening -- trouble and getting worse.

First on the new leadership.

It is a remarkable thing that in the 65-year history of the Soviet Union this is only the fourth time that supreme power has passed and only the second time that there has been anything approaching the deliberate selection of a new leader. When Lenin died it was clearly foreordained, despite his warnings against Stalin, that as the Secretary General of the Communist Party he had gathered the essential elements of power in his own hands. When Stalin died, there was a competitive process lasting some weeks, which produced a triumvirate. It took some two years for Khrushchev to gather supreme power in his own hands. Then, when he misplayed his hand, Brezhnev displaced him. And now, Yuri Andropov has arrived to replace Brezhnev in a transition which is presented as an orderly one, although we have only limited comprehension of the struggle for succession which took place during Brezhnev's long twilight.

There are three sets of circumstances which we need to fully understand in order to have a realistic perception of what we can expect of General Secretary Andropov.

The first of these is his history. He is no stranger. He first surfaced as Ambassador in Hungary in 1956 and played a key role in suppressing the brave Hungarian people's effort to regain their freedom. Performance there earned him a title -- "The Butcher of Hungary." Later he spent fifteen years running the dreaded and all powerful KGB, vastly expanding both its capacities throughout the world and the subtlety and force with which it controlled, indeed, crushed internal dissent. It was, significantly, under his leadership that psychiatry was perverted to the disposition of troublesome dissidents. Moreover, he came to power supported by two of the most threatening elements of the Soviet state, the military and the Secret Police.

Those forces have been dominant in Soviet society for a long time. Since at least the Cuban missile crisis, while engaging us in a so-called detente and a series of arms limitation talks, the Soviets steadily increased Soviet strategic and conventional power while we either stood still or lost ground until today the Soviets make claim to military superiority and are widely and generally accorded no less than parity. A combination of growing military power and active intervention abroad has brought Soviet arms and Cuban troops to far away Angola and Ethiopia, and has brought Soviet troops into Afghanistan.

Any realistic hopes that detente with the Soviet Union might survive practically disappear with these developments and vanishes when a genuine workers' revolt occurred in the Soviet empire and was met with repression. The cry, "Workers of the world unite," makes the leaders in the Kremlin tremble. They fear that it might even happen in Russia.

The military power which the Soviet leadership has at its disposal is formidable. I will spare you the details. It is sufficient to say that the Soviets have built a strong nuclear weapons establishment rivaling our own and, indeed, one that has been on a faster track. It has created a modern nuclear threat to Europe and other peripheral areas with its SS-20 missiles among other weapons. It has fielded an armed force opposite Western Europe which is large, modern and growing. Its navy has moved from coastal defense to a capacity to roam the seas. And it has, in addition, built up a powerful force opposite China.

Whatever else can be said of Brezhnev, he cannot be faulted for having left the Soviet Union militarily weaker than he found it.

This is not to say that Andropov inherits a comfortable situation. Despite the lagging defense efforts of the United States and its allies, we remain formidable. I believe that Andropov or anybody else would have to think many times and weigh the potential consequences and dangers very carefully before risking the response which the NATO powers can make. The main question before us is not who would survive or would win in a conflict in which there would probably be only losers, but how we can seize the opportunity which now presents itself to defuse risks and mitigate threats.

The main bases for optimism are the problems which Andropov inherits. Soviet agriculture has suffered crop failures in four successive years and is unable to feed itself; Soviet society suffers from declining health with alcohol addiction running rampant; corruption is massive and reaches to the top of the system; there is a suppressed but growing dissidence; ethnic conflicts are likely to be intensified in the years ahead.

The key to the drive for military power has been the ability of the Soviet economy to provide small but steady improvements to the standard of living. Until recently, the Russian economy provided enough additional butter to support the acquisition of more and more guns.

We now recognize that an important element in Moscow's ability to keep this strategy alive through the 1970s was help from the West, in the form of credits to buy equipment, technology, and food. In addition, the Russians helped themselves by acquiring Western technology through espionage, and by earning hard currency through exports of oil, arms and gold.

The Soviet economy is now in a period during which annual growth rates will be in the 1 percent to 1.5 percent range at best. Shortages of oil and declining rates of labor productivity are major causes of this declining performance. Due to low birth rates during the 1960s among ethnic Russians and other Slavs, the Soviet Union now has a shortage of workers in key regions. During this decade, the work force in the Russian Republic -- which accounts for 60 percent of the country's total industrial output and 75 percent of total military output -- will shrink by 1,300,000.

It is in large part to compensate for this shrinkage in the work force that the Russians have turned to Western equipment and technology. Their need for our equipment and technology is greater now than it was during the heyday of detente. But their ability to import equipment and technology is declining rapidly due to a shortage of hard currency:

- a. Oil prices are dropping.
- b. Gold prices are low (due, in part, to heavy Soviet selling).
- c. The market for Soviet arms is softening.
- d. Western banks are increasingly reluctant to extend credit to the Soviet Union -- or its satellites.
- e. Four consecutive poor harvests have forced the Russians to divert billions of dollars from equipment and technology purchases to gain.

But despite this, military expenditures continue to grow. Since 1965, the growth in Soviet defense spending in ruble terms has averaged about 4 percent a year -- about the same as that for the overall economy. By now, the share of GNP for defense is 13-14 percent. Given current and future economic conditions, maintaining historical rates of growth in defense spending will be economically and politically more difficult. Nevertheless, we expect that Soviet defense spending will continue to grow. If so, the defense share of GNP would increase to at least 15 percent in 1985 and could approach 20 percent by the end of the decade. In short, it's difficult to see how Moscow can continue its arms buildup without strangling its economy unless it can get help from the West.

For Kremlin leaders, the trick will be to keep the old strategy going for a while longer by finding enough money to support growing -- or even current -- levels of defense spending while fending off disaster in the civilian sectors. One option would be to order a tightening of belts, using more police power if necessary to keep the lid from blowing. A second option would be to "starve" the satellites to help the Motherland, for instance by reducing subsidies the Soviet Union now provides to Eastern Europe by selling oil at roughly half the world market price. Another would be to find alternate sources of hard currency. These might include:

- a. Credits from new lenders, such as Mid-East governments.
- b. Increased exports of raw materials including natural gas, minerals, and increased exports of chemicals.
- c. Gain access to wealth without spending hard currency through a Soviet drive politically, economically or militarily toward the Persian Gulf.

Kremlin leaders have not confronted this issue squarely and adopting a coherent, comprehensive response. Andropov is the first Soviet leader to take power at a time when his country is, arguably, the world's number one military power. If US will is perceived as weak, the ability of Moscow to intimidate is enhanced. Mid-East's governments might respond to Soviet threats by extending credits at low rates of interest -- or by selling oil to the Soviet Union and its satellites at sweetheart prices.

Only Russian nationalism and military power provides the cohesion necessary to hold this society together. These forces have been challenged in Eastern Europe and may be inadequate in the future in the Moslem and other disparate parts of the Soviet empire. Around the world, in Poland, in Cuba, in Vietnam, the Communists' system is a failure and is maintained only through the use of force. The western system of freedom of political choice and freedom of market has proven its superiority.

What the Soviet system needs is clear: Above all, it needs to be freed from the dead weight of the central controllers. It needs to be decentralized, to allow managers real authority in making decision, to allow prices to influence consuming and manufacturing decisions, to allow individual farmers (or at least small groups) to make crucial choices in the countryside. And so on. Will Andropov move in this direction? How much freedom of action will he have? We don't know. Nor, in all probability, does he.

If he does not move, or move much, in these directions, we think we know what will happen; nothing economically. The system is stagnant. Only market-type reforms will enable it to get on a higher growth path. Yet such reforms are resisted because they can occur only with the loss of power of local political and bureaucratic cadres. These cadres were central in the Brezhnev era and they are also important to Andropov. If he wants to move the system out of the doldrums, he has to weaken their power and yet they, together with the military, are crucial to the maintenance of the system.

The only other important option for economic improvement open to Andropov, one that is less promising in its effects but one that may appear less risky, is to undertake to get help from the West. The Soviets have been here before -- as have we. The basis for East-West detente in the early 1970s. was economic interaction, indeed support, for the Soviet Union in exchange for Soviet restraint on arms and foreign adventures. It foundered on the Soviet's unwillingness to adhere to their side of the bargain. Now a decade later, Andropov inherits an internal situation which is even worse than Brezhnev faced.

Therefore we can expect to hear voices calling for a softer line, more trade and credit to encourage and strengthen those in the Kremlin inclined to pursue economic and social goals rather than military and imperialist ones, and far less effort to redress our own defense deficiencies. Yet we do not know that there is a peace party in the Kremlin or, if there is one, that it has any clout. We do know that Andropov came to power with the support of the military and the secret police. It is not unreasonable to expect that he and his colleagues might hope to get that which they tried to get and didn't quite bring

off in the 1970s: both sustained Western economic benefits and sustained deterrance of Soviet imperial power. In this situation, it's just as likely that any reassurances we offer about possibilities for peaceful cooperation would be perceived as signs of weakness and lack of resolve or taken as an opportunity to lull us into complacency and create renewed opportunity for extending military superiority. The best way to strengthen any possible doves in the Kremlin is to reaffirm western will and capability to react promptly to make any Soviet adventurism dangerous.

We have a policy and the President reaffirmed it after Brezhnev's demise. It is to seek conciliation from a position of firmness and strength. It is to seek reduction in the armaments that threaten all of us. It is not to subsidize or to make our technology available to those who threaten us but to be open to trade on market terms. We have begun during the last year initiatives in arms control. President Reagan has outlined our approach to four important items -- negotiations between the United States and the Soviet Union on intermediate-range nuclear weapons, known as INF, and those on strategic nuclear arms reductions, known as START; the negotiations on mutual and balanced reductions of conventional forces in Europe, and the continuing process of discussion and negotiation stemming from the Final Act of the Helsinki Conference on Security and Cooperation in Europe. In addition, the United States is trying to prevent the spread of nuclear weapons; to eliminate the menace of chemical weapons (a case in which the Soviet Union is a clear violator of international agreements); to study the possibility of imposing further limits on the military use of outer space; and to develop new measures to minimize the risks of war by miscalculation.

How did the present situation arise? Over a period of more than 25 years the Soviet Union claimed immunity from the Charter rules against aggression, and the rest of the world tacitly accepted its claim. That course is no longer tolerable. Soviet expansion and the Soviet Union's growing military power threatens the international system. That system cannot continue to accept the Soviet practice of aggression through the use of its own forces and those of its proxies and satellites, whether organized as armies, guerrillas, armed bands, or terrorists, backed by the implicit threat of its growing nuclear forces. During the 1970s, a period when the United States nuclear arsenal was held relatively stable, the Soviet Union expanded its nuclear forces far beyond any conceivable requirements for deterrence and defense. We must give priority to our security and to that of other democratic nations in the world.

Having said all of this, I do not want to end on too pessimistic a note. With our European allies, our basic congruence in values dominates our occasional differences. We have been through a period of difficulty and largely as a result of Secretary Schultz' efforts we have reached an agreement on a better approach to our economic relations with the Soviet Union. Perhaps the new Soviet leadership will recognize that its interests lie in reducing the level of arms and in improving the material welfare of its people. We will be more than willing to join in reciprocal arms reductions efforts. And, if the new leadership elects to tend to its own affairs at home and to interfere less in the affairs of others, it would no doubt also find the path open to wider and mutually beneficial economic relations with the West.

All of these good things can happen; we need to keep our minds
alive to these possibilities. Meanwhile, let us keep our powder dry.