

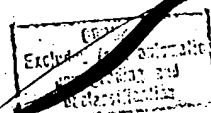
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OUTLOOK FOR CHILEAN-SOVIET ECONOMIC RELATIONS

18 January 1968

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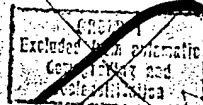
## Outlook for Chilean-Soviet Economic Relations

During the next several years, Chile may well take further positive steps toward closer economic relations with the USSR -- especially if the Frei government is succeeded in 1970 by one that is more leftist and less friendly to the United States. The Chilean foreign minister's impending trip to Moscow probably has the purpose of negotiating details on the use of the Soviet credits extended last year, discussing plans for trade expansion, and (conceivably) arranging additional Soviet aid. Although Chile seems to be modifying its traditional foreign economic orientation, closer economic relations with the USSR face various obstacles. It thus seems unlikely that Soviet aid and trade activity in Chile will assume appreciable economic importance during the next several years, however significant it might become politically.

### The Recent Soviet Credits in Perspective

Chile received its first economic aid commitments from the USSR in January 1967, joining Argentina and Brazil as the only Latin American countries that have accepted Soviet aid offers. Chile received two credit extensions amounting to \$54.8 million (\$57.0 million less a down payment of \$2.2 million on one of the credits). This total compares with commitments of \$115 million to Argentina and \$103 million to Brazil. Chile (as well as Brazil) is authorized to make a substantial part of the aid commitment available to the private sector -- an ideological concession promoted by unwillingness or inability to use large Soviet credits for public investment programs.

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Like the bulk of Soviet aid extensions to Argentina and Brazil, the commitments to Chile are trade credits. Such credits generally carry higher interest rates, have shorter repayment periods, and are less closely tied to specific projects than the credits that characterize the Soviet program in the rest of the world. The credits to Chile carry interest rates of 3 and  $3\frac{1}{2}$  percent, compared with the 4-percent rate specified for the trade credit of \$100 million extended to Brazil in 1966. Repayment over a period of 8 years (the typical period for trade credits) is indicated for some projects or contracts under the credits, while up to 12 years is prescribed for others. Although less favorable than the terms allowed for many US aid credits (not to mention the large portion of US aid disbursed as grants), the terms of the Soviet-Chilean agreement represent substantial concessions from regular commercial arrangements for such credits.

How the credits are supposed to be repaid is not entirely clear. For example, the precise share of the repayment to be made in convertible currencies is not specified. The treaty authorizes part of the repayment to be used to buy Chilean goods, but the USSR is not committed to the purchase of any specific types or amounts. This and other aspects of the repayment question probably have not been worked out yet.

Chilean Foreign Minister's Prospective Trip to Moscow

The most obvious reason for the Chilean foreign minister's expected trip to Moscow this month or next is negotiation of details of last year's economic agreements. The countries also may sign trade agreements that

would formalize and supplement the exchanges of goods envisaged in the aid agreements. Announcement of additional Soviet economic credits cannot be ruled out, if the Chilean government believes it must further mollify the country's leftist political elements or wants to underscore its dismay with US aid policies.

The necessary next step in implementing the credits extended last year is Chilean-Soviet agreement on their specific uses. The USSR seems to be taking the initiative in project planning. It already has suggested that the \$42-million credit be used for a copper rolling mill, a copper and molybdenum refinery, a petro-chemical plant, a lubricating oil refinery, a factory producing prefabricated housing material, and the improvement of port facilities. All of these projects would fill obvious needs in Chile. The National Development Corporation (CORFO) has been considering these projects, but none have yet been officially approved. Whether Chile has alternative projects to propose to the USSR is not known.

Specific arrangements for repayment of the Soviet credits also might be discussed at the prospective meeting. The aid program could founder on this point. Chile is interested mainly in diversifying its exports by finding new markets for such products as shoes, other leather goods, wood and paper products, fishmeal, processed fruits, and wine. It is not eager to divert to the USSR the copper that can easily be sold -- at least at present -- for hard currency in established Western markets. The USSR, on the other hand, has no particular need for simple manufactures and foodstuffs but is interested in importing metals.

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Although negotiation of additional credits at this meeting seems premature, it cannot be ruled out. The USSR has in the past shown a willingness to provide more aid to Latin American countries than they have accepted and easily had the capability to do so. A further aid extension of (say) \$50 million -- implementation of which would be spread over a number of years -- would add little to Soviet deliveries of economic aid, which have been running at about \$500 million annually. The USSR thus would have no problem in enlarging its aid commitment, should the Chileans desire this for political reasons.

#### Outlook for Aid and Trade Activity

Since the projects to be supported by Soviet aid are yet to be determined, the credits have had few practical results so far. Some machine tools and light equipment are said to have been sold to small Chilean enterprises under the \$12.8-million credit, but the large, credit-worthy companies have shown little interest in Soviet goods under any terms. Chilean doubts about the quality of Soviet goods, the compatibility of Soviet equipment with that previously obtained from Western countries, and availability of servicing and spare parts have prevented even a modest development of trade and probably will continue to impede it.

Other economic and political considerations also may hamper Communist aid and trade activity in Chile. Soviet aid normally involves the presence of Soviet advisors and other technical personnel. Many Latin American countries fear the opportunities that their presence would provide for subversion.

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Inasmuch as the USSR will not ordinarily accept complete responsibility for the construction and equipping of a facility (that is, supply it on a turn-key basis), implementation of Soviet credits necessarily makes financial and technical demands on the recipient country -- demands that Chile might not be willing or able to meet. This problem may be particularly important if acceptance of the credit reflected political maneuvering rather than pressing economic need.

The experience of other Latin American countries in using Communist aid also is instructive. Brazil has drawn only about 10 percent of Communist credits of \$306 million, three-fifths of which were extended before 1963. Argentina used only 29 percent of a \$100-million Soviet credit extended in 1958 before it expired in 1961.

#### Chilean and Soviet Motives

Chile's acceptance of Soviet credits and professed interest in expanded trade has a predominantly political basis. Frei's program has espoused the achievement of increased national economic sovereignty, calling for less dependence on the US and increased relations with the USSR. In addition, leftist parties and the radical element of the PDC have pressed the government to take even greater initiative in developing Soviet-Chilean relations.

No urgent economic need for Soviet aid is evident. Although the rate of growth of gross national product slowed in 1967 (estimated at 3 percent as compared with 10 percent in 1966), the country's average rate of growth

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in recent years has exceeded that of Latin America as a whole.

Continuing strong world demand for copper has boosted export earnings and tax receipts. The inflow of long-term investment funds and suppliers' credits from the US and Western Europe has continued and has helped to spur the rapid growth of imports of machinery and other capital goods during 1967. Progress has been made in slowing the rise in the cost of living, and an agricultural development program of considerable potential importance has been begun. Important economic problems remain, of course, and the economy is highly vulnerable to any deterioration of market conditions for copper. Moreover, the level of US aid declined in 1967 and may well decline further in 1968 if Chile purchases supersonic jet fighters in the face of recent US legislative restrictions on aid under such circumstances.

In its effort to win friends and promote its interests, the USSR has cast a very large net with its economic aid program. The program now embraces 40 Free World countries of varying political coloration. The initiation of sizable aid and trade activities with Chile no doubt has attractions for the USSR because of the wide influence of leftist groups in Chile and because of the dissatisfaction of other political elements with the extensiveness of US interests. Judging from past experience, however, the USSR will pursue this opportunity -- in the economic field -- in a fairly deliberate and hard-headed way.

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Supplementary Information on  
Outlook for Chilean-Soviet Economic Relations

Soviet Motives

The USSR has used commercial relationships and economic assistance during the past decade to support overall Soviet international political objectives as well as to satisfy its economic requirements. By strengthening economic ties with the less developed countries, the USSR has projected its presence into the developing world in the hope that it will reduce and eventually eliminate Western influence.

In Latin America, the USSR is intensifying its efforts to expand trade and aid activities. This initiative reflects a Soviet thrust into new markets as well as a step toward improving state-to-state relations and eventually injecting the Soviet presence into Latin America. Mazin, reporting in Pravda the increase in Soviet-Latin American trade during 1966, notes that "Trade brings nations closer together" and "...weakens their dependence on imperialist powers, especially the US.

As part of its long-run strategy of penetration as well as fulfilling more immediate economic requirements, the USSR is willing to expand trade and extend economic aid to Latin American countries without regard to their political orientation. Just as it has extended aid to Western-oriented countries in the Middle East (Iran and Turkey), the USSR is willing to extend aid to Argentina in Latin America. Beyond the \$200 million of economic aid already extended to Latin American countries, the USSR has made offers of at least \$200 million in additional aid to these countries during the past year. Offers were made to: Argentina for participation in the construction of a huge hydropower complex; Colombia for the petroleum industry; Costa Rica for an industrial complex and port facilities; and to Ecuador and Uruguay for the purchase of machinery and equipment.

Soviet motivation for its recent economic efforts in Chile appears to be no different than in the other countries of Latin America. Formal Soviet-Chilean relations were initiated in 1964 with the signing of a cultural agreement and the establishment of diplomatic relations; in 1965 the USSR participated in the Santiago International Fair and established a Cultural Institute in Santiago; in 1966, modest beginnings were made in trade between the two countries; and early in 1967 three economic accords, including credits for state sector projects, were signed. The economic rationale for recent Soviet initiatives in Chile is quite clear (i.e., the expansion of its markets into Latin America and possible future purchases of Chilean copper) but Moscow hopes that the economic ties will eventually lead to closer political relations as well.

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Recent project credits ~~extended to value~~, which are identified as "commercial" (trade) credits may, in fact, go somewhat beyond the usual trade credits. The repayment conditions provide for a range of terms (8-12 years for amortization and 3-3.5 percent for interest) which are not associated with specific uses. The softer terms (12 years to repay and 3 percent interest) undoubtedly apply to credits for State enterprises while the harder terms apply to credits for private enterprise. This would be consistent with the Soviet objective of strengthening the state sector of developing countries as a step toward socialism.

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5 January 1968

MEMORANDUM FOR: Chief, Economic Research

SUBJECT : Request for Paper on Possible Chilean/Soviet Trade

1. The U. S. Ambassador to Chile has requested an Agency study to reflect any possible trade and credit arrangements (including concessionary) the Soviets are likely to offer the Chileans in talks to be held in Moscow with Chilean Foreign Ministry personnel.

2. Inasmuch as the Chilean Foreign Minister is expected to leave for Moscow in January or February 1968, we believe we should respond to the Ambassador's request as soon as possible.

3. Attached are two copies of a cable containing the Ambassador's information to be used as a briefing paper for the Ambassador.

4. Please let us know if our office can be of assistance to you in the servicing of the Ambassador's request.

Attachments: Cables

*all copy cables*

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