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Detente and US-Soviet Trade

Long standing hostility and reciprocal barriers have kept the level of US-Soviet trade at a low level. In 1971 two-way trade amounted to about $220 million, representing only about 4% of East-West trade turnover. US exports to the USSR have increased almost three-fold since 1968 (see table), but at $162 million, the value of US exports to the USSR in 1971 was well below that of the USSR's major Western trade partners -- West Germany, Japan, France and Italy. The expansion of US exports in the last three years apparently is unrelated either to detente or to unilateral US moves to expand such trade. Expansion has occurred largely in goods normally bought in the United States -- goods that are not normally available elsewhere in the quantity or quality that the US can furnish, such as aluminum oxide, cattle hides, ore mining equipment, ~~and others~~. feedgrains and others.

The impact of detente and US unilateral moves made in 1971 will be apparent in trade flows in 1972 and beyond. The United States relaxed licensing restrictions on exports of motor vehicle manufacturing equipment -- principally machine tools -- in May 1971. This resulted in Soviet orders approximating $90 million for US machine tools. These orders and others for oil and gas pipeline equipment, mining equipment, electronics, and other items totaled about a quarter of a billion dollars in 1971 -- roughly a fourth of all Soviet orders for machinery and equipment placed in the West in that year. Of the total, equipment and technology for the Kama River Plant accounted for only $9 million. The decision to approve licenses for the Kama River Plant was made in November 1971 prior to Commerce Secretary Stans' visit to the Soviet Union. US license approvals for Kama total more than $1 billion. From these the United States might obtain $300-500 million in orders.

The United States in June 1971 eliminated the requirement that 50% of any grain or flour shipments to the USSR, China and Eastern Europe must move in US flag vessels. In November 1971 the USSR placed $160 million in orders for US feed grains. Most of this will move in the first half of 1972. Following the Stans visit and the reciprocal visit by Soviet officials to Washington in January 1972, talks will soon be underway to supply $750 million to $1 billion in US feed grains over the next five years.

The recent exchange of visits between the US and the USSR has pointed up the recent progress in reducing the barriers to expanded trade. The positive Soviet response to US moves reflects, inter alia, the USSR's need for Western technology and equipment. It has seemingly brought a more cooperative attitude toward US complaints about outstanding difficulties such as lend-lease. For its part, the USSR wants a relaxation of US export controls, government (Eximbank) guaranteed credits, and most-favored-nation (MFN) treatment on tariffs for Soviet exports. Probably the most crucial factor for any immediate large increase in this trade is the granting of long-term credits by the US.

If broad agreements are reached on removing trade barriers, US exports to the USSR could well increase from the 1971 level of about $160 million to perhaps $500-600 million by 1975. Such exports would be considerably in excess of imports, and the USSR would still have a large trade deficit just as at present. In 1971, US exports to the USSR exceeded imports by about $100 million. By 1975 the US surplus would be substantially higher because most Soviet exports would not find a market in the United States for the next few years at least.

The bulk of Soviet imports would be in the machinery and equipment category. The USSR has indicated a long list of expensive capital equipment it desires from the West -- automotive manufacturing, deep well drilling, automatic oil transfer and storage, oil refining, rolling mill, off-the road vehicles, computers, instruments, data transmission, and numerically controlled machine tools -- and it considers the US equipment and technology for many of these categories superior to all others. Many of these Soviet needs thus might be purchased from the United States if credit terms can be arranged, although some will be purchased from the US in any case.

The USSR's need for credits to enable it to increase its purchases from the US points up the problem of the limits of the already substantial Soviet debt to the West. Any large orders from the US would lead to a large increase in this indebtedness. Long-term credit/barter arrangements, such as those calling for the exchange of pipe for gas, and cooperation deals (so-called joint ventures) would mitigate the debt problem. The proposals made to other Western countries for oil, gas, copper, and other raw materials development with repayment in products are also being made to the United States, and some may be concluded, e.g., the proposed LNG transaction. The LNG deal could involve billions of dollars with repayment of the credit in LNG shipments to the US.

Developed West and US Trade
with the USSR, 1965-1971

Million US$ a/

	Developed West		United States	
	Exports b/	Imports c/	Exports b/	Imports c/
1965	1,397	1,712	44	43
1966	1,475	1,935	42	50
1967	1,587	2,195	60	41
1968	1,896	2,322	57	58
1969	2,277	2,458	106	51
1970	2,603	2,733	118	72
1971	2,600 e/	2,900 e/	162	58

a. Rounded to nearest million; based on Western statistics.
b. f.o.b.
c. c.i.f. except US (f.a.s.); Canada and South Africa (f.o.b., inland point of shipment); and Australia (f.o.b.).
d. f.a.s.
e. Preliminary estimate.

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The Soviet Economy as a Factor in US-Soviet Political Relations

Introduction

The state of the USSR economy as viewed by its leaders will be an important factor affecting their negotiating posture during the President's visit. Certainly, the current Soviet leadership displays a greater preoccupation with the domestic economy than any of its predecessors. And, like any economy, the Soviet economy has both strengths and weaknesses that permit the leadership to pursue certain noneconomic goals and prohibit it from undertaking others.

The State of the Economy

The USSR is the second largest economy in the world. The basis of Soviet economic strength lies in its great natural wealth, providing self-sufficiency in nearly all important raw materials, and a labor force that is about half again as large as the US. Deployed under strong central direction, these resources have permitted rates of economic growth that are high by international standards, a military complex about equal to that of the US, and a steadily rising standard of living.

During the Eighth Five-Year Plan (1966-70), Soviet GNP grew at an annual rate of 5½ percent. By comparison the rate posted in 1961-65 was about 5 percent and for the decade of the 1950s about 6 percent. Because of the wide fluctuation in agricultural production, however, year-to-year growth in GNP has varied considerably in recent years -- from a low of 2.5 percent in 1969 to a high of 8.2 percent in 1970. All of the increase in the growth rate of GNP since 1965 can be attributed to an improved performance in agriculture and construction. Industry, the largest contributing sector to GNP, grew at about the same pace as in the first half of the decade. The rate of growth of Soviet GNP for the past five years was less than half that of Japan, roughly the same as that of France and Italy, but substantially above that of the United States, West Germany, and Great Britain.

Preliminary results for 1971 suggest that, contrary to planners'hopes, the new Soviet five-year plan got off to a slow start. Gross national product grew by only about 3.5 percent. A decline in agricultural output from the record level in 1970 was largely responsible, but the pace of industrial growth also sagged, especially in the last six months of the year. The failure to meet the goals for labor productivity and for putting new plant and equipment into use suggests that some of the key goals of the five-year plan are threatened.

In the new five-year plan ending in 1975, the main objectives of Soviet economic policy remain roughly the same as in recent years. The average annual rates of increase planned for GNP and industry are somewhat above the average annual growth achieved in 1966-70. No major shifts are apparent in the allocation of resources among the principal claimants -- defense, investment, and consumption. As before, investment is to grow at a slightly higher annual rate (6½) than GNP, and consumption at a lower rate (5%). The directives place unusual emphasis on bettering the lot of the consumer, but the figures given imply that the rate of progress planned for the standard of living is somewhat lower than that achieved in 1966-70. Although the available data do not permit precise estimates of defense outlays, it appears that the plan would allow expenditures for military and space programs to rise at least as rapidly as GNP.

Most Western (and many Soviet) observers believe that the economy of the USSR faces a number of serious economic challenges including: (1) declining rates of growth, (2) discontent among consumers, (3) low efficiency caused partly by a marked gap between Soviet and Western technology, and (4) an agricultural sector that remains the Achilles' heel of the Soviet economy, absorbing vast resources and retarding overall growth. Although it has been argued that these problems are a strong inducement to the Soviets to seek a SALT agreement and to increase trade with the US, Soviet leaders rightfully view such agreements with the West as no panacea for domestic economic problems.

Economic Implications of a SALT Agreement

The short-run economic benefits of a SALT agreement are limited and insufficient to make an agreement compelling for the USSR. The USSR has achieved parity with the US in important military areas, and continued economic growth will permit maintenance of the parity without adding to the share of resources devoted to military programs. Moreover, the amount of resources likely to be released under the kind of agreement being discussed does not bulk large in relation to the scale of economic activity. If, for example, the rubles that might be saved in the next few years from a curb on strategic programs could be transfered entirely to investment projects, the effect on the growth of fixed capital would be too small to raise the rate of economic growth appreciably. Moreover, whereas swords may be beaten into plowshares, the transferability of the resources of the missile programs and military R&D is limited in the short run and problematical in the longer run.

Potential long term economic benefits may be a more persuasive factor for entering into a SALT-type agreement. Having achieved military parity, the Soviets probably believe that the US will spend enough to prevent Soviet superiority, so that a new round spending to arrive at the same "relation of forces" would only be a waste. Moreover, knowing US capabilities, especially in R&D, they cannot be sure they could keep pace if military spending spirals.

<u>The Effect on the Soviet Economy of Expanded Trade with the US</u>

Despite a bent toward self-sufficiency, the USSR has traded with Western nations when there were clear advantages in doing so. Usually, the USSR has used its limited foreign exchange to import Western technology.

The technological gap, however, remains, and productivity is low. The relatively low standard of living provided to Soviet workers explains some of the differences between productivity in the USSR and in the West. To improve incentives and dampen consumer discontent -- the lesson of the 1970 riots in Poland has not been lost on Soviet leaders -- agricultural products and consumer goods have been purchased abroad in increasing amounts. Indeed, the rush to spend hard curency on feed grains in the past few months after two good harvests seems explicable only by a determination that the plans to increase meat consumption shall not fail.

The USSR can buy most industrial and agricultural products in other western countries, but some kinds of machinery, some licenses, and some agricultural products (feed grains and concentrates in the quantities desired) can be purchased only from the US. To this extent, at least, the Soviet leadership has reason to promote trade with the US. Nevertheless, the volume of such trade will be limited, and its contribution to the economy will be small, except perhaps in agriculture.