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Quarterly Bulletin on Soviet Economic Growth



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Annual Edition 1985

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*SOV SEG 86-001
April 1986*

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Quarterly Bulletin on Soviet Economic Growth [Redacted]

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Annual Edition 1985

This bulletin was prepared by [Redacted]
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Comments and queries are welcome and may be
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**Quarterly Bulletin on
Soviet Economic Growth**

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Preface

*Information available
as of 1 April 1986
was used in this report.*

Because we have shifted the price base for our measures of Soviet economic performance from 1970 to 1982, the estimates of gross national product (GNP) and its several components presented in this paper differ from our previous estimates. The move to a more recent price base culminates a three-year research effort and allows us, we believe, to give a more accurate assessment of the resources associated with Soviet production. Although the basic trends have not changed, the use of 1982 prices has resulted in somewhat different estimates of historical growth rates for the Soviet economy, as well as the share of GNP devoted to consumption, investment, and defense. These findings are discussed in more detail in the appendix.

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Contents

	<i>Page</i>
Preface	iii
The Soviet Economy in 1985: A Year of Transition (foldout)	vii
Introduction	1
Performance in 1985	1
Industry Recovers	2
Industrial Materials	3
Energy	4
Machinery	5
Consumer Nondurables	5
Transportation Rebounds	5
Agriculture Disappoints	6
Hard Currency Trade Deteriorates	7
Resource Policy Trends	8
Higher Priority for Investment	9
Mixed Results for the Consumer	9
Slow Defense Growth	10

Appendix

Revised Estimates of Soviet GNP	13
Nature of the Revision	13
Results of the Revision	14
Impact on Estimates of Defense Spending	14

Tables

1.	USSR: Growth of GNP and Selected Sectors of the Economy	1
2.	USSR: Industrial Growth by Branch	3
3.	USSR: Growth in Industrial Output and Factor Productivity in 1981-85	4
4.	USSR: Growth in Energy Production	5
5.	USSR: Freight Turnover by Transport Mode	6
6.	USSR: Growth of Farm Output	7
7.	USSR: Total Trade, 1981-85	8

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25X1

		<i>Page</i>
8.	USSR: Indicators of Capital Formation Growth	9
9.	USSR: Growth in Per Capita Consumption	10
10.	USSR: Comparison of Average Annual GNP Growth at Factor Cost in 1970 and 1982 Prices	14
11.	USSR: Shares of GNP by Sector of Origin at Factor Cost, 1982	14

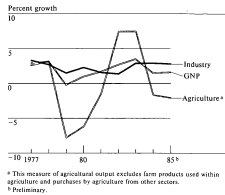
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**The Soviet Economy in 1985:
A Year of Transition**

A. Economic Performance Mixed

Shrinking farm output held GNP growth to about 1½ percent for the second straight year. Meanwhile, nonfarm output rose by roughly 2½ percent.

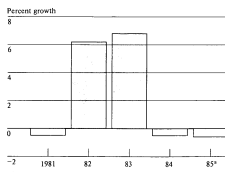
Since he became General Secretary in March 1985, Mikhail Gorbachev has announced an ambitious strategy for modernizing the economy through massive replacement of outdated plants and equipment and an emphasis on high-technology industries. As Gorbachev was putting forward his blueprint for the latter part of the 1980s, however, the economy was turning in another lackluster performance. Nevertheless, he could take some satisfaction from the 1985 results. Through a combination of factors, a year that started out very badly became at least respectable. After a poor first quarter, industry and transportation made strong recoveries. Improved weather, after the severe winter, eased pressures throughout the economy. (A similar situation during 1982, when harsh weather also disrupted production, did not result in nearly the same turnaround.)



* This measure for agricultural output excludes farm products used within agriculture and purchases by agriculture from other sectors.
* Preliminary.

D. Agriculture Disappoints

While industry posted a relatively good showing, Soviet farm output shrank for the second year in a row as production (net of feed, seed, and waste) declined by about ½ percent in 1985. An improved grain harvest estimated at 200 million tons allowed Moscow to pare grain imports substantially in the second half of the year and contributed to slightly larger output of meat, milk, and eggs. Poor crops of potatoes, sugar beets, and vegetables, and declines in livestock numbers, however, more than offset these gains. Disease and insect infestation hurt the sugar beet and vegetable harvests, while excessive soil moisture has held down potato yields.



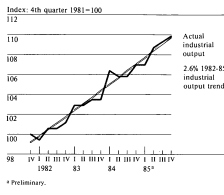
* Preliminary.
Note: This measure for agricultural output excludes into agricultural use of farm products that does not include adjustment for purchases by agriculture from other sectors.

Meat production increased by less than 1 percent, an unexpectedly low result in view of increases reported early in the year and the perceived improvement in the overall feed supply. The small increase in meat output, taken together with output of other livestock products, suggests no progress in the long-run goal of improving feed efficiency. Overall, per capita availability of farm products declined for the second year in a row.

B. Industry Recovers

After showing a moderate improvement in 1983-84 from the depressed levels of the previous two years, Soviet industrial performance worsened abruptly during first quarter 1985, as the USSR was hit by the coldest winter of the last 20 years. Nonetheless, for the year as a whole, industrial production rose nearly 3 percent, roughly on a par with the previous two years. By the end of 1985, quarterly industrial output was growing at close to 3½ percent.

Much of the rebound is attributable to improved weather during the last three quarters of the year. Modest improvements made in Soviet industry and rail transport over the last three years also provided a strong foundation for a upturn. Gorbachev's vigorous campaigns for labor discipline and against corruption and alcoholism probably also paid some dividends. His firing of one-third of the industrial ministers during the year showed that he was willing to follow through on his criticisms of poor performance. In addition, Gorbachev postponed two scheduled holidays to add extra workdays.

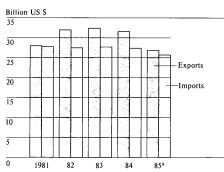


* Preliminary.

E. Hard Currency Trade Deteriorates

Although the USSR maintained its excellent credit rating, overall the Soviet financial position was much less comfortable at the end of 1985 than at the beginning of the year.

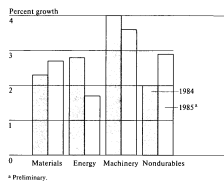
The fall in Soviet oil exports to the West precipitated a slight decline in overall Soviet trade from the 1984 level. Reduced trade with non-Communist countries was responsible for all of the decline as exports to these countries dropped by almost 15 percent from the previous year. Soviet oil exports to the West fell by about 20 percent, and arms deliveries to developing countries dropped almost 30 percent. To offset the resulting fall in earnings in hard currency trade, which accounts for about 80 percent of Soviet trade with the West, the Soviets stepped up borrowing, doubled gold sales, and postponed planned purchases (imports from the West were down 4 percent). In contrast with trade with the West, Soviet trade with the Communist countries in 1985 continued to increase. Overall, it grew by 2 percent, and its share in total Soviet trade increased to 61 percent, the highest level since 1972.



* Preliminary.

C. Basic Materials Smooth Way for Industry

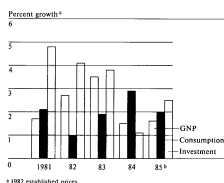
Growth in the output of industrial materials helped the rest of industry in 1985. Despite the setbacks in the first quarter, production increases of basic materials such as steel, cement, and plastics roughly matched the rate of 1984 for the year as a whole. The rate of increase of energy production slowed compared with that of 1984, however. A drop of nearly 3 percent in oil production dampened the effect of a 9-percent increase in natural gas and smaller increases in coal and electricity. Machinery output, as usual, grew faster than most of the rest of industry, although more slowly than in 1984. Production of high-tech equipment showed the best results. In contrast, growth in output of transport equipment was slight. Output of consumer nondurables grew 3 percent, up from recent annual rates. Light industry was largely unaffected by the bad winter. The food-processing industry showed a substantial improvement over 1984—milk and fish products did particularly well.



* Preliminary.

F. No Sharp Change in Resource Allocation

Although Gorbachev probably deserves some credit for the economy's showing in 1985, the programs and decisions involving resource allocation resulted from policies that predate his selection as General Secretary. During 1985, for example, growth in investment was 2.7 percent, according to official Soviet statistics, up from the 1.9-percent rate in 1984, but far below that rate necessary to carry out Gorbachev's modernization program. Similarly, whatever Gorbachev's intentions about increasing the availability of consumer goods as a spur to labor productivity, such a policy was not evident during 1985. Shortages of sought-after goods and services continued, limiting growth of per capita consumption to less than 1 percent, one-fourth the rate achieved in 1984.



* Preliminary.

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The Soviet Economy in 1985: A Year of Transition

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Introduction

In the USSR, 1985 was a year of transition, a bridge to new leadership and to a new economic planning period. The old generation of leaders, personified by the dying Chernenko, was replaced by a younger, better educated, more technically oriented generation, represented by General Secretary Mikhail Gorbachev. Almost immediately this leadership expressed its dissatisfaction with the state of the economy and persisted in revisions of the new Five-Year Plan, then in draft, to set a challenging course for economic development in the 1986-90 period.

The year 1985 also was the link between the 11th and 12th Five-Year Plans—both the concluding year of the disappointing 11th Five-Year Plan and the base from which achievements in the 12th will be measured. It was a year when overall performance was

lackluster, but ambitious plans were announced and new promises made to get the economy moving at a faster pace.

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Performance in 1985

Gorbachev devoted much of his attention last year to putting forward his blueprint for reviving the economy during the latter part of the 1980s. But, as he focused on the future, the economy was turning in another pedestrian performance. Disappointing farm output held GNP growth to about 1½ percent in 1985, about the same as in 1984 (table 1). Meanwhile, nonfarm output rose by about 2½ percent. Industrial output increased by nearly 3 percent, but slightly below the 1983-84 pace. Efforts to move to a pattern

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Table 1
USSR: Growth of GNP and
Selected Sectors of the Economy

Percent

	Average Annual 1981-85	1981	1982	1983	1984	1985 ^a
GNP^b	2.2	1.7	2.7	3.5	1.5	1.6
Agriculture ^c	2.2	-0.5	6.2	6.8	-0.5	-0.6
Nonagriculture	2.3	2.4	1.6	2.5	2.4	2.5
Industry	2.3	1.6	1.4	2.9	2.9	2.8
Construction	2.8	4.4	3.1	2.4	1.9	2.2
Transportation	2.4	4.1	1.2	2.8	1.6	2.5
Trade	2.0	2.3	0.8	2.3	2.8	2.0
Services	2.1	2.3	1.5	2.0	2.1	2.3

^a Preliminary.

^b Value added at 1982 factor cost.

^c This measure for agricultural output excludes intra-agricultural use of farm products but does not make an adjustment for purchases by agriculture from other sectors. Value added in agriculture grew at an average annual percentage rate of 1.8 in 1981-85, and at an annual percentage rate of -1.5 in 1981, 7.4 in 1982, 7.4 in 1983, -1.7 in 1984, and -2.1 in 1985.

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Gorbachev Addresses the Human Factor

Gorbachev has made it clear, almost since the day he became General Secretary, that revitalization of the Soviet economy is a top priority. He has acknowledged that, without improved economic performance, the USSR will have trouble simultaneously meeting requirements for defense, boosting consumer welfare sufficiently to improve labor productivity, and modernizing the economy. Focusing his efforts squarely on increasing efficiency, he has adopted a two-step approach. Initially, Gorbachev is relying on a combination of measures to strengthen party discipline, improve worker attitudes, and weed out incompetents—what he refers to as the “human factor.” Over the longer term, he is counting on achieving major productivity gains as a result of a series of organizational changes, reform initiatives, and, most important, an extremely ambitious campaign to modernize the country’s stock of plant and equipment. []

At the recently concluded 27th Party Congress, party leaders hailed Gorbachev for the economy’s improved performance since he took over. On the surface, their praise seems justified. After a miserable first quarter in 1985, nonfarm output rebounded strongly. Industry, in particular, did well. []

Much of the rebound is attributable to improved weather during the last three quarters of the year. Milder spring weather allowed transportation and power supplies to return to normal and equipment to

function properly. Modest improvements in industry and rail transport since 1982 also supported an upturn in the latter half of 1985. Another factor was the postponement of two holidays during the second half of 1985, so that there were two more workdays during the last six months of 1985 than in the same period in 1984. []

Gorbachev’s vigorous campaigns to increase worker discipline and cut alcohol abuse also probably paid some dividends. His campaigns for discipline and against corruption and alcoholism, like those pushed less vigorously by Andropov, received widespread public support. According to Soviet figures, purchases of alcohol at state stores declined 25 percent during the second half of 1985 compared with those of the last six months of 1984. Soviet press statements indicate that, as a result, there was a marked decrease in absenteeism, fewer industrial accidents, and increased productivity overall. By reducing alcohol-related absences and unauthorized leave, Gorbachev sought to raise the number of hours worked by the labor force. []

At an April plenum, Gorbachev issued an urgent call for better economic performance. Although acknowledging the severe winter weather, he blamed lack of discipline and passive management for the poor first-quarter results and told workers and managers, in effect, to shape up or “move aside.” []

of intensive growth based on productivity gains continued to be frustrated by the many economic problems Gorbachev inherited. []

Despite the relatively slow growth in the economy overall, Gorbachev could take some satisfaction from the 1985 results (see inset). Through a combination of factors, a year that started out very badly became at least respectable. Certainly, improved weather, after the first quarter, eased pressures throughout the economy. (A similar situation during 1982—when harsh weather also disrupted production—did not result in nearly the same turnaround.) []

Industry Recovers

After showing a moderate improvement in 1983-84 from the depressed levels of the previous two years, Soviet industrial performance worsened abruptly in first quarter 1985. The USSR was hit by the coldest winter of the last 20 years. Industrial growth slumped. Output of several industrial products was so low that customary data on their production were omitted from official monthly plan fulfillment reports. Cold and snow snarled transportation—rail freight traffic

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Table 2
USSR: Industrial Growth by Branch

Percent

	Average Annual 1981-85	1981	1982	1983	1984	1985 ^a
Industry^b	2.3	1.6	1.4	2.9	2.9	2.8
Industrial materials	2.2	1.6	0.7	3.7	2.3	2.7
Ferrous metals	0.8	-0.3	-0.0	2.6	0.9	0.9
Nonferrous metals	2.0	0.3	0.8	3.0	3.0	3.0
Chemicals	4.3	4.0	2.1	6.9	3.5	5.2
Wood products	2.0	1.9	0.5	2.9	2.7	2.2
Construction materials	1.2	1.3	0.1	2.0	1.3	1.4
Energy	2.2	1.9	2.2	2.3	2.8	1.7
Fuel	1.0	1.4	1.6	1.2	0.9	0.2
Electric power	3.6	2.5	3.1	3.7	5.2	3.6
Machinery	2.7	1.4	1.6	2.8	4.0	3.6
Consumer nondurables	2.1	2.0	1.3	2.1	2.0	2.9
Soft goods	1.6	1.8	-0.5	1.2	2.8	2.9
Processed food	2.4	2.2	2.8	2.9	1.3	3.0

^a Preliminary.^b Value added at 1982 factor cost.

fell sharply, apparently causing shortages of raw materials throughout industry. The severe weather also caused equipment breakdowns and cut power supplies to industry. Nonetheless, for the year as a whole, industrial production rose by nearly 3 percent, roughly on a par with the previous two years. By the end of 1985, quarterly industrial output was growing at an annual rate close to 3½ percent [redacted]

Within industry, the performance of all branches improved during the course of 1985, but not all branches performed better than in 1984 (table 2). The most substantive recovery was in the branches producing industrial materials—steel, chemicals, cement, and the other basic products used throughout Soviet industry. After registering a 2½-percent *decline* during first quarter 1985 (compared with first quarter 1984), output of industrial materials rebounded to an *increase* of more than 2½ percent for the year. As usual, growth in machinery production outstripped

growth in most industrial branches, although there was little acceleration during the year. Output of consumer nondurable goods increased enough during the year to raise the rate for 1985 above that for 1984. On an annual basis, productivity in industry slipped slightly in 1985 as it had in 1984. Even though growth in labor productivity—the only productivity measure for which quarterly data are available—improved in the course of the year, such growth did not offset a continuing decline in capital productivity (table 3). [redacted]

Industrial Materials. In branches producing industrial materials, output grew a little faster in 1985 than in 1984. Continued expansion in these branches is needed to avoid the shortages that have led to bottlenecks in other sectors. That such shortages did not prevent recovery from the setbacks of the first quarter is a sign of resilience in 1985 performance. [redacted]

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Table 3
USSR: Growth in Industrial Output and
Factor Productivity in 1981-85

Percent

	Average Annual 1981-85	1981	1982	1983	1984	1985 ^a
Industrial production	2.3	1.6	1.4	2.9	2.9	2.8
Combined inputs	4.1	4.7	4.3	4.1	3.9	3.7
Work hours	0.4	0.7	0.8	0.4	0.1	0.3
Capital	7.0	7.8	7.0	6.9	6.8	6.4
Overall productivity	-1.7	-2.9	-2.8	-1.1	-1.0	-0.9
Labor productivity	1.9	1.0	0.6	2.5	2.8	2.5
Capital productivity	-4.3	-5.7	-5.3	-3.8	-3.6	-3.3

^a Preliminary.

Growth in the output of *ferrous metals* was slightly less than 1 percent in 1985—the same as in 1984. Steel plants struggled to overcome the paralysis caused in the first quarter by energy shortages and the railroads' failure to transport about 8 million metric tons of raw materials. Output of *nonferrous metals* also grew at the same rate in 1985 as in 1984, thanks to additions of new capacity and modernization of equipment at aluminum, copper, and nickel plants. []

Shortages of railcars and raw materials, as well as delays in construction, were problems for the *chemical industry* throughout the year. Even so, growth increased in 1985. Fertilizer output rose by 8 percent, and the four new ammonia plants that came on stream should boost fertilizer production again in 1986. Disruptions in supplies of ethylene feedstock stemming from below-plan refinery output held down output of plastics and synthetic resins. Sluggish growth in caustic soda output constrained production of artificial fibers and dye, both key inputs to textile manufacturing. []

Growth in the production of *wood products* in 1985 slowed because of the severe weather early in the year. Because 90 percent of the USSR's timber is harvested in remote northern and eastern parts of the country, felling and transport are extremely difficult even under average weather conditions. []

Construction materials was the branch hit hardest by the abnormal cold. In the first quarter, output dropped by more than 5 percent. By yearend, however, production of cement and precast ferroconcrete exceeded 1984 levels. Some progress in using secondary materials and wastes, such as slag, ash, and broken glass, has been made in this branch. []

Energy. Growth in the Soviet energy sector slowed in 1985 (table 4). A drop of nearly 3 percent in oil production dampened the effect of a sizable increase in natural gas output and smaller increases in coal and electricity production. The Soviets coped with declining oil output by cutting exports and shifting some oil users to natural gas. []

In 1985, growth in production of energy from primary sources dropped to 2.7 percent from 3.1 percent in 1984. *Oil* production declined for the second consecutive year, resulting in declines in exports and, thus, in hard currency earnings of about \$3.5 billion. The *gas* industry achieved a 9½-percent increase in output in 1985. Gas exports to Western Europe increased by 10 to 15 percent; however, soft market demand forced the Soviets to lower prices by roughly 10 percent. As a

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Table 4
USSR: Growth in Energy Production

Percent

	Average Annual 1981-85	1981	1982	1983	1984	1985 ^a
Primary Energy ^b	2.6	2.4	2.6	2.5	3.1	2.7
Oil	-0.3	0.6	0.6	0.6	-1.0	-2.9
Gas	8.1	6.9	7.6	7.0	9.6	9.5
Coal	0.3	-1.7	2.0	-0.3	-0.5	1.9
Electricity	3.6	2.5	3.1	3.7	5.2	3.6

^a Preliminary.

^b Data are for coal, crude oil, natural gas, natural gas liquids, and hydroelectric and nuclear electric power expressed in terms of oil equivalent, and exclude minor fuels such as peat, shale, and fuelwood.

result, hard currency revenues from gas of about \$4 billion in 1985 were roughly unchanged from the previous year. *Coal* production increased about 2 percent but was still less than 2 million tons above the previous 1978 high. Moreover, the energy content of coal continued to decline. []

Electricity production in 1985 grew by 3.6 percent over that in 1984. Output was just under the original target, with above-plan results at fossil-fueled power plants making up for most of the shortfalls at nuclear plants and hydroplants. The surge of natural gas to the power industry accounts for most of the improved performance at the fossil-fueled plants. Ample gas supplies have meant that power stations, previously under fuel-use restrictions, could generate at full capacity. []

Machinery. The source of consumer durables, investment goods, and military hardware, machine building traditionally has been a fast-growing branch. But in 1985 growth slipped below the 4-percent increase in 1984. Civilian machinery grew about half a percentage point less than in 1984, while military machinery grew at roughly its 1984 rate. Growth was fastest in production of computers, high-tech machine tools, other types of automated equipment, and chemical equipment. Output of petroleum equipment picked up, but production of transport equipment stagnated. []

Consumer Nondurables. Overall growth in consumer nondurable goods rose by 3 percent in 1985, a substantially better performance than in recent years. Within *light industry*, textile production increased moderately, although the 1984 cotton crop was poor, and production of chemical fibers was down compared with that in 1984. Knitwear did better, and the rate of increase in sewn goods remained healthy. Lower-than-planned output of footwear partly reflected continuing problems with the timely supply of usable leather. []

The overall performance of the *food-processing* industry in 1985 was good. Milk and fish products did particularly well. The trouble spots of the industry remained vegetable oil and margarine, largely because of poor oilseed crops. []

Transportation Rebounds

Like industry, transportation rebounded during 1985 from a disastrous first quarter. Overall freight traffic (measured in ton-kilometers) grew by only 1.6 percent in 1985, but the results represented a respectable recovery when compared with the 1-percent decline recorded in the January-June period (table 5). []

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Table 5
USSR: Freight Turnover by Transport Mode

	Average Annual 1981-85	1981	1982	1983	1984	1985 ^a
<i>Billion ton-kilometers</i>						
Total	7,084	6,700	6,786	7,127	7,345	7,463
Rail	3,585	3,503	3,465	3,600	3,639	3,719
River	264	256	262	273	264	262
Highway	141	140	143	142	138	142
Oil pipelines	1,321	1,263	1,307	1,353	1,370	1,313
Gas pipelines	889	681	772	863	997	1,131
<i>Percentage rate of growth</i>						
Total	2.9	3.4	1.3	5.0	3.1	1.6
Rail	1.3	1.8	-1.1	3.9	1.1	2.0
River	1.0	4.4	2.3	4.1	-3.3	-1.0
Highway	1.2	6.9	2.1	-0.7	-2.8	2.0
Oil pipelines	1.4	3.9	3.5	3.5	1.3	-4.0
Gas pipelines	13.6	14.1	13.3	11.9	15.5	13.0

^a Preliminary Soviet data; growth rates as officially reported.

The *railroad* recovery was the top story in Soviet transportation in 1985. After the rail sector staggered under a 5.5-percent drop in freight traffic during the first quarter, railroads rebounded faster than they did in a similar situation during 1982. Measures adopted over the last several years to improve railroad performance appear to have paid off. Management has squeezed additional capacity out of the system over the last three years—primarily through increased discipline and strategies to get more tonnage on crowded lines by boosting train weights. This added capacity allowed the railroads to expedite backlogged shipments later in the year, spurring their own recovery and that of their customers in the industrial materials branches. Railways Minister N. S. Konarev kept the discipline campaign alive during the year by issuing severe reprimands and forcing the retirements of several officials, including a first deputy minister.

Agriculture Disappoints

Farm output fell by about a ½ percent in 1985. Crop production actually declined, and growth in output of the livestock sector slowed (table 6). Generally improved weather conditions in many of the major grain-producing areas raised grain production to an estimated 200 million tons—the best harvest since the record of 237 million tons in 1978 and 20 million tons above the 1984 estimated outturn. This—together with increased production of sunflower seeds, fruits, and cotton—was countered by lower output of key crops (such as potatoes, sugar beets, and vegetables) caused in part by disease and insect infestation. The improved grain crop enabled Moscow to cut grain imports during second half 1985 by nearly 60 percent from the record 28 million tons imported during January-June.

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Table 6
USSR: Growth of Farm Output

	Average Annual 1981-85	1981	1982	1983	1984	1985 ^a
	<i>Percent change</i>					
Total output^b	2.2	-0.5	6.2	6.8	-0.5	-0.6
Crops ^c	1.7	-3.4	11.5	4.6	-2.9	-0.5
Livestock ^d	2.8	1.1	0.0	8.6	3.8	0.8
	<i>Million metric tons (annual average), except where noted</i>					
Major crops						
Grain ^e	182.6	158.0	180.0	195.0	180.0	200.0
Potatoes	78.3	72.1	78.2	82.9	85.5	73.0
Sugar beets	76.3	60.8	71.4	81.8	85.3	82.0
Sunflower seeds	4.9	4.7	5.3	5.0	4.5	5.2
Cotton	9.1	9.6	9.3	9.2	8.6	8.8
Vegetables	29.0	27.1	30.0	29.1	30.7	28.0
Major livestock products						
Meat (<i>slaughter weight</i>)	16.2	15.2	15.4	16.4	17.0	17.1
Milk	94.4	88.9	91.0	96.4	97.6	98.2
Eggs (<i>billions of units</i>)	74.3	70.9	72.4	75.1	76.0	77.0

^a Preliminary.

^b Net of feed, seed, and waste.

^c Net of seed and waste.

^d Excluding changes in inventory and net of feed and waste.

^e Estimate.

The slump in the livestock sector was largely the result of a decline in herd and flock inventories—reflecting the culling of unproductive cows and above-normal slaughtering of hogs, sheep, and goats to reduce winter feed requirements early in the year. The output of livestock products increased slightly. Meat production was up by less than 1 percent, an unexpected result in view of the higher monthly increases reported for meat produced on state and collective farms, roughly two-thirds of total meat, and the perceived improvement in the overall feed supply. The implied reduction in the share of meat produced by the private sector, however, may reflect a shift of private production to production under contract with state or collective farms, a practice the leadership is encouraging, and one that reportedly guarantees feed

to the private producer. Officially, meat produced under such contracts is used to meet state and collective farm targets for sales of meat to the state. The small increase in meat output, taken together with output of other livestock products, suggests no progress in the long-run goal of improving feed efficiency. Overall, per capita availability of farm products declined for the second year in a row.

Hard Currency Trade Deteriorates

The fall in Soviet oil exports to the West precipitated an estimated slight decline in overall Soviet trade from the 1984 level. An erosion in trade with non-Communist countries was responsible for all of the

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Table 7

Billion US \$

USSR: Total Trade, 1981-85 ^a

	Annual Average 1981-85	1981	1982	1983	1984	1985 ^b
USSR: Exports by region						
Total	87.3	79.4	87.2	91.7	91.5	86.7
Communist	49.3	43.4	47.1	51.0	51.9	53.2
Developed countries	25.2	24.4	26.2	26.7	26.4	22.4
Less developed countries	12.7	11.6	13.8	13.9	13.2	11.1
USSR: Imports by region						
Total	78.3	73.2	77.8	80.5	80.3	82.6
Communist	44.3	37.2	42.5	45.5	47.0	50.5
Developed countries	24.6	25.4	26.2	25.4	24.2	23.2
Less developed countries	9.4	10.6	9.1	9.6	9.1	8.9

^a Includes both hard currency trade and trade conducted with soft currency partners on a clearing account basis.

^b Preliminary.

decline. Soviet trade data for 1985 show that exports to these countries dropped by 15 percent from the previous year—largely because of a 20-percent decline in oil exports and a 30-percent fall in Soviet arms deliveries. Almost all of the decline was due to lower export volume compounded somewhat by softening prices. Imports from the West were down by 4 percent from the 1984 level (table 7). To offset the fall in hard currency earnings from lower oil prices and production, the Soviets stepped up borrowing, increased gold sales, and postponed some planned purchases. In 1985 the Soviets sold nearly twice the amount of gold sold annually in 1982-84. Overall, Moscow ended 1985 in a much less comfortable financial position than it started with. []

In contrast with trade with the West, Soviet trade with the Communist countries in 1985 continued to increase. Soviet imports from Communist countries have grown faster than exports, reducing Moscow's trade surplus with these countries, especially its East European partners. Overall, the share of Soviet trade with the Communist countries increased to 61 percent, the highest level since 1972. A sharp drop in

Eastern Europe's trade deficit with the USSR compared with that in 1984 was the result of slower growth of Soviet exports and of Moscow's pressure to balance trade. Poland was the only country with a larger deficit, which reflected special treatment by the Soviets in consideration of Warsaw's economic difficulties. The boost in Soviet imports from Romania, Hungary, and Czechoslovakia at the same time that exports by these countries to the West dropped suggests the strength of Soviet pressure to reduce its trade surplus with Eastern Europe. []

Resource Policy Trends

Soviet economic priorities can be evaluated by examining how resources are distributed among the three major categories of uses—consumption, investment, and defense. During the 1981-85 period, investment in the productive capacity of the economy took a slowly rising share of GNP, while the share of goods

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Table 8

Percent

USSR: Indicators of Capital Formation Growth ^a

	Average Annual 1981-85	1981	1982	1983	1984	1985 ^b
Total new fixed investment	3.5	3.7	3.5	5.6	1.9	2.7
Of which:						
Machinery	4.2	5.0	4.8	6.9	1.4	NA
Gross additions of new fixed capital ^c	2.8	0.3	5.2	5.9	2.2	0.7
Backlog of unfinished con- struction (<i>current prices</i>)	3.0	2.8	0.8	0.8	7.8	2.9

^a Unless otherwise noted, rates of growth are based on official Soviet series valued in constant 1984 prices.

^b Preliminary.

^c The term "gross additions of new fixed capital" differs from "new fixed investment" in that it counts only those investment projects that were completed.

[redacted]

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and services used for consumption slipped slightly. The share going to defense remained largely unchanged. The small shifts in resource allocation discernible in 1985 showed the same basic pattern. Although Gorbachev probably deserves some credit for the economy's showing in the latter part of 1985, the programs and decisions involving resource allocation resulted from policies that predate his selection as General Secretary. [redacted]

Higher Priority for Investment

Investment in reproducible fixed assets now takes more than one-fourth of Soviet GNP, in comparison with one-fifth of US GNP. Investment grew by slightly over 2½ percent in 1985—about 1 percentage point below plan for the year because the harsh winter delayed many construction projects, but up from the rate in 1984 (table 8). Even when the weather improved, however, problems bringing new production facilities on line continued despite repeated calls by Gorbachev and other top officials to reduce the backlog of unfinished construction during the year. Nonetheless, by yearend the pace of growth of both investments and additions to capacity had speeded up. [redacted]

[redacted]

The 1981-85 Plan originally called for investment to grow more slowly than the overall economy. The decision to slow down planned investment growth to roughly 2 percent per year was made on the assumption that economic growth could be stimulated by more efficient use of existing plant and equipment. It was tied to a strategy that concentrated on replacing obsolescent machinery and equipment rather than building new capacity on "green field" sites. For the 1981-85 Plan period as a whole, investment increased at an average annual rate of 3½ percent, about a percentage point faster than GNP. [redacted]

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Mixed Results for the Consumer

In 1985 per capita consumption grew less than 1 percent, continuing the very slow progress of recent years (table 9). Food supplies—the main indicator by which consumers judge their well-being—probably slipped slightly on a per capita basis as total availability of farm products declined somewhat in 1985. Meat production, for example, increased only marginally over the 1984 output level. [redacted]

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Table 9
USSR: Growth in Per Capita Consumption^a

Percent

	Average Annual 1981-85	1981	1982	1983	1984	1985 ^b
Total	1.0	1.8	-0.1	0.7	2.0	0.5
Food	0.2	1.0	0.3	0.3	1.2	-1.9
Soft goods	1.2	2.0	-1.5	0.6	2.4	2.6
Durables	2.9	6.3	-2.6	1.7	4.6	4.9
Services	1.5	1.4	1.5	1.0	1.9	1.5

^a Established 1982 prices.^b Preliminary.

Meanwhile, personal incomes continued to grow, contributing to the mismatch between purchasing power and supplies of some goods and services. Average monthly wages of workers and employees grew by nearly 3 percent in 1985. []

Because of an official policy to maintain prices unchanged in state retail outlets, we depend on price movements in the collective farm markets (CFMs) to signal inflationary pressures. Reporting from our Embassy in Moscow indicates that CFM prices, following a rapid increase in the late 1970s and early 1980s, had leveled off in 1984 and the first half of 1985. Prices began to climb again, however, in second half 1985, suggesting another tightening of food supplies. []

On the brighter side, supplies of nonfood goods—soft goods and consumer durables—showed improvement in 1985. In addition, per capita consumption of personal care and repair services grew about 4 percent in 1985. Construction of new housing reached 113 million square meters, the largest increment to the housing stock in two decades. Larger volumes of new apartments will be necessary to keep up with new family formation, however. In 1984, for example, 1.3 million more household units were created than new apartments. []

Gorbachev's campaign against alcohol achieved some success in 1985. Sales of alcohol in state stores fell by 25 percent in the second half of the year as compared with the same period in 1984. At least some of the drop in official sales probably was offset by an increase in homebrew. Nonetheless, the campaign has, at a minimum, reduced drinking on the job and probably has contributed to the upswing in economic performance in the second half of 1985. []

Slow Defense Growth

We have a fairly good sense of consumption and investment trends in 1985, but our information on Soviet defense spending is much less solid, and we have not settled on an estimate for 1985. What is certain is that the Soviets continued the broad-based modernization of their military forces during 1985. They augmented their strategic nuclear strike capability by beginning to deploy new bases for the mobile SS-25 ICBM. At the same time, they added new units of both the Typhoon and Delta-IV classes of ballistic missile submarines. []

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Modernization of general purpose forces also continued apace, with many of the programs—especially those in the ground forces—apparently intended to make them more capable of extended operations. As part of this effort, for example, Moscow continued to field new tanks, an improved tracked infantry vehicle, and a new wheeled armored personnel carrier. Meanwhile, Soviet air force units received their initial complement of SU-27 Flanker fighters, as well as other aircraft already in serial production. Finally, the Soviets continued their commitment to a blue water navy with the addition of a new Oscar-class cruise missile submarine and the fitting out of both the fourth Kiev-class aircraft carrier and a new large aircraft carrier.

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Appendix

Revised Estimates of Soviet GNP

Nature of the Revision

The economic growth rates presented in this paper are based on a major revision of the estimates that have been published annually in CIA's *Handbook of Economic Statistics* and described in detail in *USSR: Measures of Economic Growth and Development, 1950-80* (issued in December 1982 under the aegis of the Joint Economic Committee). The purpose of the revision is to base the estimates on prices of a more recent year—1982 instead of 1970. The results should be regarded as preliminary and subject to further revision as more information becomes available.

The shift to a new price base affects estimates of GNP and its growth rates in three major ways when compared with previous estimates:

- Values of output are higher, because prices in general increased between 1970 and 1982.
- Rates of real growth—excluding price effects—are lower for GNP and most key components. This result is to be expected when prices of a more recent year are used to calculate growth rates (see inset for explanation of the “index number” effect). In converting estimates of US GNP from 1972 prices to 1982 prices, the Department of Commerce obtained similar results (see inset).
- Shares of key components of GNP are different because the components experienced diverse rates of change in both real growth and prices.

The estimates of Soviet GNP are calculated first by using prevailing 1982 prices and then adjusted to measure more accurately the actual allocation of resources in the economy and changes over time in its potential to produce goods and services. Official Soviet prices give quite a distorted picture of the true costs of economic resources, largely because the prices include huge sales taxes, levied mostly on consumer goods, and subsidies, which affect mainly food and services. Moreover, the profits included in the prices

The “Index Number” Effect

To understand why measured economic growth is likely to be lower the more recent the price base used in the calculation, consider an example. Suppose you want to estimate the real growth in output of precision instruments, a group of products ranging from clocks to automation equipment to computers. The prices of new products (computers), whose production is growing fastest, tend to fall relative to other prices because of more rapid gains from advances in technology and economies of scale. Therefore, the fastest growing products will have smaller weights—and less impact on average growth of the group in a later base year than they would in an early base year.

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The US Revision

Estimates of real GNP for the United States are now based on 1982 prices rather than 1972 prices. The changes in the rate of increase of US GNP as a result of this shift resemble changes in our estimates of Soviet GNP growth:

	Average annual percent	
	US ^a (1973-84)	USSR (1971-82)
Old price base	2.7	3.0
New price base	2.3	2.6

^a US estimates are reported in the US Department of Commerce journal, *Survey of Current Business*, December 1985, p. 13. Only changes due to the shift in price base are shown here. Other revisions of the estimates, including new definitions and a new price index for computers, partly offset the effects of this shift. Another article on the revised US estimates appears in the October 1985 issue, pp. 19-28.

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Table 10 *Percent per year*
USSR: Comparison of Average Annual GNP Growth at Factor Cost in 1970 and 1982 Prices

	Price Base	
	1970	1982
1966-70	5.3	4.9
1971-75	3.8	3.1
1976-80	2.7	2.3
1981-85	2.4	2.2
1981	1.9	1.7
1982	2.4	2.7
1983	3.5	3.5
1984	2.0	1.5
1985 ^a	2.1	1.6

^a Preliminary.

do not accurately reflect the differences in efficiency among producers. To correct for such distortions in official prices, a so-called factor cost adjustment is made in which profits and indirect taxes are subtracted, and subsidies and charges on fixed and working capital are imputed. The resulting values give a much better picture of patterns of resource allocation by producing sector and by final end use than the distributions shown by official prices. Also, estimates of changes in GNP using factor cost valuations give more accurate measures of growth in production potential over time. [redacted]

Results of the Revision

With *both* prices and real output rising, Soviet GNP increased by nearly 90 percent between 1970 and 1982, to a level of 720 billion rubles. Prices accounted for over a third of this increase, implying a rate of inflation of a little more than 2 percent per year. In contrast, official Soviet statistics for measures similar to GNP imply an inflation rate of less than half a percent per year during that period. Most Western specialists believe that these official statistics seriously understate the extent of price increases and therefore overstate Soviet economic growth. [redacted]

Annual growth rates of Soviet GNP in real terms as measured in 1982 prices are, with few exceptions, lower than previously estimated rates measured in

Table 11 *Percent*
USSR: Shares of GNP by Sector of Origin at Factor Cost, 1982

	Shares in 1970 Prices	Shares in 1982 Prices
GNP	100.0	100.0
Industry	36.8	33.7
Construction	7.6	7.9
Agriculture	14.3	20.0
Transportation	10.4	10.3
Communications	1.2	1.1
Trade	7.7	6.3
Services	20.2	18.2
Military personnel	1.6	1.8
Other branches	0.3	0.7

1970 prices (table 10). Shifting the price base reduced annual rates of increase by a few tenths of a percentage point in the 1980s. The differences between rates are a little larger in earlier years—half a percentage point or more in the 1970s. [redacted]

The shift to a new price base had a significant effect on the relative shares in total output coming from the two largest producing sectors—industry and agriculture (table 11). The share of industry is smaller when measured in 1982 prices, because average wages in industry increased much less during 1971-82 than average incomes in agriculture, and the capital-output ratio increased more rapidly in agriculture than in industry. The shares of the trade and services sectors dropped somewhat, while the shares of the remaining sectors are little affected by the change in the price base. [redacted]

Impact on Estimates of Defense Spending

Moving Soviet defense spending estimates from a 1970 to a 1982 price base affected assessments of defense spending and its components in four major ways:

- The overall level of spending rose.

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- The share of GNP allocated to defense spending increased from 12 to 14 percent in the early 1970s to about 15 to 17 percent in the early 1980s.
- Estimates of the rate of real growth decreased slightly.
- The shares of major resource categories in total defense spending changed.

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The estimates of defense spending in 1982 prices show a higher overall level of spending than did the 1970 series. The new series averages almost 50 percent higher for the period since 1970 than the series in 1970 prices, indicating that military costs increased about 3 percent per year. When both price change and growth in real output are taken into account, the growth in defense spending averaged over 5 percent annually during 1971-84. Price changes accounted for more than half of this increase.

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The change to a 1982 price base shows a somewhat higher share, than the earlier series, of GNP allocated to defense. This result implies that prices for defense goods and services increased faster than those for civilian goods and services. During 1966-84, total defense spending increased on average by about 3 percent annually—somewhat less rapidly than the series in 1970 prices. The direction of this change in relative growth rates is what index number theory predicts, but it is not a large effect. In the conversion to 1982 prices, the share of defense spending devoted to procurement increased, while the shares of the RDT&E (research, development, testing, and evaluation) and personnel categories—which experienced less price increase than procurement—fell.

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