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OUTLOOK FOR AN INDEPENDENT AUSTRIA

Submitted by the

DIRECTOR OF CENTRAL INTELLIGENCE

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Concurred in by the

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OUTLOOK FOR AN INDEPENDENT AUSTRIA

THE PROBLEM

To estimate post-treaty Austria's probable policies and courses of action, and its ability to maintain internal stability and independence.

CONCLUSIONS

1. After 17 years of foreign occupation, Austria is regaining sovereignty with a high degree of confidence in its future. Despite markedly different views and mutual antagonisms, the conservative People's Party and the Socialists have maintained a stable postwar coalition government. However, the end of the occupation will remove a powerful cohesive force, and give rise to complex problems which will strain coalition unity. (*Paras. 7, 13-14*)

2. Nevertheless, the coalition will probably maintain its unity at least until the next general election, to be held not later than February 1957. The persistence of party loyalties and the fairly rigid social pattern in Austria will militate against either major party winning a parliamentary majority in the election. In the event that either party should gain an absolute majority of seats, it could probably not resist the natural temptation to govern alone. However, as long as relatively favorable economic and international conditions prevail, moderate forces in Austria will remain vigorous enough to insure the maintenance of political de-

mocracy and stability. As a consequence of the Soviet withdrawal, Communist Party strength — already low — will almost certainly decline. (*Paras. 15-18*)

3. Austria has favorable economic prospects though it remains highly vulnerable to adverse conditions of world trade. The restoration of independence will have a stimulating effect on investment, production, and exports. Provided inflationary pressures are checked, we believe that Austria can probably overcome its short-run balance of payments difficulties and liquidate its sizeable economic obligations under the State Treaty. Under such circumstances, and barring a marked decrease in world demand for Austrian products, over the longer term Austria's rate of economic growth will probably exceed the Western European average. (*Paras. 19, 28*)

4. The proportion of Austrian trade with the Bloc is not likely to increase substantially unless: (a) the Bloc is able to satisfy Austrian import requirements far more adequately than in the past; (b) inflation makes Austrian goods noncompet-

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itive in Western markets; or (c) Western demand for Austria's products declines for other reasons. (*Para. 27*)

5. Most Austrian political leaders agree that their country needs a military establishment adequate to support a policy of genuine neutrality. Austria will probably hold to its program of building up the army to the level of 55,000 men, but political and economic considerations almost certainly will prevent this from being accomplished within the presently contemplated two-year period. (*Paras. 31-32*)

6. The Austrians face the problem of trying to retain the moral and political support of the Western Powers while avoiding actions which might dangerously antagonize the Soviet Bloc. Therefore, in foreign policy they will seek to maintain a delicately balanced position between the two great power blocs, and to exploit their independent role for whatever advantage can be gained from either side. Concern for its neutrality and fear of provoking the USSR will inhibit Austria's military cooperation with the West. (*Paras. 35, 37*)

DISCUSSION

7. After 17 years of foreign occupation, Austria is regaining sovereignty with a high degree of confidence in its future. Nearly 10 years of stable coalition government, continuous economic improvement, and bitter experience with political extremism have given Austrians a new faith in democratic processes. The Nazi and Soviet occupations have contributed to a marked reduction in pan-German sentiment and to a vigorous dislike of Communism.

8. Austria has natural affinities with the West and is anxious to participate in Western European economic and political institutions. However, Austria is also eager to improve its relations with the Succession States of the Hapsburg Empire, all of which are now dominated by Communist regimes. Austria avoids taking sides in the international conflict, not only because of the State Treaty, but also from inclination. Austrians regard the ending of their occupied status as due in large measure to their moderation and ability to compromise, and believe that their independence can best be preserved through continuing conciliatory and flexible policies toward their neighbors and the great powers.

I. POLITICAL TRENDS

The Current Political Scene

9. Since 1945, Austria has been governed by a moderate coalition composed of the two major political parties, the conservative People's Party and the Socialist Party. Approximately equal in strength, these parties won 83 percent of the vote in the 1953 national election, and they control 147 of the 165 seats in the Nationalrat.

10. *The People's Party.* In the 1953 election the People's Party gained 41 percent of the vote and 74 seats in the Nationalrat. Chancellor Raab, Foreign Minister Figl, and five other cabinet members are the party's leading representatives in the government. The People's Party derives its strength from the farmers, big business, and practicing Catholics of all social classes. In effect, the party stands for state-regulated capitalism. It opposes public investment, advocates higher prices for farm products, and favors partial denationalization of heavy industry. The high prestige of Raab and Figl resulting from their successful negotiations on the State Treaty may have checked the moderate decline in the party's strength since 1949.

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11. *The Socialist Party.* The Socialists won 42 percent of the vote and 73 Nationalrat seats in the 1953 election. President Koerner and six cabinet ministers, including Vice Chancellor Schaerf, are Socialists. The Socialist Party represents the vast majority of Austrian labor and segments of the lower middle class. The party advocates social and labor legislation and a high level of public investment. The political militancy of the workers has declined as they have moved closer to the middle class in economic status. Moreover, the party has in practice abandoned Marxism and has adopted moderate programs designed to attract a wider segment of the population. The Socialists nevertheless retain their highly disciplined organization. Recent local elections, as well as national elections since 1949, have demonstrated a small upward trend in Socialist strength.

12. *The extremist parties.* The parties of the extreme right and left have been ineffective in postwar Austria. The rightist Independent Party, composed of political malcontents and pan-German nationalists of the upper middle class, received 11 percent of the vote and 14 seats in the Nationalrat in 1953. However, as a result of its negative policies and weak leadership, the party now appears to be on the verge of disintegration. Austria's Communist Party is one of the least effective in Europe. Its proportion of the national vote has remained static at about five percent since 1945, and it had an estimated membership of 60,000 in 1954. The party has four seats in the Nationalrat. Communism has suffered in Austria from the excesses of the Red Army, from prolonged Soviet obstruction of the State Treaty, and from the traditional preference of the workers for the Socialist Party. The pending withdrawal of Soviet occupation forces is already having a demoralizing effect on the party, especially on those persons in Eastern Austria for whom party membership was a matter of political expediency.

13. *The coalition.* The People's Party and the Socialists have maintained their coalition over a decade, both because they were virtually equal in strength and because the delicate

task of governing an occupied country imposed a special need for presenting a united front in bargaining with the occupying powers. Although the two parties differ markedly in their basic social and economic views, they have successfully surmounted serious policy clashes and have preserved a moderate government. The parties have maintained a balance of power within the coalition by sharing evenly in the distribution of the posts at the disposal of the government.

The Short-Term Political Outlook

14. The end of the occupation will not only remove a powerful cohesive force, but will present the Austrian government with some complex problems which will strain coalition unity. The People's Party and the Socialist Party will continue to disagree fundamentally on the problem of financing and controlling investment. The People's Party will advocate conservative policies designed to attract foreign capital and to restore the domestic capital market. The Socialists will press for a high level of public investment financed by taxation. The specific issue most likely to strain coalition unity is the handling of the vast complex of properties which the USSR has agreed to restore to Austria. The People's Party is strongly opposed to placing them under the Socialist Minister of Nationalized Industries, lest the Socialists thereby gain a dominant influence on the economy and obtain political advantages from patronage. However, because these firms will be in need of substantial public capital investment, some form of state control appears to be inevitable. This dispute may be solved by a compromise; e.g., by giving the Socialists control over the oil properties through the Ministry of Nationalized Industries and giving the People's Party control of most of the remaining enterprises through the Ministry of Finance.

15. The approach of the next general election, which is to be held not later than February 1957, will almost certainly generate intense rivalry as both the major parties strain to achieve a parliamentary majority. However,

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the widespread satisfaction with the present division of political power, the eagerness of both major parties to share in the advantages of government positions, and the experience of collaboration and compromise through the past decade indicate that Austria's present moderate leaders probably will not permit party competitive differences to go so far as to lead to dissolution of the coalition prior to the election.

Longer-Term Prospects

16. Strong competition between the People's Party and the Socialists will continue to characterize Austrian political life for the foreseeable future. The Socialists may continue their slow but steady gains in the next election, although their rate of progress may be reduced by the great personal popularity which People's Party leaders Raab and Figl attained as a result of the conclusion of the State Treaty. The persistence of party loyalties and the fairly rigid social pattern in Austria will militate against either major party winning an absolute parliamentary majority. If the Socialists were to win a plurality, their subsequent efforts to gain the chancellorship probably would result in heated and prolonged negotiations. However, despite the theoretical possibility of an alternate coalition between the People's Party and the remnants of the Independents, we believe that both major parties would agree to reconstitute the coalition government.

17. In the event that either party should gain an absolute majority of seats, it could probably not resist the natural temptation to govern alone. However, as long as relatively favorable economic and international conditions prevail, moderate forces in Austria will remain vigorous enough to insure the maintenance of political democracy and stability.

18. As long as Austria maintains its economic health the small parties of the extreme right and left appear to have virtually no chance of increasing their present limited political effectiveness or popular support. The next general election will almost certainly result

in a further decline of Independent Party strength. Many of the conditions that once fostered right-wing extremism have been eliminated, and the fragmented Independents will probably drift to both major parties. The outlook for the Communist Party following the Soviet withdrawal is bleak; its strength will almost certainly decline at the next general election. However, in the event of markedly deteriorating economic conditions in the post-election period there would be a substantial increase in the number of Austrians who would be willing to adhere to an extremist political organization with pan-German tendencies. Under those conditions, Communist strength might also increase.

II. ECONOMIC TRENDS

19. As a result of extraordinary recovery and industrial expansion, assisted by over one billion dollars in US aid, the Austrian economy is in a much stronger position than it was in 1937. The prewar conviction of the Austrians that their country did not form a viable economic unit has been largely dispelled. However, even more than most Western European countries, Austria is highly vulnerable to shifts in world economic conditions.

20. *Current conditions.* Austria's GNP in US FY 1955 (converted at the official exchange rate) is estimated to have been about \$3,350,000,000. Although this represents an increase of 40 percent over 1937 in real terms, per capita GNP is still below the Western European average. Industrial production has doubled since 1937, while agricultural production is only slightly above prewar levels. Employment in the inflated services sector of the economy has been sharply reduced, while industrial employment has been expanded. At present about 40 percent of the labor force is employed in industry and about 32 percent in agriculture. Wartime investments by Germany, postwar US aid, and additional government expenditures have brought about a marked shift from the manufacture of consumer goods to that of capital goods. Austria's substantial resources of timber, ores, fuel, and hydroelectric power have been de-

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veloped. Two major new industries, petroleum and aluminum, were also developed during World War II. These large investments and new enterprises have laid the basis for further gains in productivity and general economic growth.

21. On the other hand, Austria's economic growth and stability remain subject to certain handicaps: (a) industrial, agricultural, and labor elements seek to protect themselves with rigid regulatory systems which hamper adjustment to new conditions and render the economy vulnerable to inflation; (b) low incomes and fear of currency depreciation make it difficult to mobilize investment funds without recourse to inflationary financing; and (c) Austria's heavy dependence on foreign trade makes it extremely vulnerable to any decline in world economic activity or to any retrogression in the trade liberalization policies of the West.

22. Heavily dependent on imports of industrial raw materials and food, Austria at the close of World War II faced serious problems due to unfavorable terms of trade and the shrinkage in its traditional Eastern European markets. With the help of US aid, Austria has adjusted to these problems. The volume of all exports in 1954 was 77 percent greater than in 1937, while imports had risen by only 21 percent. Austrian trade has been redirected toward the West. Trade with Eastern Europe has declined from 33 percent of the total in 1937 to about 9 percent. However, Austria still receives a significant proportion (about 20 percent) of its coal imports from the Satellites.

23. Growth in purchasing power, combined with relaxed import restrictions and 1954 flood damage, resulted in a greatly increased level of imports in late 1954 and early 1955. Exports have not expanded enough to prevent a substantial trade deficit, currently running at an annual rate of about \$200 million. As a consequence, Austria's small 1954 surplus in its European Payments Union cumulative net position has been replaced by a growing deficit, amounting to \$86 million by May 1955. Although prices have remained stable since

1952, the trade deficit, sharply expanded bank credit, and the appearance of labor and material bottlenecks recently caused the government to raise the discount rate, to increase reserve requirements, and to defer certain public investments in an attempt to contain inflationary pressures.

24. *Economic effects of the end of Occupation.* Under the provisions of the State Treaty, Austria must pay the USSR — either in goods or in cash — \$25 million annually for six years as compensation for the Soviet-controlled (USIA) enterprises. Austria is also to deliver one million tons of petroleum annually to the USSR during the next ten years in payment for the Soviet-held oil fields.¹ Moreover, the removal of occupation forces will probably cause an annual loss of \$45 million in foreign exchange after allowance is made for transfer of properties to productive purposes. Additional imports of about \$5 to 10 million may be required during the establishment of a national army. This figure would have to be substantially higher if Austria does not receive grants of basic military equipment from external sources.

25. Austria will therefore have a gross loss of foreign exchange on the order of \$80 million annually. On the other hand, Austria gains control over two-thirds of the present petroleum output and over the entire USIA output, estimated at about 10 percent of total net production of manufactured goods. There are no concrete data on the profits or present condition of the USIA and oil properties being returned to Austria. However, the net accretion of foreign exchange to Austria from the oil properties may amount to as much as \$15 million in the first year of independence, provided that oil production can be maintained at the estimated present level of 3.4 million tons annually. A roughly similar return will be possible in succeeding years if production keeps pace with growing domestic requirements. The total net accrual of foreign exchange to Austria from the USIA enterprises

¹ Austria also is to make lump payments of \$20 million for USIA inventories and of \$2 million for the assets of the Danube Steamship Company.

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may be about \$12 million. Consequently, the net adverse impact of the end of occupation on Austria's balance of payments will probably be roughly \$50 million annually over the next few years. However, this loss will probably gradually be offset by expanded exports resulting from economic growth, and by new foreign investments which have been withheld during the Soviet occupation. Meanwhile, Austria's cushion of gold and dollar reserves of about \$330 million should be sufficient to protect Austria's balance of payments, provided that domestic inflationary forces are kept under control.

26. The restoration of Austria's independence in itself will have only limited adverse effects on internal financial stability. On an annual basis, payments to the USSR probably will be less than the estimated Soviet profits extracted from Austria in the recent past. The creation of an Austrian Army on the scale now planned may constitute an additional burden of about \$28 million in the first year and about twice that amount in the second year. There will also be capital requirements for the rehabilitation of the oil and USIA properties; but these expenditures will be small in relation to Austria's total resources, and the investments probably will yield relatively quick returns. However, since this additional effort is required at a time when Austria's resources are already strained by an economic boom, the danger of a renewed inflationary spiral cannot be excluded.

27. The predominately westward direction of Austria's foreign trade is not likely to be significantly altered by the nondiscrimination provisions of the State Treaty. On the other hand, Austrian cooperation with the West's strategic trade controls will probably deteriorate. Austria's attempts to expand the overall volume of its trade will almost certainly be accompanied by a special effort to increase its trade with Eastern Europe. Nevertheless, the proportion of Austrian trade with the Bloc is not likely to increase substantially unless: (a) the Bloc is able to satisfy Austrian import requirements far more adequately than in the past; (b) inflation makes Austrian goods non-competitive in Western markets; or (c) West-

ern demands for Austria's products declines for other reasons.

28. *Economic prospects.* Austria's postwar recovery has provided a strong base for further economic growth. The restoration of independence will have a stimulating effect on investment, production, and exports. Provided inflationary pressures are checked, we believe that Austria can probably overcome its short-run balance of payments difficulties and liquidate its obligations under the State Treaty. Under such circumstances, and barring a marked decrease in world demand for Austrian products, over the longer term Austria's rate of economic growth will probably exceed the Western European average.

III. MILITARY DEVELOPMENTS

29. The State Treaty does not limit the size of the Austrian military forces, but does prohibit the manufacture or possession of weapons of mass destruction, guided missiles, and certain other categories of arms. Austria is committed not to join any military alliance and not to permit the establishment of foreign military bases on its territory.

30. Austria's security forces at present consist of the Federal Police (16,500 men) in the major cities, of the Gendarmerie (10,200) in the rural areas, and of the Special Gendarmerie, a 6,500-man force trained in the Western occupation zones. The Austrian government plans to use the Special Gendarmerie as the cadre for the new army. Its state of training is excellent, although little training in infantry heavy weapons has been undertaken. Most of its officers and many of its NCO's have had extensive combat experience, in many cases against the Soviet Army. Its loyalty is unquestioned, and Communist penetration has been negligible.

31. The creation of an army will probably cause some dissension within the coalition government. However, both major parties are mindful of Austria's dangerous experiences under similar conditions after World War I and are attempting to minimize their differences. Austria's armed forces have been

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placed directly under the Chancellery. Basic policy questions thus will be reviewed by leaders of both major parties. There is also coalition agreement on such issues as term of military service, creation of a professional officer corps, establishment of reserves, and introduction of a volunteer system. Most political leaders agree that Austria needs an effective military establishment in order to pursue a policy of genuine neutrality. Therefore, we believe that the military issue of itself probably will not cause serious strains on coalition unity.

32. The speed with which the army is created will be limited by political and economic considerations. The Socialists will insist on extensive political and parliamentary controls, especially on army personnel policies. Both parties will be influenced by budgetary considerations and will be reluctant to endanger economic expansion by diverting financial and manpower resources to the army. Problems involving parliamentary controls and the army's organization also remain to be resolved. Thus, while Austria will probably hold to its program of building up the army to the level of 55,000 men, this almost certainly will not be accomplished within the scheduled two-year period.

33. Present plans call initially for an army of 25-30,000 men. Organizational plans have not yet been firmly established. Planned military appropriations for the first year of the build-up will barely cover the maintenance of 30,000 men. Government authorities have accepted the US stockpile of weapons and basic equipment which has been held in readiness. Further expansion will depend on the receipt of foreign assistance. Although Austria would prefer to rely on Western aid, it will be careful to avoid any appearance of violating its neutrality, and therefore might be prepared to accept at least token Soviet military aid provided no strings were attached, and provided it did not introduce too great an element of heterogeneity into the army's equipment.

34. The Austrian Army probably will not exceed a strength of 55,000 men in the foreseeable future. The forces available after the

first year of independence probably will be able to do no more than maintain internal security. However, at its planned full strength the army probably will be able to carry out limited delaying actions in the event of invasion.

IV. PROBABLE FOREIGN POLICY

35. Austria will seek to maintain a delicately balanced position between the two great power blocs, and to exploit its independent role for whatever advantage can be gained from either side. Austrians are vigorously pro-Western but they face the problem of trying to retain the moral and political support of the Western Powers while avoiding actions which might dangerously antagonize the Soviet Bloc. Austria believes that the present world balance of power will enable it to maintain its neutral position. Most Austrians believe that the deterrent power of the US will provide continued protection, even though they hold to a strictly neutral position on cold war issues, provided only that Austria maintains its domestic anti-Communist policy. Austria thus probably hopes to be able to remain aloof in the cold war and to benefit from Western protection without paying the price either of an arms contribution to NATO or of a strong military effort of its own.

36. Under existing world conditions, Austria will almost certainly remain alert toward the internal Communist threat and will resist subversive attempts by its Satellite neighbors. Nevertheless, the Austrians may be especially vulnerable to Bloc protests in connection with granting asylum to future Iron Curtain refugees. Without abandoning the principle of asylum, the Austrian authorities will be likely to make it increasingly difficult for new refugees to reach or to remain in Austria. They will, however, probably continue to cooperate with Western agencies in supporting and resettling refugees now in the country. In keeping with its policy of neutrality, Austria will permit international Communist organizations to maintain headquarters or hold meetings in Vienna so long as they do not endanger internal security or governmental stability. In order to offset this, Austria may encourage

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the establishment of international non-Communist organizations in Vienna.

37. Concern for its neutrality and fear of provoking the USSR will inhibit Austria's military cooperation with the West. While a few top-ranking officials may covertly discuss military plans and dispositions with the West, it is unlikely that any specific commitments will be contemplated. The Austrians would probably calculate that: (a) substantial military contacts with the West would involve an unnecessary risk of antagonizing the Soviets; (b) such contacts would not aid in halting a Bloc invasion at the borders or in saving the large population centers in the eastern half of the country; and (c) the main weight of the West's protective value lies in its deterrent power which would operate regardless of any Austrian military commitment.

38. Austria's relations with its non-Bloc neighbors are likely to develop favorably despite occasional disturbances stemming from such issues as Italy's administration of the South Tyrol. The State Treaty bans the return of assets in Austria to former German owners. The West Germans appear to be grudgingly abandoning hope of obtaining a satisfactory set-

tlement from the Austrians for wartime German capital investments. However, since Austria needs new investments and tourists, it will seek to improve relations with West Germany and probably will compensate many Germans, especially those who made pre-*Anschluss* investments.

39. Austria has indicated its intention of applying for membership in the United Nations and in the Council of Europe, in addition to maintaining membership in international agencies such as OEEC and EPU. If the USSR should oppose a policy of association with Western organizations as being incompatible with Austria's neutrality policy, the Austrians nevertheless would probably feel safe in joining, wherever they could point to the fact of Swiss or Swedish membership. Austria may also seek associate membership in the Coal and Steel Community (CSC). However, we believe that it would not join the CSC in the face of strong Soviet objection. Austria will probably apply for membership in the East Danube Commission in order to gain access to the entire river and thus make progress toward restoring the Austrian prewar shipping position.

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