



National
Foreign
Assessment
Center

~~Confidential~~

APPROVED FOR RELEASE
DATE: FEB 2001

12

Soviet Energy Policy Toward Eastern Europe

An Intelligence Assessment

~~Confidential~~

PA 80-10160
April 1980

Copy 193

**National Security
Information**

~~Unauthorized Disclosure~~
Subject to Criminal Sanctions

**EO 12958 6.1(c)<10Yrs
(U)**

All material on this page
is unclassified.



National
Foreign
Assessment
Center

~~Confidential~~

Soviet Energy Policy Toward Eastern Europe (U)

An Intelligence Assessment

*Research for this report was completed
on 1 March 1980.*

EO 12958 6.1(c)>10<25Yrs
(U)

[REDACTED]
[REDACTED] Office of Political Analysis. It
was coordinated with the Office of Economic
Research and the National Intelligence Officer for
USSR-EE. [REDACTED]
[REDACTED]

~~Confidential~~

PA 80-10160
April 1980

[Next page is blank]

Soviet Energy Policy Toward Eastern Europe * (U)

Key Judgments

The Soviet leadership views the USSR's energy relationship with Eastern Europe in the context of its efforts to increase specialization and division of labor among the Soviet bloc countries, strengthen East European economic dependence on the USSR, and weaken East European ties with the West—that is, to promote bloc economic “integration.” This energy relationship has in fact been the single most important element in the 1970s defining the substantive content of economic integration.

The significance of the energy issue, however, transcends economics. Economic integration is seen by Moscow as one of the three pillars—together with military and political integration—that support Soviet hegemony in this strategically vital region. The manner in which the energy needs of the Soviet client states are satisfied—or not satisfied—is an important factor affecting their economic growth and domestic political stability.

Despite countercurrents and resistance both in Eastern Europe and the USSR, bloc economic integration has gradually increased in recent years. Given Eastern Europe's bleak prospects for substituting imports of energy and raw materials from other suppliers for imports from the USSR, or for substantially expanding exports of manufactured goods to the Western market, the trend toward integration probably will continue in the 1980s. If sustained, this further tilt toward the Soviet Union in the orientation of the East European economies will represent a major political achievement for the Soviet leadership.

Over the last 10 years Soviet energy policy toward Eastern Europe has been characterized by remarkable continuity and consistency. This stability is not surprising, since the policy has been shaped in response to an unchanging set of fundamental Soviet interests:

- To put the brakes on Soviet oil exports to Eastern Europe.
- To recoup the costs of Soviet fuel deliveries to Eastern Europe.
- To assure that East European energy needs are nevertheless met as much as possible.
- To use the energy relationship as a means of strengthening integration.

* This assessment is an overview of a major study of the same title that will be published in the near future.

~~Confidential~~

These interests are not all mutually complementary, however, and in recent years tensions in Soviet policy and conflicts between the USSR and its allies on these issues have grown. The outlook for the 1980s is that these policy dilemmas and conflicts will become still more acute, forcing even tougher choices on Moscow. In the face of potential instability, the Soviets are as likely to demand that their East European allies strengthen discipline or take other political countermeasures to cope with it as they are to attempt to buy it off with more fuel or credits.

The above information is Unclassified.

~~Confidential~~

Soviet Energy Policy Toward Eastern Europe (U)

EO 12958 6.1(c)>10<25Yrs
(U)

The Soviet-East European Dialogue

Despite their domination of key energy-related posts in the institutional structure of the bloc's Council of Economic Mutual Assistance (CEMA), the Soviets have been compelled by the principle of unanimous voting to engage in protracted negotiations as they have attempted to push their strategy through CEMA. Thus, it has taken half a dozen years or more simply to reach agreement on what the bloc energy program ought to be. [REDACTED]

In the negotiations, the East Europeans have argued implicitly that:

- There can be no comprehensive solution to the East European energy problem that depends upon the states in this region substantially meeting their own needs by developing indigenous resources.
- The central element in a bloc energy program must be energy and raw materials deliveries from the USSR.
- The program must address critical near-term energy problems.
- The program should offer long-term guarantees within the CEMA framework for energy supply.
- The costs to the East Europeans must be kept within tolerable limits. [REDACTED]

To a large extent, these arguments have been ignored by the Soviets. The leading Soviet spokesman on CEMA matters, Premier Aleksey Kosygin, has never publicly accepted the premise that the solution of the East European energy problem is basically a *Soviet* responsibility. The themes he has stressed point in the opposite direction: that although the USSR will help, the basic responsibility lies with the East Europeans themselves. Thus Kosygin and other Soviet officials have talked about conservation, the role of coal in the energy balance, the upgrading of secondary refining capacity, nuclear power, synthetic fuels, expansion of the unified electric power grid, and renovation of electric power generating equipment—all areas in which Soviet assistance is possible, but in which the main burden must be borne by the East European economies. [REDACTED]

Soviet Strategy

The Soviets conduct a two-track policy in their energy relations with Eastern Europe, proceeding simultaneously along multilateral and bilateral planes. The main multilateral arena has been CEMA and its various organs. The CEMA forum has been used by the Soviets primarily as a means of channeling bloc economic discussions in the proper direction and of committing allies to agree in principle to various common economic activities. Bilateral relations are used for establishing concretely who should get what and at what cost, and they provide a more private and effective mechanism for the Soviets to bring to bear the full complement of their power resources, to play off one partner against another, and on occasion to make concessions. [REDACTED]

The CEMA Program. The current Soviet strategy for dealing through CEMA with the East European energy problem is embodied in the so-called Power, Fuel and Raw Materials Target Program adopted by the CEMA session of June 1978. The Target Program represents an almost total victory for the Soviet position. It places the burden of responsibility for energy provision basically on the East European states themselves. [REDACTED]

First, it assigns top priority to electric power generation. The increase in electric power supply is to be accomplished in the near term through the expansion of coal-burning thermal power generation, and in the longer run through nuclear energy—to which the Target Program assigns highest priority. Second, the Target Program reflects the Soviet line in its heavy stress on conservation and efficient energy utilization. Third, and most importantly from the East European perspective, the Target Program responds only slightly to the critical East European concern over future Soviet energy deliveries. [REDACTED]

The Target Program includes no joint projects that would guarantee oil to East European states in the 1981-85 plan period and no follow-on to the jointly undertaken

EO 12958 6.1(c)>10<25Yrs
(U)

EO 12958
6.1(c)>10<25Yrs
(U)

EO 12958
6.1(c)>10<25Yrs
(U)

EO 12958
6.1(c)>10<25Yrs
(U)

~~Confidential~~

EO 12958 6.1(c)>10<25Yrs
(U)

Orenburg natural gas pipeline project that has now been essentially completed. The only joint projects now on the books that will guarantee delivery of energy from the USSR to Eastern Europe are two nuclear power plants to be built in the Ukraine. Given the likely lead times for commissioning these plants, there are thus no collective CEMA projects at the moment that will increase Soviet energy deliveries to Eastern Europe in any way during 1981-85. [REDACTED]

Bilateral Dealings. The East European states collectively exercise no influence over the key decisions of how much oil the USSR will export, and what the delivery proportions will be among CEMA, hard-currency, and less developed countries markets. Decisions on exports to individual East European countries are arrived at through strictly bilateral negotiations in which the East European states are able to affect Soviet policy only marginally [REDACTED]

For several years, the Soviets have been telling the East Europeans not to expect significant increases in "planned" oil deliveries during the 1981-85 five year plan period. On occasion they have warned that unless stiff terms are met they may be compelled to reduce the volume of deliveries. The evidence currently available suggests that the Soviets are largely adhering to this line and providing for little increase in oil deliveries for 1981-85 above the 1980 level. The Soviets have tempered their position somewhat by a willingness to discuss marginal deliveries above the 1980 level that would be paid for in hard goods or hard currency. In the negotiations about the USSR's 1981-85 trade agreements with individual East European countries, there are some recent signs that there may be some flexibility in the Soviet position, although the Soviets so far appear to have made only small concessions on the volume, price, or method of payment. [REDACTED]

Currently, it appears that the Soviets intend to intensify rather than relax the oil price pressure on their East European clients during 1981-85. They will probably increase the share in total oil deliveries of so-called "above-plan" oil, which must be paid for in hard currency or goods salable for hard currency (that is, hard goods), and they have shown signs of unwillingness to agree to predetermined prices for such oil. They have been seriously considering moving from the

existing five year base to a three year base (or even shorter period) for calculating the lagged average world market price they use in setting the yearly CEMA oil price. This would raise the price of Soviet oil still closer to the level set by the Organization of Petroleum Exporting Countries (OPEC). There have also been signs that the Soviets might insist on receiving more hard goods for "planned" oil delivered under the five year agreements. In addition, they have generally been very unreceptive to requests from the East Europeans for credits over the 1981-85 period, although there have been recent reports that they may be prepared to help the Poles with ruble credits. [REDACTED]

Policy Dilemmas

If the Soviets are unprepared fully to meet rising East European oil needs, or to meet them at a cost affordable to Eastern Europe, they are in effect telling the East Europeans both to cut back economic growth and consumption and to find oil elsewhere. Fundamentally, additional supplies of oil can only be acquired by Eastern Europe now for hard currency—which in turn can only be earned through exports to Western industrialized nations or oil-producing states and their beneficiaries. [REDACTED]

The East Europeans are being put in the position of having to increase exports to hard currency markets while reducing imports from the West as much as possible (even at the expense of sacrificing equipment and raw materials imports that in the longer run would promote greater hard currency exports). At the same time the East Europeans are being pressed to expand their hard goods trade with the USSR. The pressures on Eastern Europe to export more to the West and to the East are likely to be satisfied, if at all, only through a reduction in consumption. [REDACTED]

This dilemma confronting the East Europeans also poses policy problems for the Soviets, who wish to avoid both political instability arising from consumer frustrations in their East European client states and a more Westward orientation in their trade. The Soviet response so far has been ambivalent. To some extent, the Soviets may believe that the CEMA energy program will satisfactorily resolve the dilemma. The Soviets unquestionably also feel that they have already made major sacrifices to meet East European energy

~~Confidential~~

EO 12958
6.1(c)>10<25Yrs
(U)

EO 12958
6.1(c)>10<25Yrs
(U)

EO 12958
6.1(c)>10<25Yrs
(U)

EO 12958
6.1(c)>10<25Yrs
(U)

EO 12958 6.1(c)>10<25Yrs
(U)

needs, and they resent having to do even more to support living standards that they perceive to be higher than their own. [REDACTED]

EO 12958
6.1(c)>10<25Yrs
(U)

In principle, the Soviets favor strengthening intra-CEMA trade ties and reducing East European dependence on Western trade. But even as Moscow has increasingly pressured the East European states in recent years to direct more trade toward the USSR and to limit their indebtedness to the West, it has tolerated new East European trade arrangements with the West. To be sure, Moscow's tolerance is especially evident in areas that have helped promote specific Soviet political or economic objectives—such as enhancing the prospects for Soviet arms control initiatives or facilitating the transfer to the USSR of Western technology. The Soviets, however, have tended to look the other way rather than meet East European hard currency borrowing needs themselves when this has been the only option. [REDACTED]

EO 12958
6.1(c)>10<25Yrs
(U)

CEMA and the Oil Producing States

The clear and present need of Eastern Europe to supplement Soviet oil with growing OPEC deliveries, and the Soviet political and economic stake in the satisfaction of this need, are the factors that give the USSR even today such a critical interest in assuring rising CEMA imports of oil from other oil-producing states. This interest will further intensify as the USSR's own oil consumption is increasingly constrained by falling oil production. [REDACTED]

EO 12958
6.1(c)>10<25Yrs
(U)

The idea of a joint approach by the CEMA countries to the oil-producing states goes back at least to 1971, and in 1975 CEMA signed cooperation agreements with Mexico and Iraq, although so far nothing much appears to have come from these agreements. In 1978 the notion of a collective CEMA approach to the oil-producing states was elevated to a declared policy objective in the CEMA energy Target Program. The Soviets have probably made the greatest effort to coordinate and control activities in the lucrative and politically sensitive area of arms trade and military assistance. In other economic areas, however, joint CEMA collaboration with oil-producing countries is more problematic: there have certainly been some attempts at it, but often there appears to be either no collaboration or outright competition. [REDACTED]

EO 12958
6.1(c)>10<25Yrs
(U)

Even if Eastern Europe turns more to the West or the Middle East to earn the hard currency needed to purchase additional quantities of oil, its overall energy dependency on the USSR will not be substantially affected. Eastern Europe gets almost all its natural gas, increasing volumes of electric power, and (with the exception of Romania) the major share of its nuclear-related technology imports and all its nuclear fuel from the USSR. Natural gas deliveries will rise in the future, and nuclear ties with the USSR will in time become critical for a majority of East European countries. The point at issue is thus not declining dependency, as some observers have argued, but the degree of *leverage* that a strong persisting dependency will actually provide the Soviets in a situation in which attempts to exploit it could undercut the USSR's own prospective gains from economic integration or threaten political stability in Eastern Europe. [REDACTED]

Outlook: Soviet Energy Policy and Political Instability in Eastern Europe

Moscow is obviously concerned about the possibility of political instability in Eastern Europe (especially in Poland, which is probably the country most vulnerable to mass upheaval), and is prepared at least to listen to the argument that failure by the USSR to satisfy fuel demand in one or another country could precipitate a crisis. Soviet leaders, however, have heard this argument before, and are probably disposed to interpret it in the first instance as a sign of unwillingness on the part of their allies to shoulder a fair share of the burden. Nor does it necessarily follow that the Soviet leadership will be prepared to make concessions on fuel deliveries even if they are convinced there is a threat of political instability. There are limits to disposable Soviet fuel reserves. Under certain conditions Soviet leaders may be prepared to go along with a leader such as Hungary's Kadar, who attempts to employ a muted nationalism as a means of getting people to suffer willingly and quietly. But when push comes to shove the Soviets are as likely to demand that East European regimes strengthen "discipline" or undertake other political countermeasures aimed at coping with impending instability as they are to attempt to buy it off with more fuel or credits. [REDACTED]

EO 12958 6.1(c)>10<25Yrs
(U)

~~Confidential~~

EO 12958 6.1(c)>10<25Yrs
(U)

EO 12958 6.1(c)>10<25Yrs
(U)

Soviet policymakers will probably regard having to use military force to suppress disturbances in Eastern Europe as undesirable. But, under the conditions that are likely to exist in the first half of the 1980s, there will be a limit to the price they will be willing to pay to preempt this eventuality, even if it were to occur in Poland, where the costs of military action could be high. [REDACTED]

The most likely way in which Soviet energy-related behavior might help to precipitate a crisis in Eastern Europe would be through a number of possible miscalculations. There is a reasonable likelihood that the Soviet commitment undertaken in 1979 to maintain oil deliveries to Eastern Europe at the 1980 level during the 1981-85 period, upon which East European production and foreign trade plans for 1981-85 will be based, may be predicated upon the assumption that Soviet oil production can also be stabilized or even slightly increased over this period, rather than decline by 2 to 4 million barrels per day as we predict. [REDACTED]

The Soviets may also have miscalculated the possibilities for implementing the CEMA Target Program:

- The conservation potential in Eastern Europe involves high costs and may not be realized.
- Coal production may be much harder to increase than the Soviets believe (with the added danger of unrest among hard-pressed coal miners).
- Nuclear power plants almost certainly will not be commissioned as scheduled.
- East European hard currency export earnings could fall below anticipated levels.
- Both the East European states and the USSR could have a more difficult time acquiring OPEC oil even at world prices, much less on concessionary terms, than they may have bargained for—as 1979-80 negotiations already suggest. [REDACTED]

The Soviets may also miscalculate energy-induced political developments in Eastern Europe. In their willingness to see living standards lowered in the region if need be, Soviet policymakers may misjudge the tolerance level of East European populations. They may also miscalculate the degree of effective control

and managerial competence exercised by East European regimes in coping with their energy problems. It is highly questionable, for example, whether the Polish leadership even has a real energy policy. [REDACTED]

There are some elements of flexibility in the situation, however, that may ease the pressures on Soviet policymakers. Energy-produced deprivations felt by East European populations to some extent are measured by comparisons with living standards in the West, and these may also be stagnating or declining in the 1980s. In addition, the Soviets have the option of permitting or encouraging East European governments to accept higher hard currency debt service ratios. Assuming Western lenders could be found, such borrowing would provide temporary relief, and—in the case of Poland—it might be repaid through an expansion of coal or electricity exports to Western Europe. Finally, the Soviets have the option of sacrificing their own domestic needs, at least temporarily, in order to supply an East European country in desperate straits with more natural gas, oil, or credits with which to purchase oil on the world market. [REDACTED]

EO 12958 6.1(c)>10<25Yrs
(U)

~~Confidential~~

~~Confidential~~

~~Confidential~~