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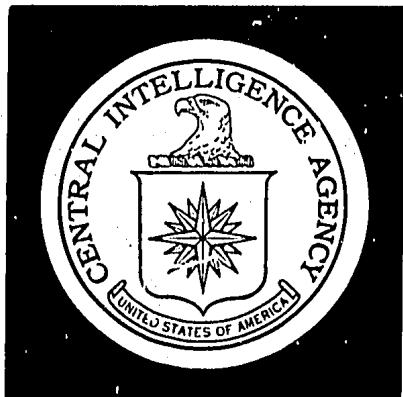

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**DIRECTORATE OF
INTELLIGENCE**

Intelligence Memorandum

Recent Developments In Soviet Hard Currency Payments

Secret

ER IM 71-127
July 1971

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CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
July 1971

INTELLIGENCE MEMORANDUM

RECENT DEVELOPMENTS IN SOVIET
HARD CURRENCY PAYMENTS

Introduction

1. The USSR attaches considerable importance to its hard currency position because of its need to import Western equipment and technology to modernize Soviet industry and to buy other items in short supply that can be obtained only by spending hard currency. This memorandum briefly describes developments in the Soviet trade and payments position with convertible currency countries during 1970 and probable trends in 1971.

Discussion

Merchandise Trade

2. The USSR incurred a hard currency trade deficit of \$500 million in 1970 (see Table 1), the largest since 1964, when the Soviet Union was buying large quantities of Western wheat. Soviet imports from hard currency countries rose by about \$270 million - less than the 1968-69 average increase of approximately \$410 million - but exports increased less than \$100 million, the poorest export performance since 1964.

3. The deterioration in the Soviet hard currency trade balance stemmed from a sharp increase in imports from overseas countries. As Table 2 indicates, the deficit with these countries increased more than \$190 million, continuing last year's trend. In 1970 the Soviet deficit in trade with Canada increased by more than \$100 million (wheat) and with Australia by \$20 million (meat). The Soviet surplus with Japan fell by \$60 million because of sharply increased imports of machinery and other

Note: This memorandum was prepared by the Office of Economic Research.

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Table 1
Soviet Hard Currency Trade

Million US \$			
<u>Year</u>	<u>Exports</u>	<u>Imports</u>	<u>Balance</u>
1960	744	1,017	-273
1961	866	1,060	-194
1962	917	1,181	-264
1963	960	1,278	-318
1964	1,011	1,545	-534
1965	1,326	1,544	-218
1966	1,482	1,746	-264
1967	1,691	1,600	+91
1968	1,893	1,988	-95
1969	2,105	2,425	-320
1970	2,196	2,696	-500

manufactured goods. The deficit with Malaysia remained roughly the same, as the USSR continued large purchases of natural rubber. The tabulation below shows Soviet trade with selected overseas countries in 1969 and 1970:

<u>Country</u>	Million US \$					
	1969			1970		
	<u>Ex-ports</u>	<u>Im-ports</u>	<u>Bal-ance</u>	<u>Ex-ports</u>	<u>Im-ports</u>	<u>Bal-ance</u>
Canada	12	33	-21	8	131	-123
United States	61	117	-56	64	115	-51
Australia	2	45	-43	2	67	-65
Japan	357	264	+93	379	345	+34
Malaysia	2	122	-120	2	123	-121

4. There was little change in the balance of hard currency trade with Western Europe, contrary to the experience of recent years when imports rose substantially. In 1970, imports were up only \$75 million over those of 1969 as against an average of more than \$300 million in each of the previous two years. Export growth fell off to \$85 million in 1970 as against \$150 million annually in 1968-69. The USSR increased somewhat its already significant favorable balance with the United Kingdom, and

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Table 2

Distribution of Soviet Hard Currency Trade
with Western Europe and Overseas Countries

Million US \$			
<u>Geographic Area</u>	<u>Exports</u>	<u>Imports</u>	<u>Balance</u>
1967			
Western Europe	1,163	1,015	+148
Overseas areas	528	585	-57
Total	<u>1,691</u>	<u>1,600</u>	<u>+91</u>
1968			
Western Europe	1,282	1,363	-81
Overseas areas	611	625	-14
Total	<u>1,893</u>	<u>1,988</u>	<u>-95</u>
1969			
Western Europe	1,462	1,622	-160
Overseas areas	643	803	-160
Total	<u>2,105</u>	<u>2,425</u>	<u>-320</u>
1970			
Western Europe	1,547	1,696	-149
Overseas areas	649	1,000	-351
Total	<u>2,196</u>	<u>2,696</u>	<u>-500</u>

continued its large deficits with France, West Germany, and Italy, as shown in the following tabulation:

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<u>Country</u>	<u>Million US \$</u>					
	<u>1969</u>			<u>1970</u>		
	<u>Ex-ports</u>	<u>Im-ports</u>	<u>Bal-ance</u>	<u>Ex-ports</u>	<u>Im-ports</u>	<u>Bal-ance</u>
United Kingdom	427	240	+187	465	248	+217
France	141	323	-182	140	319	-179
West Germany	229	350	-121	257	375	-118
Italy	232	317	-85	212	313	-101
Sweden	108	129	-21	117	144	-27

5. Few data are available yet on the commodity movements underlying the 1970 trade figures. On the export side, it is estimated that oil exports rose by about \$20 million to a total of \$360 million, in part reflecting a rise in exports of oil products to Japan. Exports of logs to Japan were also up over those of 1969. Similarly, lumber and other wood products were exported to the United Kingdom in larger quantities than in 1969. Exports of diamonds and platinum fell off somewhat in 1970 as a result of slackening Free World demand.

6. Leading the growth in imports were food (wheat and meat) from Canada and Australia and pipe from West Germany. Imports of machinery and equipment apparently stayed at about the \$1 billion level in 1970. Imports of plant and equipment from West Germany, France, and the United Kingdom declined, but imports from Japan apparently increased substantially.

Nonmerchandise Elements

7. Developments in the nonmerchandise elements of the Soviet current account with convertible currency countries produced no major changes in 1970. Net revenues from transportation increased from \$10 million to an estimated \$35 million in 1970. (For Soviet balance of payments, see Table 3.) Net receipts from tourism rose by \$7 million to an estimated level of \$63 million. These receipts plus miscellaneous earnings of some \$8 million offset interest (\$69 million) and other payments. The net current account deficit was thus somewhat smaller than the trade deficit but, like the trade deficit, was substantially larger than in 1969.

8. The hard currency deficit again was financed largely through the use of Western credit. Drawings on medium-term and long-term credits used to finance many of the producer goods (machinery, equipment, and pipe) imported from the West were estimated at about \$730 million for 1970 --

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Table 3

Estimated Soviet Balance of Payments
with the Free World in Hard Currency

	Million US \$			
	1969		1970 ^{a/}	
	<u>Credit</u>	<u>Debit</u>	<u>Credit</u>	<u>Debit</u>
Goods and services		<u>298</u>		<u>463</u>
Merchandise, f.o.b. <u>b/</u>	2,109	2,422	2,196	2,696
Transportation, net <u>c/</u>	10		35	
Travel <u>d/</u>	71	15	79	16
Interest payments on credits <u>e/</u>		59		69
Dividends received <u>f/</u>	8		8	
Other services				
Professional services, net <u>g/</u>		N.A.		N.A.
Miscellaneous, net <u>h/</u>		N.A.		N.A.
Transfer payments		<u>41</u>		<u>46</u>
Contributions to international organizations <u>i/</u>		41		46
Personal remittances <u>j/</u>	N.A.		N.A.	
Student grants <u>k/</u>		N.A.		N.A.
Capital and monetary gold	<u>340</u>		<u>524</u>	
Medium-term and long-term credits				
Supplier credits and tied loans <u>l/</u>	525	248	730	291
Other loans <u>m/</u>				
Compensation payments <u>n/</u>		10		10
Hard currency repayments on credits to less developed countries <u>o/</u>	73		90	
Monetary gold <u>p/</u>	Negl.		5	
Net errors and omissions <u>q/</u>		<u>1</u>		<u>15</u>

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Table 3

Estimated Soviet Balance of Payments
with the Free World in Hard Currency
(Continued)

-
- a. Preliminary.
- b. Official Soviet statistics adjusted to exclude estimated Soviet deliveries of goods and services to hard currency countries under economic aid agreements as well as goods received by the USSR as repayment and interest.
- c. Estimates for net transportation are for ocean transportation only. Soviet expenditures and receipts from transportation of foreign trade freight by land are believed to be more or less offsetting.
- d. The number of Free World visitors is from official Soviet sources, except for 1970 which is estimated at 735,000. No firm information is available on earnings from tourism, but average cost per stay per Free World visitor from different areas has been estimated. Expenditures of Soviet tourists in Free World countries are estimated on the basis of very little information.
- e. Interest payments are those made on medium-term and long-term credits obtained from Western countries mainly to finance machinery and equipment imports. Interest payments and receipts for short-term loans are not included.
- f. Dividends received include profits of Soviet-owned banks, insurance companies, and other enterprises in the West.
- g. Professional services refer principally to the cost of technical services received in connection with the installation of facilities imported from the West.
- h. This category includes receipts and payments for political and economic representation. Expenditures for Soviet representation abroad are in excess of receipts from foreign representatives in the USSR, but no reasonable estimate can be made.
- i. Payments made in hard currency to the UN and UN-affiliated organizations.
- j. Personal remittances include gift packages and cash sent to Soviet citizens by persons abroad.
- k. No data are available on the value of Soviet government grants to foreign students (chiefly from less developed countries of the Free World) in the USSR. Hard currency expenditures are largely for the transport of the students to and from the USSR in those instances where Soviet carriers are not used.

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Table 3

Estimated Soviet Balance of Payments
with the Free World in Hard Currency
(Continued)

- l. Estimates of drawings and repayments on medium-term and long-term supplier credits and on lines of credit tied to Soviet purchases in the countries extending the credit are based on the details of contracts between Soviet foreign trade organizations and Western suppliers and banks, on Soviet imports of machinery and equipment, and on other information.*
- m. The 1946 loan from Sweden was repaid in 1967.*
- n. Compensation payments are Soviet payments of principal and interest in accordance with the US lend-lease "pipeline" agreement.*
- o. Military credit agreements between the USSR and some less developed countries such as Iraq, Syria, Indonesia, and Uganda provide for repayment in hard currency. This provision is not always honored, and estimates of what is actually paid are highly tentative. Hard currency repayments on economic aid have been added to these estimates.*
- p. These are minimum estimates of Soviet gold sales based on the date that the Soviet gold is delivered to the buyer, rather than the date of the sale agreement. Sales of gold for industrial purposes are included.*
- q. Including changes in hard currency holdings and short-term capital movements.*

about \$200 million more than in 1969. Scheduled repayments and interest rose by about \$50 million. Thus, net credits received amounted to approximately \$370 million compared to about \$220 million in 1969. Outstanding Soviet debt in convertible currency rose by about \$440 million to a total of about \$1.6 billion. Short-term credit facilities were also employed to finance Soviet hard currency transactions, although a meaningful numerical balance on this aspect of financing is lacking. The USSR, however, has been a net short-term borrower in recent years, particularly on the Eurodollar market, and apparently remained so in 1970.

9. In spite of the larger deficit, the USSR sold almost no gold in 1970, a policy it has pursued for the past five years -- there was only one recorded sale, about \$5 million, to the West. Gold production in 1970 was estimated at \$230 million and domestic consumption of gold at about \$45 million. We estimate that the USSR added about \$180 million to its

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bullion reserves. At the close of 1970, such reserves were estimated to have reached about \$1.8 billion.

Prospects for 1971

10. The growth of imports from convertible currency areas is expected to slow somewhat in 1971 largely because of a decline in the value of Soviet contracts concluded in 1969 and early 1970 with Western suppliers of plant and equipment. Accordingly, imports of plant and equipment will decline somewhat. ^{1/} Imports of pipe, on the other hand, will rise perhaps by as much as \$50 million. Imports of wheat (\$130-\$150 million) will be little more than the 1970 level, and meat imports will be about the same. The growth of Soviet exports to hard currency countries probably will not increase in 1971, although it is too early to judge on the basis of available data. Increased prices for Soviet oil will generate additional revenue if price increases are not offset by a decline in volume. Sales of platinum and diamonds continue to be sluggish, and there are no noteworthy increases anticipated in exports of traditional export commodities such as lumber, coal, cotton, grain, and furs.

11. No significant changes are anticipated in the nonmerchandise elements of the Soviet hard currency balance of payments. Revenues from tourism and transportation should continue to increase and will offset interest and other payments. On balance, it is anticipated that both the merchandise trade deficit and the current account deficit will be smaller than in 1970. Western credit will again play a major role in financing the deficit, and perhaps gold will assume a greater role. The USSR has already sold about \$20 million in gold on the free market in 1971. The Soviet leadership may now feel less constrained to withhold gold from international bullion markets if it believes that current reserves of \$1.8 billion are adequate for unforeseen contingencies. Some \$200 million in gold could be sold annually without reducing reserves. Moreover, the level of medium-term and long-term indebtedness to the West has increased to the point where the USSR may now feel it necessary to finance part of its hard currency deficit by selling gold. Gold sales might also be necessary to settle short-term obligations and to help client states in Eastern Europe (the USSR loaned \$100 million in hard currency to Poland early this year).

1. *There has been a substantial pickup in the value of contracts concluded since mid-1970. A large volume of automotive machine tools, which will include equipment for the Kama River project yet to be awarded, will be reflected in 1972 imports and those of subsequent years.*

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12. The Soviet hard currency trade deficit of \$500 million in 1970 was the largest since 1964, reflecting in large part the smallest rate of annual increase in exports since that time. The growth of exports was about one-third the size of the increment in imports. A substantial increase in imports from Canada and Japan was the principal element of growth in imports. Soviet trade with Western Europe increased very little, with exports and imports rising at about the same rate. Changes in the nonmerchandise elements of the Soviet hard currency current account were minor, but they produced a net surplus as a class.

13. The deficit was again covered largely by Western credit. Net medium-term and long-term credits received rose by about \$150 million to a level of \$370 million and increased Soviet outstanding indebtedness to the West to about \$1.6 billion. The USSR sold very little gold, thus continuing its policy of building up its bullion reserves, estimated to have reached \$1.8 billion at the end of 1970.

14. The Soviet hard currency deficit is expected to diminish in 1971 largely because the growth of imports will probably decline. In spite of an anticipated decline in the deficit in 1971, some Soviet gold has been sold, contrary to the Soviet practice of the last five years. The Soviet leadership may now feel that gold reserves are adequate to take care of unforeseen contingencies, thus permitting the sale of up to \$200 million in gold annually should Soviet authorities need the additional convertible currency to finance foreign trade plans.