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14 AUG 1963

MEMORANDUM FOR: Mr. Allan Evans
Deputy Director for Research
Office of Intelligence and Research
Department of State
Washington, D. C.

SUBJECT: Transmission of Material on East-West Trade Requested by Mr. Morris Crawford

The attached paper, which is addressed to answering a number of specific questions relating to East-West trade, was prepared at the request of Mr. Morris Crawford, 19 July 1963.

Assistant Director

Enclosures: (30)
"Material for Use by US Representative in ECE Export Group on East-West Trade Questions," dated 14 August 1963

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Material for Use by US Representative in ECE Export Group on East-West Trade Questions

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prepared by

CENTRAL INTELLIGENCE AGENCY

Office of Research and Reports

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Material for Use by US Representative in ECE Export Group on East-West Trade Questions

Customs Tariff Systems in the Soviet Bloc

The customs tariff systems of most of the countries in the Soviet Bloc provide for double-column tariffs with minimum rates to be levied against goods imported from countries according MFN treatment to the individual Bloc country and maximum rates to be applied to goods from other countries. Minimal rates concede free entry to the majority of goods imported from the West, such as machinery and equipment, chemicals, fuels, and raw materials. Maximum rates usually impose a 7-20 percent duty on imports of those goods essential to the domestic economy, with considerably higher rates for imports of such non-essentials as manufactured consumer goods. In most Bloc countries, when goods are imported at higher rates, the foreign trade corporation bears the additional cost in terms of its internal accounting and plan fulfillment.

The tariff system currently in force in the Soviet Bloc is patterned on the October 1961 tariff reform of the Soviet Union. The Soviet measure was specifically drafted to provide a commercial bargaining tool to be used in negotiations with the EEC and EFTA. Neither the Soviet Union nor any other Bloc country considers membership in a European custom union as legitimate grounds for an exception to the extension of MFN treatment.

Within this Bloc tariff model there exist certain deviations, based on the individual circumstances of a particular country. Czechoslovakia as a member of GATT is required to extend MFN treatment to other member countries; however, the Czechoslovak government refuses tariff concessions to the USA and the Federal Republic of Germany, despite its GATT commitment. East German tariff negotiations are tied to the problem of recognition of the GDR as a sovereign state, as a result of which very restricted MFN arrangements exist between East Germany and non-Communist countries. The Polish tariff system is not of the same character as those elsewhere in the Soviet Bloc. The current customs system was established in Poland on 21 July 1960. Goods imported on the basis of yearly plans are duty free, whereas other goods are subject to Column I or II tariffs, depending upon the quantity imported. Column I rates apply to goods imported in quantities not exceeding the amounts given in that column. Column II rates apply to other listed goods and to excess quantities of Column I items imported. Certain specified commodities, including non-ferrous metals, fertilizers, timber, and flour, are imported duty-free, regardless of quantity. There is no information available on the current tariff system of Albania.

The Effect of Customs Tariffs on Bloc Imports

Generally, the customs tariffs on Bloc countries have no real effect either on the volume or the sources of Bloc imports. The state monopoly of foreign trade and the divorce of foreign trade prices from final domestic prices for all practical purposes eliminate the effect on Bloc foreign trade that customs tariffs have in Western countries.

Although affecting only a relatively small volume of trade, the fact that customs duties are paid by the importing foreign trade corporation may serve as an indirect tool for control of foreign trade because bonuses are paid on the basis of the trading company "profits". To the extent that a higher tariff can be avoided by purchasing from a List I country, the profits of the foreign trading company in terms of internal accounting are increased. This, in turn, may discourage the trading company from contracting for purchases in countries from which its government has withdrawn MFN treatment. However, since foreign trade is a state monopoly, this indirect control on the direction of trade may be nullified by executive order at any time, without penalty to the trading corporation, in order to conclude a particular trading transaction. For instance, it is doubtful that Czechoslovakia's import of soybeans from the US in 1961 as a result of their unavailability from Communist China or from a MFN source actually caused the Czechoslovak trading enterprise, KOOSPOL, to be charged the higher tariff legally applicable to imports from the United States, which is a non-MFN country. To obtain the soybeans in the quantity required, the duty increment applicable to imports from the United States was probably either waived or paid from the Czechoslovak state budget.

A tariff has no effect on foreign exchange requirements (except insofar as the direction of trade might alter the type of exchange needed) because the amount paid in foreign exchange by the National Bank of a Bloc country on behalf of the Bloc importer is the same, whether a higher or lower customs tariff in domestic currency is charged to the foreign trade importing corporation by the Bloc government. Furthermore, the difference in domestic currency between the foreign trade price and the domestic price is not retained by the trade enterprise, but is paid into the state budget, whether in the form of customs duties or "profits" paid into the Compensation Fund.*

A non-Bloc nation can expect to gain little from being accorded MFN treatment by a Bloc country. The MFN concept was designed for trade among nations whose chief weapon of commercial policy was the tariff. A nation extended MFN treatment could legitimately claim discrimination if its goods were later subject to a duty higher than that levied against identical goods from "the most favored nation." In the case of a Bloc country, however, the state trading monopoly

* In terms of internal accounts, the importer will have a larger "profit" in the case where the tariff is smaller.

can increase, reduce, or eliminate its purchases in a given country by administrative fiat without making any change in its tariff legislation; hence it is virtually impossible for the affected country to prove discrimination. Nevertheless, trade can be affected when a Bloc country withdraws MFN treatment. Retaliatory increases in Czechoslovak duties were put into effect against Switzerland on 1 January 1960 as a result of Swiss tariff changes.

The New Intra-Bloc Multilateralism

The CEMA scheme for intra-Bloc "multilateral clearing" which is to become operative in January 1964 will be a departure from present Bloc trading practice but will differ markedly from Western multilateralism. Currency convertibility lacking in the Bloc, is the basis of multilateralism in the West where convertible currency holdings resulting from sales in one country can represent claims on products in any other country. While the new CEMA multilateral clearing system should facilitate expansion of intra-Bloc trade exchanges, it will not allow free transferability of credit balances with Bloc countries, and represents no move toward convertibility or free transferability of any Bloc currency.

For the Bloc multilateral clearing will mean that each Bloc country will be able to plan to balance its demands and its obligations arising from foreign trade, services performed, and other exchanges multilaterally, with all the other countries participating in the clearing agreement. This removes the inherent strictures of the present bilateral system, where planned turnover is limited by the buying or selling limitations of the weaker partner; but it in no way reduces the planned, state-monopoly nature of Bloc trade. All aspects of trade, including bilateral imbalances, will be pre-planned--specified goods in specified quantities from a specified trading partner will be stipulated through the planning process.

The most significant aspect of the shift to multilateral clearing appears to be the fact that the Bloc now face the problem of establishing a Bloc-wide foreign trade price system. The present practice of bilateral negotiation of trade prices must be abandoned if a credit balance acquired by country A in trade with country B is to represent imports of equal value in trade with countries C, D, and E. The establishment of uniform Bloc foreign trade prices is a first step toward true multilateralism; however, complete convertibility will come only when planned economies are willing to accept the disrupting effect of unplanned claims on their goods and services.

Multilateralism in East-West Trade

Because East European currencies are inconvertible on commercial account, trade with the developed West has been conducted on the basis of either bilateral clearing accounts or direct payment in transferable Western currencies. Since the return to convertibility of most West

European currencies in 1958, there has been a trend away from bilateral clearing in East-West trade. Even where clearing arrangements have remained, greater multilateralism has been encouraged because imbalances increasingly have been settled in convertible currencies rather than in commodity deliveries. Bloc export earnings in the West, therefore, are for the most part no longer restricted bilaterally.

In order to remove the remaining restrictions on multilateral trade with the West there are two major lines of approach available to Bloc governments. One approach would be to seek through negotiations the elimination of remaining bilateral clearing agreements, or the reduction of such agreements to shopping lists that do not aim at balanced trade. Where bilateral clearing agreements still exist, however, the Western countries may favor such arrangements due to their own weak trading position and/or balance of payments difficulties. They may, therefore, resist efforts to modify or eliminate such agreements for fear Bloc countries plan to achieve a surplus on trade account with which to pay for higher priority imports elsewhere.

As an alternative, Bloc governments could attempt to expand their multilateral ties with the West by developing a better market for settling clearing balances. The proposed CEMA bank, for example, could be made to serve as broker within the Bloc for the trading of favorable Western clearing balances either against each other, against intra-Bloc balances (in foreign trade rubles), or for free Western currencies.