

CONSEIL DE L'ATLANTIQUE NORD
NORTH ATLANTIC COUNCIL

EXEMPLAIRE
COPY

N° 181

ORIGINAL: ENGLISH
15th November, 1963

NATO CONFIDENTIAL
DOCUMENT
AC/127-D/139

COMMITTEE OF ECONOMIC ADVISERS

COMMUNIST PURCHASES OF WHEAT IN FREE
WORLD MARKETS

(Draft note by the Economics Directorate)

I. SUMMARY AND CONCLUSIONS

The present note attempts briefly to evaluate the importance of recent sales of cereals to Communist countries, both for these countries and for the free world. In addition some tentative conclusions are drawn.

2. The record harvest of 1958, which proved to be an exceptionally good year in most of the Communist countries, gave rise to many expectations that were to be disappointed during the following three years. The first among the Communist countries which had to admit the failure of its economic policy to solve its agricultural problems was Communist China. The results during 1959, 1960 and 1961 brought the Chinese to the verge of famine and, since the USSR was apparently not in a position to fulfil China's needs, forced this country to turn to the free world markets for large-scale imports of grain to escape a major disaster.

3. In early May 1961, Communist China signed a long-term agreement with Canada under which it was to import between June 1961 and December 1963 some 6 million tons of cereals (1 million tons of barley and the rest in wheat and wheat flour). Coming in addition to smaller, earlier orders, the total value of Canadian deliveries for the three calendar years 1961/63, amounted to about \$426.6 million, to be paid 25% in cash and the rest in 270 days(1).

(1) At the time, the Canadian authorities brought the conclusion of their long-term agreement with Communist China to the notice of the Committee of Economic Advisers (meeting of 15th June, 1963). The Canadian Government, while extending its guarantee to a maximum of \$50 million for credits necessary to the Canadian Wheat Board to conclude such large purchases on a short-term basis, justified its decision on the basis of the "substantial benefits" of these deals for the Canadian economy in general. (See AC/127-R/66, Item II(d) and the statement of the Canadian Minister of Agriculture to the House of Commons on the long-term agreement for grain deliveries to Communist China added to the letter of the Canadian Delegation.)

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At the same time large-scale orders of wheat and wheat flour were placed with Australia amounting to over 6 million tons during the three years mentioned, and less important ones, mainly of flour, with France (1.3 million tons), with the Federal Republic of Germany (0.5 million tons) and the Argentine. In total, Communist China imported about 5.6 million tons of cereals in 1961, 5 million in 1962(1) and will probably import over 4.5 million tons in 1963 while further purchases are expected in 1964.

4. The cost of these purchases has been estimated at about \$335 million for 1961 and almost as much for 1962. In order to pay for these deliveries, Communist China undertook to sell gold and silver from her reserves and reduced her imports of other goods from the free world. In addition, the Communist Chinese leaders drastically reversed the order of economic priorities, putting the emphasis on agriculture and light industry instead of heavy industry, and moderated their overambitious targets of extremely rapid, if unbalanced, economic growth.

5. The collapse of the Chinese "Great Leap Forward" policy did not directly affect the grain situation of the Soviet Union, although the USSR had imported from Communist China about 600,000 tons of rice in 1959 and another 400,000 tons in 1960. Chinese rice exports to the USSR were practically stopped during 1961. In 1962, they again reached about 150,000 tons, but China had obviously not recovered from her agricultural failure to the extent that she could have been of any assistance to the USSR in solving the Russian food problems, even if political factors could possibly have been disregarded.

6. In the Soviet Union production of bread grains has in recent years failed to keep pace with the growth of the population and consequently stocks have been depleted. An unusually bad harvest in 1963 has therefore obliged the Soviets to import large quantities of wheat from the West. Although the total volume of these imports cannot yet be stated with certainty, they appear likely to exceed 13 million tons and to cost the Soviet Union about \$1,000 million in hard currency. The European satellites also will probably be obliged to purchase more Western grain this year than in the past.

7. These large-scale purchases by Communist countries of cereals come at a time when Canada has announced an all-time record harvest, and the United States has also enjoyed an excellent crop. In Western Europe, crops have suffered, at least in quality, from the wet summer(2). As a result, Western Europe will probably increase its imports of wheat from North America.

(1) See AC/127-D/129(Revised)

(2) A study on the economic evolution of Western Europe in 1963, just completed by the United Nations Economic Commission for Europe, foresees a slight increase of total production of food, but a decline in the wheat crop in Western Europe of about 15%, as compared to 1962.

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8. These prospects, together with the large-scale Communist wheat deals, have reflected on free world market prices of wheat, which increased by about 15% since the announcements of the Soviet deals. The volume of the deliveries from Australia and America to the Soviet Union has also resulted in a sharp increase of the world freight charges for all bulky cargoes and even for oil tankers. World freight rates for wheat (North American Atlantic coast/Russian ports) in October 1962 were quoted at about \$6 a ton, while at the beginning of November 1963 world charter rates \$12.5 to \$13 a ton. The laid-up shipping has been reduced to a minimum, the bulk of which now consists of ships built during the war and most of the rest of vessels more than 23 years old.

Tentative conclusions

9. It is obvious that the recent wheat deals will have immeasurably more far-reaching repercussions upon the economy of the Soviet Union and possibly those of the European satellites than upon the economy of any exporting Western nations.

10. Among the latter, Canada is the main and only one where the importance of those deals will have any sizeable significance from a purely economic point of view.

11. Given the urgency and the size of the need in the Communist countries for these foodstuff, the argument has been advanced that the opportunity should have been taken to attach political conditions to these sales. Even if the validity of this argument were to be accepted and the advisability of such measures agreed, it is clear that political conditions could have only been attached to the sales if this subject had been discussed within the Alliance and agreement reached upon it before negotiations with the Soviets had commenced.

12. Apart from the benefit that the agricultural sector in the various Western countries will derive from the rise in wheat prices, the gap between the subsidised prices in internal markets and the world prices may possibly be reduced. Among the favourable repercussions of the Soviet wheat purchases for the West, the maritime countries will certainly count the improved shipping situation. But again, this must be set against the probability that many importing countries will see their shipping bill for various bulky cargoes, including coal and mineral ores, as well as oil, increased.

13. The wheat sales demonstrate clearly the efficiency of Western farming methods. At the same time they emphasise the fact that Soviet agriculture has suffered a major set-back, the effect of which will be felt directly or indirectly throughout the Soviet economy. Although imports of wheat will suffice to keep Soviet consumption of bread grain near its normal level, a shortage of fodder grain must inevitably damage the prospects for livestock farming.

14. There are already signs that, in order to avoid a repetition of this year's failure, the Soviet leadership has accepted the need for a thorough reappraisal of agricultural policy and is prepared to pay the price which such a reappraisal will entail, namely a redistribution of resources in favour of agriculture and those sectors of industry upon which it depends.

15. The wheat shipments from the West will greatly increase the Soviet import bill. The authorities will probably seek to maintain essential imports of machinery, equipment and certain industrial raw materials at their previously-planned levels. At the same time, the scope for reductions in non-essential imports is limited; neither will it be easy for the Soviets to increase their hard currency earnings by expanding their exports to the West. As a result, the strain on their balance of payments will prove severe. They have already been forced to sell large quantities of gold in London and Zurich and will undoubtedly have to sell still more in the coming months. To mitigate the pressure on their gold reserves, they may be expected to seek credit facilities wherever possible in their dealings with Western countries.

16. The situation in the European satellites is more difficult to assess. No certain information on grain production in these countries this year is yet available, nor is it known how much grain they will be able to import from the Soviet Union. Thus, no forecast can yet be made of their grain import requirements from the West, although these are likely to be appreciably greater than usual. Should this prove to be the case, their balance of payments difficulties would be aggravated, but it does not seem likely that the internal repercussions on their economics would be very serious.

17. Finally, the fact that the "Socialist Camp" has had to import such large quantities of wheat from the West will do little to enhance the prestige of Communism, particularly in the under-developed countries, where the efficiency of an economic system is likely to be judged, at least in part, by its success or failure in expanding food production.

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II. IMPORTANCE OF WHEAT PURCHASES BY COMMUNIST COUNTRIES FOR THE FREE WORLD COUNTRIES

(1) Canada

18. The 1963 wheat crop in Canada has been estimated at the record figure of about 19 million tons (1), while the available stocks, which had reached their peak in 1957 (almost 20 million tons) stood by mid-September at about 13.3 million tons. Annual domestic consumption absorbs some 3 to 4 million tons.

19. According to the OECD statistics, Canada exported in 1962 some 8 million tons of wheat and about 600,000 tons of flour. Western Europe accounted for about 4 million tons of this total, the rest of the free world for 2.4 million tons and the Communist countries for 2.2 million tons (Communist China 1.8 million, Poland 378,000 tons and Albania 47,000 tons).

20. From what is known so far during the 1963/64 trading year Canada will probably export to the Communist countries about 9 million tons of wheat and wheat flour, of which 6.5 million tons to the Soviet Union, about 1 million tons to the European satellites and possibly up to 1.4 million tons to Communist China, for a total value of between \$650 and 680 million, roughly equivalent to total Canadian receipts from wheat exports in 1962. This represents 10% of total Canadian exports during 1962 and about 1.5% of Canadian GNP and illustrates the fact that Canada is economically by far the most interested free world country in Sino-Soviet wheat deals.

21. In addition, the large Western European demand has been reinforced by the low quality of its domestic grains, which suffered more than the quantity from the wet summer at harvesting. In entering into the agreement with the USSR, the Canadian authorities have stressed that every care had been taken by the Canadian Wheat Board to ensure the country's ability to deliver the quantities committed, as well as to honour supply obligations to its major markets in the United Kingdom, Western Europe, Japan, Asia and elsewhere under the International Wheat Agreement. But the repercussions of the large-scale wheat deals with the USSR on the price of wheat and the increased demand of Western Europe will benefit the Canadian overall situation.

22. For a number of years, Canada has relied on a heavy inflow of capital from the United States to cover its chronic deficit on the balance of international payments. The recent measures taken by the United States administration had tended to reduce this inflow. Under the wheat agreement with the USSR, down-payment of 25% on delivery with the balance payable in equal instalments over 6, 12 and 18 months had been provided. The USSR appears, however, to be reluctant to make use of the credit terms extended by the Canadian Government. As a result it is estimated that if deliveries continue on schedule, Soviet payments may well provide some \$170 million to the Canadian balance of payments before the end of the year.

(1) According to the Minister of Trade and Commerce on 16th September 1963, but these forecasts were made before widespread draught afflicted the Ontario harvest.

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(2) Australia

23. The wheat harvest in Australia during the crop season December 1962/November 1963 has been estimated at about 7.5 million tons. In addition, at the end of 1962, the wheat stock amounted to 0.3 million tons. Domestic consumption, which absorbed 2.1 million tons in 1961, may be estimated between 2 and 2.5 million tons in 1962. In 1962, the total value of Australian wheat exports amounted to \$283 million, of which some 30% or \$86.6 million came from the sales to Communist China of 1,440,000 tons of wheat.

24. The USSR has placed orders of 1.6 million tons of wheat for delivery during 1963/64, at an approximate value of \$100 million. If sales to Communist China amount to another \$75 million during the same period, it would mean that Australian sales of wheat to the Communist countries would represent about 7% of total Australian exports (all commodities) and not far from half the total wheat surplus available for export.

(3) Argentina

25. The wheat crop for the season December 1962-November 1963 has been estimated at 4.5 million tons. In addition, the carry-over of the previous year's surplus amounted to 0.5 million tons. Domestic consumption absorbed during 1962 3.7 million tons. Argentina's total wheat exports during 1962 represented some 14% of total exports while maize exports accounted for another 10%. Depending on the size of the crops Argentina sometimes exports more maize than wheat. During 1961, Argentina delivered 45,000 tons of wheat to Communist China and probably a similar amount in 1962. Last year, the estimated amount of receipts from sales to Communist China amounted to \$2.9 million out of a total of \$173.2 million earned by Argentina in foreign currency from wheat sales.

26. It has been reported that the USSR is negotiating the purchase of 500,000 tons of wheat. The value of this deal has not been revealed and the qualities involved are not known but on the basis of the prevailing prices it would seem that the value of this deal might be of the order of \$30 to \$35 million. If this were the case, it would represent some 17 to 20% of total receipts from wheat sales by Argentina in 1962, but not more than 3% of total Argentinian exports and a negligible fraction of less than $\frac{1}{3}$ of 1% of her GNP.

(4) United States

27. The actual size of the 1963 wheat harvest in the United States has been estimated at about 30.33 million tons or 1.1 million tons more than last year's crop. A new record of about 100 million tons of maize is forecast, representing an increase of 9.1 million tons over last year's crop. The stored surpluses reached their peak at the end of 1961, when 38.4 million tons of wheat and 51 million tons of maize were reportedly carried over. Domestic consumption in 1962-63 (16.3 million tons of wheat and 91 million tons of maize) however, accounts practically for the entire maize and for over half of the wheat crop.

28. According to OECD statistics, during the calendar year 1962, the United States exported 16 million tons of wheat and wheat flour and 11 million tons of maize (in addition to 2 million tons of barley and 1 million tons of rice). Total value of all grain exports (\$1.97 billion) approximated 9% of total United States exports (\$21.4 billion), 70% of maize exports and 18% of wheat exports went to OECD Europe and almost all the rest to other free world countries (mainly to India, Egypt, Brazil and Japan). Grain exports to Communist countries did not exceed \$35 million and went exclusively to Poland, who imported under PL 480 433,000 tons of wheat and wheat flour, 20,000 tons of rice and 41,000 tons of maize.

29. At the time of writing, the final outcome of the negotiations with the USSR and with some European satellite countries (Hungary, Bulgaria and Czechoslovakia) is not known. It had, however, been announced that the volume involved would probably be 4 million tons of wheat and possibly maize, to be sold to the USSR for a total value of approximately \$250 million, and that Hungary, Bulgaria and Czechoslovakia were trying to obtain 1 million tons of grain, representing about \$60 million. Although the importance of these negotiations for the United States economy is in no way comparable to that which it represents for any of the previously-considered countries, they have drawn most of the attention.

30. Apart from their political and psychological significance the marginal effects upon the United States balance of payments have been stressed by President Kennedy. The importance at the present stage of an additional income of \$300 million, mainly in gold, strengthening the position of the dollar, has been underlined, as well as the fact that by mid-1964 United States wheat stocks are now expected to be reduced to between 19 and 20 million tons. Farm prices in the United States will be strengthened, and the additional income that the deal would provide to farmers, transport and port workers and grain traders was also mentioned by President Kennedy in the justification of this decision to permit these exports(1).

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- (1) President Kennedy's letter of 10th October, 1963, to the President of the Senate and to the Speaker of the House of Representatives.

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31. If the Soviet Union decides to accept the proposed deal, the United States grain would be for delivery and use in the Soviet Union and the Eastern European countries only. It will be carried by American ships, supplemented by vessels of other countries as required, and the wheat will be sold at the world price under normal commercial conditions. It has been stressed that, if the deal were concluded, this new development was in no way to be considered as a departure from the earlier United States policy concerning trade in non-strategic goods with the Eastern bloc.

32. The condition concerning the transport by United States ships gave rise to negotiation difficulties. At the time when the discussions were going on, the United States freight rates for shipping from the North American Atlantic coast to Russian ports were quoted to be generally at about \$26 per ton, while the comparable world rates, although more than double those of a year ago, were said to be \$12.5 to \$13 per ton. The European maritime countries have reportedly protested against the United States transport reservation clause. According to most recent information, it would seem, in view of the urgency of the deliveries, that only 25% of total tonnage could be shipped by United States carriers and that the American freight rates might be lowered to reduce this difference with world rates to about \$5 per ton.

(5) Western European exporting countries

33. France appears to be the main Western European exporting country maintaining grain deliveries to the Communist countries in recent years. In 1962, out of a total of 1,891,000 tons of wheat exports, France exported to China 361,000 tons, to Poland 162,000 tons, to Albania 56,000 tons and to Hungary 51,000 tons, representing a total value of about \$38 million. In addition, France exported barley to Communist China (134,000 tons) and to Bulgaria (30,000 tons) for a total value of \$7.5 million.

34. The 1962 wheat crop harvested in France had, however, been a record one, owing to very favourable yields, and an increase in area. The 1962 wheat harvest amounted to 13.77 million tons, leaving about 3 million tons available for export. It would seem, however, that production of wheat in 1963 will present a decline of as much as 4.8 million tons, reducing the total wheat crop to 8.98 million tons, which would not leave surpluses to be exported over and above the traditional French wheat exports to the other European countries (mainly West Germany). There are even doubts as to whether France will be able to export during this year the fraction of the 1 million tons of wheat it agreed in 1962 to sell to Communist China over the three years 1962 to 1964. As regards the USSR, the only agreement so far announced provides for the delivery of 80 thousand tons of flour.

35. During 1962, the Federal Republic of Germany reportedly exported about 187,000 tons of wheat flour to Communist China, worth over \$12.2 million and about 83,000 tons of flour to Hungary and Bulgaria for a total value of approximately \$5 million. The 1963 wheat harvest in the Federal Republic is expected to exceed by some 200,000 tons the 1962 crop, thus reaching 4.79 million tons, which will leave the Federal Republic a net importer of wheat. The USSR is said to be negotiating with the Federal Republic for the delivery of 250 to 300,000 tons of flour to be exported to the Soviet Union during this year. An estimate of anticipated exports to Communist China is not available but it will almost certainly be less than last year.

(6) Western European importing countries

36. Wheat prices which already stood above the minimum fixed in the International Wheat Agreement have risen by 15% since September, largely as a result of the expected large-scale Soviet purchases. According to the International Wheat Agreement, the exporting countries have undertaken to supply all the commercial requirements of importing countries, so long as prices are within the range fixed by the Agreement. This obligation does not seem to apply to exporting countries wanting to import, as is the case of the USSR, who is party to the Agreement. Canadian and United States authorities have declared that they disposed of ample supplies to fulfil their commitments towards the importing countries, even after sales to the Soviet bloc.

(7) Impact on freight rates

37. Even if grain imports by Communist China, amounting to about 4.5 million tons annually, are not taken into account for evaluating the repercussions of Soviet wheat purchases on world transport, the size of the intended deliveries to the Soviet Union (13 million tons, of which 4 million to be bought in the United States), represents some 20% of all sea-born grains transported over the world (over 60 million tons during the trade season 1961/62), 40% of grain shipped to Western Europe and 30% more than total grain imports to the United Kingdom, traditionally by far the largest grain importer of Western Europe. The massive and urgent requirements for grain by Communist countries have already suggested that suitable tramp transport might be in short supply, since they come in addition to large grain imports anticipated by Western European countries, Japan and India from North and South America and from Australia.

38. Since early 1957, freight markets went through a prolonged depression but after the announcement of the first Soviet wheat deals, freight rates for tramp vessels, dry cargo and tankers have risen sharply to the highest point reached over the last six years, and well over twice the rate reached at the same period last year. The unemployed tonnage laid-up has consequently been reduced to a minimum, leaving only 2% (consisting almost entirely of ships at least 20 years old) of the world dry cargo fleet unutilised.

39. The demand for grain transport is expected to last well beyond next Spring and dry cargo as well as oil tanker tramps can hope for profitable operation over the next six months. The increase in freight charges will not be confined to grain, but will affect most other categories of cargo.

III. IMPORTANCE AND POSSIBLE CONSEQUENCES OF THE GRAIN PURCHASES FOR THE SOVIET COUNTRIES

A. PRODUCTION AND UTILISATION OF GRAIN IN THE SOVIET UNION

Production (1)

40. The Soviet Union is traditionally one of the world's major growers and exporters of grain. Grain production during the last years of tsarist rule averaged about 80 million tons annually. Throughout the next three decades, as a result of civil war, forced collectivisation and the Second World War, production fluctuated wildly but during the last five years of Stalin's life, still averaged only 81 million tons a year. Meanwhile, the population had risen from 160 million in 1913 to nearly 190 million in 1953.

41. Largely as a consequence of Khrushchev's Virgin Lands campaign of 1954-58, during which some 40 million hectares of marginal land in Siberia and Kazakhstan were ploughed up and sown to grain, production rose rapidly from 82.5 million tons in 1953, to 141.2 million tons in 1958. Under the current Seven-Year Plan (1959-65), it is proposed to raise production to 164-180 million tons by 1965, but progress since 1958 has been unimpressive, although a new record harvest of 148.2 million tons was claimed for 1962. Exceptionally unfavourable weather conditions throughout the whole country appear to have caused a sharp fall in the 1963 crop. Although no official figures have yet been issued, it is thought that claimed production for this year may be between 115 and 125 million tons.

42. The composition of the grain harvest has also changed significantly over the years. Output of bread grains rose from 49 million tons (57% of total grain production) in 1913, to 56 million

(1) Throughout this paper, unless explicitly stated otherwise, official statistics are used. These are not always reliable. Thus Soviet figures for gross grain production are generally thought to exaggerate the real harvest by 10 to 15%. Were this not the case, it would be difficult to see why the Soviets should be experiencing such difficulties at the present time. The record harvest of 1962 (148.2 million tons) should have provided them with ample stocks. However, since it is in the interest of local officials to report the highest possible production, figures are based on bunker weight and are known to contain insufficient allowance for moisture and other extraneous matter. Figures for state purchases may also be exaggerated, though perhaps to a lesser degree. Figures for exports and imports are believed to be reliable. Similar considerations may be assumed to apply to production, exports and imports in the European satellites.

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tons (68% of total production) in 1953, whilst output of fodder grains fell from 37 million tons (43% of total production) to 26 million tons (32% of total production) over the same period. Since then output of fodder grain has more than doubled, reaching 60 million tons (40% of total production) in 1962, but output of bread grains, after rising rapidly to 92 million tons (65% of total production) in 1958, declined to 87 million tons (59% of total production) in 1962, probably as a result of Khrushchev's pre-occupation with livestock farming and the need to boost fodder output. Production of bread grains in 1963 may be as little as 70 to 75 million tons.

TABLE I
Production of Grain in the Soviet Union 1913-62
(million tons)

| | 1913 | 1953 | 1958 | 1959 | 1960 | 1961 | 1962 |
|---------------|------|------|-------|-------|-------|-------|-------|
| Bread Grains* | 49.3 | 56.0 | 92.5 | 86.2 | 80.9 | 83.4 | 88.0 |
| Fodder Grains | 36.7 | 26.5 | 48.7 | 39.7 | 53.5 | 54.6 | 60.2 |
| TOTAL | 86.0 | 82.5 | 141.2 | 125.9 | 134.4 | 138.0 | 148.2 |

* (including rice)

Utilisation of Supplies

(a) Domestic Consumption

43. No statistics are available for consumption of bread grains in the Soviet Union but certain conclusions can be drawn from the published figures relating to state purchases. From these it appears that since 1958 the producing farms have retained for their own use (i.e. for seed, feed, payments in kind to members, etc.) a roughly constant amount of about 85 million tons a year, of which around 45 million tons a year have been bread grains. During this period, the rural population has declined by about half a million, from 108.8 million in January 1959, to 108.2 million in January 1963. Per capita consumption of bread grains in rural areas would thus seem to have remained more or less unchanged.

44. State purchases of grain, which cover supplies to urban areas and certain deficit rural areas, additions (if any) to stocks, and exports have fluctuated considerably from year to year. Purchases of bread grains, after rising to 47.6 million tons in 1958, have fallen off and have never since then exceeded 42 million tons. This year they seem unlikely to be more than 35 million tons.

(see Table II at Annex)

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45. However, during these years the urban population has risen rapidly from 100 million in January 1959, to about 115 million in January 1963. Presumably, therefore, consumption of bread grains in the towns can only have been maintained by running down stocks. These were probably high after the good 1958 crop, but must have fallen dangerously low since then.

46. During the past 12 months, two additional factors may have combined to increase demand for bread grains still further. In the first place, following the disastrous potato harvest of 1962, there has been a serious shortage of potatoes, and this has been felt most acutely in the towns where potatoes have had to be replaced to some extent in the citizens' diet by bread. Secondly, the rise in the price of meat decreed in June 1962, has made it profitable for private owners of livestock to fatten their animals on bread, the price of which remains relatively low and which is often more readily obtainable than more orthodox varieties of fodder. To judge by the numerous indignant articles which it has provoked in the Soviet press, this practice is becoming surprisingly widespread, mainly, though not exclusively, in rural areas.

47. Thus, the overall picture that emerges is that whilst in rural areas both supply of and demand for bread grains have remained more or less constant since 1958, in urban areas a decline in supplies has been accompanied by a steady rise in demand, which has probably accelerated during the past year. As a result stocks must have been depleted.

(b) Exports and Imports

48. In tsarist times, Russia used to export some 8 to 10 million tons of grain (mainly wheat) a year. Under the Soviet régime, grain exports fell sharply and during the last years of Stalin's life averaged about 1 million tons a year. During the 1950's, as domestic production increased, exports rose and reached 6.1 million tons (net) in 1959. Since then the growth of exports has been much less rapid, although they reached 7.4 million tons (net) in 1962, some decline in bread grain exports being more than outweighed by a rise in exports of fodder grains, although the former's weight in the total has remained predominant. The Soviet Union also exports small quantities of flour and meal.

49. During 1959-62, some two-thirds of total Soviet grain exports went to the European satellites, the main buyers being the Soviet Occupied Zone of Germany, Czechoslovakia and Poland. About 5% went to other Communist countries (i.e. Cuba, China and North Korea). Western European countries accounted for about a quarter and the developing countries of Asia, Africa and Latin America for about 5%, although among these, only Brazil has regularly purchased significant quantities of Soviet grain.

(See Table III at Annex)

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50. The fact that the Soviets have seen fit to maintain their exports at this level can probably be explained by their predilection for long-term trade agreements, by which they have committed themselves in advance to supply given quantities of grain. When domestic supplies have proved insufficient to meet these commitments, the deficit has had to be covered by imports, although in the past these have generally been small. The only form of grain to be imported regularly by the Soviet Union on a significant scale is rice, imports of which, mainly from Communist China, averaged nearly 400,000 tons annually during 1959-62.

51. As a result of this year's bad harvest, the Soviet Union has been obliged to order large quantities of grain in Western markets. Orders have already been placed in Canada and Australia for over 8 million tons of wheat for delivery in 1963/64 and it seems likely that about 4 million tons of grain (mainly wheat, but possibly including some maize) will be imported from the United States. Negotiations are in progress for the delivery of half a million tons of wheat from the Argentine and for a quarter of a million tons of wheat flour from the Federal Republic of Germany, whilst a small quantity of wheat flour has already been ordered from France. In addition, 400,000 tons of wheat are to be imported from Roumania, apparently in repayment of a loan extended to that country some years ago. Thus, total Soviet imports of grain in 1963/64 will probably exceed 13 million tons, and it seems likely that their total cost in hard currency, exclusive of transport charges will amount to some \$ 900 million.

(See Table IV at Annex)

52. Whilst the greater part of these imports will no doubt be used to maintain domestic consumption and replenish stocks, it seems probable that a substantial proportion (perhaps about a quarter) will be re-exported to the European satellites and Cuba (according to some reports as much as 450 thousand tons of the Canadian order will be shipped directly to Havana) and to certain other nations such as Brazil, to whom the Soviet Union has commitments. However, the Soviets are reported to have requested the cancellation of sales of about 100,000 tons of wheat to Britain, Holland and Finland. It is likely to be a condition of sale that no part of the United States order be re-exported.

Likely Repercussions of the 1963 Harvest Failure

(a) Repercussions on Internal Economic Policy.

53. This year's agriculture failure must inevitably be immensely damaging to the prestige of the Soviet rulers and, in particular, to that of Khrushchev, who has made agriculture his special responsibility during the past ten years and whose lavish promises to raise food consumption - promises which have received wide publicity both at home and abroad - provide a rather embarrassing contrast to the reality of his achievements.

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Khrushchev himself has admitted to the Soviet public that it will be necessary to import wheat from the West and has mentioned the quantities involved.

54. The fact that the Soviet rulers have chosen to import wheat on a large scale shows clearly that, in contrast to the situation during Stalin's time, they are unwilling, and perhaps unable, to enforce a drastic cut in food consumption. Nevertheless, these imports will not insulate the consumer entirely from the ill effects of this year's poor crop, since a reduced supply of fodder grains is likely to put a further brake on the development of livestock farming and, consequently, of meat production (1).

55. The Soviet rulers cannot afford a repetition of this year's agricultural disaster. Although on this occasion full allowance should be made for the part played by the weather, it must be remembered that since 1958 the rate of increase of agricultural production has consistently failed to match that of the population. The underlying causes of agricultural stagnation are to be found in inadequate investment and the absence of effective incentives for the peasants. A radical solution to the problem will thus require a large-scale re-direction of resources towards agriculture and consumer goods output. Investment in the production of agricultural machinery and -even more important- of mineral fertilisers (consumption of which per hectare of arable land is less than one third of that in the United States) will have to be increased substantially. But if such investment is to yield any significant return, if waste of scarce supplies and neglect of costly equipment are to be avoided, the attitude of the peasants towards their work will have to be completely transformed. This will entail a significant increase in peasant incomes, which in turn will necessitate a proportional rise in the output of consumer goods in order to absorb the additional purchasing power thus created.

56. Such measures would amount to a complete reversal of traditional Soviet economic priorities and it is doubtful whether the present leadership could bring themselves to swallow such strong medicine. Nevertheless, some redistribution of resources towards agriculture seems inevitable. There are, in fact, already signs that such a redistribution is being prepared -for instance, the decision, recently announced by Khrushchev, to withdraw from the moon race, which appears to have been dictated by the need to shift resources from the space programme to other sectors. Within the agricultural sector, Khrushchev seems to have realised, somewhat belatedly, that no further significant returns can be
/expected from

(1) It is unlikely that meat supplies will actually diminish. In fact, the immediate result will probably be an increase in meat production during the winter of 1963/64, since a larger than average number of animals will have to be slaughtered. This in turn, however, will reduce the future rate of growth.

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continued expansion of the sown area, and therefore to envisage a switch to more intensive methods of cultivation. He has publicly stated that any future increase in production will have to come from higher yields per hectare and with this end in view production of mineral fertiliser is to be rapidly increased during the next two years. Although grain yields rose by 45% between 1953 and 1958, they fell by 3% over the next four years and still remain well below United States and Canadian levels.

TABLE V

COMPARATIVE SOVIET, UNITED STATES AND CANADIAN GRAIN YIELDS
(quintals per hectare)

| | USSR (average 1958-62) | United States (average 1958-60) | Canada (average 1958-60) |
|-------|---------------------------|------------------------------------|-----------------------------|
| Wheat | 10.8 | 16.6 | 12.8 |
| Rye | 9.7 | 11.4 | 10.4 |
| Maize | 17.1 | 32.7 | 37.7 |

57. Exploitation of the Virgin lands will no doubt continue, although perhaps on a reduced scale. In certain areas of Kazakhstan and Western Siberia, soil and wind erosion have already sapped from the land most of what little fertility it ever possessed. It may be that some of the most exhausted areas will not be left fallow until production of fertiliser can be expanded sufficiently to justify their continued exploitation.

(b) Repercussions on External Economic Relations

58. There is no reason to suppose that the decision to import grain this year represents any permanent shift in Soviet foreign trade policy, or that the future prospects for exports of foodstuffs to the Soviet Union have been significantly enhanced. The Soviet leadership has always brought to maintain self-sufficiency in food production. This year's grain imports are clearly regarded as an emergency measure. In similar circumstances they might be repeated, but it is likely that the Soviet authorities will now redouble their efforts to ensure that such circumstances do not, in fact, recur.

59. The harvest failure, will, however, have serious repercussions on Soviet foreign trade. Grain imports from the West in 1963-64 are likely to cost the Soviets some \$900 million in hard currency, and in addition they may be obliged to pay up to \$100 million in transport charges to Western ship owners. Furthermore, they will be deprived of most, if not all, of the \$100 million of hard currency, which they have been earning each year through grain exports to Western Europe. Their net loss of hard currency earnings will probably, therefore, be about \$1,100 million, equivalent to 17% of total Soviet imports in 1962, 57% of their imports from all non-Communist countries and 84% of their imports from the OECD countries.

60. Although the Soviets have obtained limited credit facilities from the Canadian authorities, it appears that the greater part of their total purchases will be made for cash(1). As a result, their capacity to import machinery and equipment from the West may be seriously impaired. In 1962, Soviet imports of machinery and equipment from the OECD countries totalled \$606 million or 46% of total Soviet imports from these countries. A reduction of machinery imports could have serious consequences for the development of certain branches of Soviet industry. Unfortunately for the Soviets, one of the branches that might be most seriously affected is the chemical industry, considered by the leadership as a priority sector, partly, of course, because of its importance (as a producer of fertilisers and pesticides) to agriculture. Earlier this year, the Seven-Year Plan (1959-65) was completely recast in order to accelerate the growth of the chemical industry, but the latter's development remains dependent to a considerable extent on supplies of certain types of advanced equipment from the West.

61. In order to avoid a reduction of machinery imports, the Soviets are likely to:

- (i) seek generous credit terms in transactions with Western countries;
- (ii) curtail, as far as possible, their imports of low priority goods. This may entail some reduction in their trade with the developing countries;
- (iii) endeavour to increase their exports to the West, particularly of those commodities such as oil, of which they have a surplus, or production of which could be easily expanded;
- (iv) increase their gold sales in Western markets. In fact, they have already begun to do this (2).

(1) See Page 7, Table IV.

(2) See SOVIET GOLD SALES, PRODUCTION AND RESERVES - AC/127-D/137

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B. PRODUCTION AND UTILISATION OF GRAIN IN THE EUROPEAN SATELLITES AND THE SOVIET OCCUPIED ZONE OF GERMANY

Production

62. Production of grain in this area before the Second World War averaged about 43 million tons annually, with bread grains accounting for slightly more than half the total. In the early post-war years, output, particularly of fodder grains, fell sharply but by the late 1950's had regained its pre-war level. During 1960-62, the harvest averaged about 45 million tons annually but preliminary reports indicate that in 1963 it will be well below average.

TABLE VI

PRODUCTION OF GRAIN IN THE EUROPEAN SATELLITES

(million tons)

| | 1934/8 | 1948/52 | 1955/59 | 1960 | 1961 | 1962 |
|---------------|--------|---------|---------|------|------|---------------|
| Bread Grains | 23.2 | 22.0 | 23.6 | 24.2 | 24.8 | - |
| Fodder Grains | 19.5 | 14.8 | 20.1 | 23.0 | 20.7 | - |
| Total | 42.7 | 36.8 | 43.7 | 47.2 | 45.5 | approx. 45 |

Utilisation

63. Before the war, these territories used to export about 4 million tons (net) of grain annually. Since the war, however, imports have consistently exceeded exports and during the years 1959-1962, net imports averaged 5.4 million tons a year.

64. The transformation of this region from a substantial net exporter of grain into a large net importer is somewhat surprising in view of the fact that the population has increased by only about 4 million (i.e. by approximately 4%) since 1937. Although it is probable that official statistics exaggerate the real size of the grain harvest, at least in some of the satellites, and that losses through waste are greater than in pre-war years, it is clear that per capita consumption in these territories is now considerably higher than in the pre-war period.

(See Table VII at Annex)

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Main Sources of Imports

65. The European satellites' principal source of grain imports is the Soviet Union. Until 1960, virtually all grain imports from the Soviet Union consisted of bread grains, but since then imports of Soviet fodder grains have grown rapidly and reached 1.2 million tons in 1962. Satellite grain imports from the West, of which Polish imports of wheat from the United States and Canada are by far the largest component, averaged 1.5 million tons (0.8 million tons net) annually during 1959-62. Imports of rice, mainly from Communist China, averaged about 320,000 tons (240,000 tons net) a year during 1957-60. No figures for more recent years are available.

66. Given the likelihood of a poor harvest in most of the satellite countries this year, and allowing for the possibility that the Soviet Union, despite its own large imports, may have difficulty in maintaining exports to the satellites at their previous level, the latter will probably have to buy appreciably more grain in the West in 1963-64 than they have usually done in the past. Hungary, Czechoslovakia and Bulgaria are reported to be contemplating large purchases of grain in the United States. Nevertheless, contracts actually signed by the satellites for grain deliveries from Western suppliers in 1963-64 do not so far appear to be unusually large. (See Table VIII at Annex)

Consequences for the Satellite Economies

67. It seems unlikely that the fall in grain production in the European satellites will prove comparable with that experienced by the Soviet Union. The consequences for the former will, therefore, be much less serious than for the latter. A large part of their deficit will probably be covered as usual by imports from the Soviet Union. Although in recent years the satellites have regularly shown a deficit in their balance of trade with the non-communist world, and in particular with the industrialised Western countries, and although abnormally heavy grain purchases in the West would tend to swell their import bill still further, it seems reasonable to suppose that such purchases could, if necessary, be offset by a reduction in other, lower priority, categories of imports, without any very serious repercussions on the satellite economies.

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Paris, XVIc.

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ANNEX

TABLE II
Grain Tonnage Retained by Farms and Purchased by State 1953-62

(Million Tons)

| | 1953 | | 1958 | | 1959 | | 1960 | | 1961 | | 1962 | | 1963 | |
|---------------|-------------------|-----------------|-------------------|-----------------|-------------------|-----------------|-------------------|-----------------|-------------------|-----------------|-------------------|-----------------|-------------------|-----------------|
| | Retained by Farms | State Purchases |
| Bread Grains | 30.8 | 25.2 | 44.9 | 47.6 | 45.6 | 40.6 | 44.4 | 36.5 | 42.8 | 40.6 | approx. 46 | approx. 42 | - | - |
| Fodder Grains | 20.6 | 5.9 | 39.7 | 9.0 | 33.7 | 6.0 | 43.3 | 10.2 | 43.1 | 11.5 | approx. 46 | approx. 15 | - | - |
| TOTAL | 51.4 | 31.1 | 84.6 | 56.6 | 79.3 | 46.6 | 87.7 | 46.7 | 85.9 | 52.1 | 91.6 | 56.6 | - | approx. 47 |

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SOVIET EXPORTS AND IMPORTS OF GRAIN 1959/62

(thousand tons)

| | 1959 | | | | 1960 | | | | 1961 | | | | 1962 | | | |
|---|--------------|-------|-------------|---------|--------------|---------|-------------|---------|--------------|---------|-------------|---------|--------------|---------|-------------|-------|
| | Fodder grain | | Rice | | Fodder grain | | Rice | | Fodder grain | | Rice | | Fodder grain | | Rice | |
| | Bread grain | Total | Bread grain | Total | Bread grain | Total | Bread grain | Total | Bread grain | Total | Bread grain | Total | Bread grain | Total | Bread grain | Total |
| I. EXPORTS | | | | | | | | | | | | | | | | |
| (a) to COMECON countries | 4,696.5 | 128.5 | 4,825.0 | 4,676.2 | 208.1 | 4,884.3 | 3,448.5 | 592.6 | 4,041.1 | 1,260.5 | 3,640.5 | 742.2 | 4,783.3 | 1,403.4 | 4,901.0 | |
| (b) to other Communist countries | 40.2 | - | 40.2 | 59.7 | - | 59.7 | 683.1 | 59.1 | - | 142.9 | 670.3 | - | - | - | 813.2 | |
| to total Communist world | 4,736.7 | 128.5 | 4,865.2 | 4,735.9 | 208.1 | 4,944.0 | 4,131.6 | 651.7 | 4,081.1 | 1,546.4 | 4,310.8 | 742.2 | 4,783.3 | 1,403.4 | 5,714.2 | |
| (c) to Western Europe and Japan | 1,442.3 | 228.3 | 1,670.6 | 1,173.3 | 278.7 | 1,452.0 | 1,437.7 | 937.5 | 2,375.2 | 345.4 | 1,144.4 | 322.1 | 2,375.2 | 345.4 | 1,489.8 | |
| (d) to developing countries | 392.6 | - | 392.6 | 337.2 | - | 337.2 | 319.3 | 2.8 | - | - | 498.0 | - | - | - | 498.0 | |
| to total non-Communist world | 1,834.9 | 228.3 | 2,063.2 | 1,510.5 | 278.7 | 1,789.2 | 1,757.0 | 940.3 | 2,697.3 | 345.4 | 1,642.4 | 322.1 | 2,697.3 | 345.4 | 1,987.8 | |
| (e) unaccounted for | 29.3 | 51.1 | 80.4 | 60.5 | 0.9 | 61.4 | - | 0.3 | 0.3 | - | 112.3 | - | 0.3 | - | 112.3 | |
| TOTAL EXPORTS | 6,600.9 | 407.9 | 7,008.8 | 6,306.9 | 487.7 | 6,794.6 | 5,888.6 | 1,592.3 | 7,480.9 | 1,748.8 | 6,065.5 | 1,064.3 | 7,480.9 | 1,748.8 | 7,814.3 | |
| II. IMPORTS | | | | | | | | | | | | | | | | |
| (a) from COMECON countries | - | 9.5 | 9.5 | 50.4 | 104.5 | 154.9 | 167.2 | 3.8 | 171.0 | - | 45.1 | - | 171.0 | - | 45.1 | |
| (b) from other Communist countries | 48.0 | - | 706.4 | 47.6 | - | 498.5 | - | - | 19.9 | - | - | - | 19.9 | - | 150.2 | |
| from total Communist world | 48.0 | 658.4 | 715.9 | 98.0 | 104.5 | 653.4 | 167.2 | 3.8 | 190.9 | - | 45.1 | - | 190.9 | - | 195.3 | |
| (c) from Western Europe and North America | 198.9 | - | 198.9 | - | 14.2 | 14.2 | 485.6 | 18.8 | 504.4 | - | - | - | 504.4 | - | - | |
| (d) from developing countries | - | 30.7 | 30.7 | - | 21.0 | 71.2 | - | - | - | - | - | - | - | - | 145.1 | |
| from total non-Communist world | 198.9 | 689.1 | 945.6 | 98.0 | 142.4 | 741.5 | 485.6 | 18.8 | 698.6 | - | - | - | 698.6 | - | - | |
| (e) unaccounted for | - | 0.1 | 0.1 | - | 2.7 | 2.7 | 3.1 | 0.2 | 3.3 | 1.1 | 42.2 | 1.1 | 42.2 | 1.1 | 43.3 | |
| TOTAL IMPORTS | 246.9 | 9.6 | 256.5 | 146.0 | 142.4 | 741.5 | 485.6 | 18.8 | 701.9 | 1.1 | 42.2 | 1.1 | 701.9 | 1.1 | 383.7 | |
| NET EXPORTS | 6,354.0 | 398.3 | 6,063.2 | 6,208.9 | 345.3 | 6,053.1 | 5,232.7 | 1,569.5 | 6,782.3 | 1,747.7 | 6,020.4 | 1,064.3 | 6,782.3 | 1,747.7 | 7,430.6 | |

TABLE IV

Likely Soviet Grain Imports 1963/64

| Exporting Country | State of negotiations | Type of grain | Quantity (000 tons) | F.o.b. value (in million US \$) | Terms |
|-----------------------------|--------------------------|-----------------------|---------------------|---------------------------------|---|
| Canada | Contract concluded | Wheat and wheat flour | 6,477 | 500 | 25% cash at date of shipment Remaining 75% after 6,12 and 18 months. \$200 million ceiling on credit outstanding at any one time |
| Australia | Contract concluded | Wheat | 1,592* | Approximately 100 | Unknown (thought to be cash). |
| United States | Negotiations in progress | Wheat (and maize?) | 4,082 | Approximately 250 | |
| Argentina | Negotiations in progress | Wheat | 500 | | Probably cash |
| Federal Republic of Germany | Negotiations in progress | Wheat flour | 333 | Approximately 70 | |
| France | Contract concluded | Wheat flour | 107 | | Unknown |
| Roumania | Contract concluded | Wheat | 400 | - | Repayment of previous loan |
| | | | 13,491 | Approximately 920 | |

* Plus an option on a further 150,000 tons.

TABLE VII

Satellite Exports and Imports of Grain (excluding rice)
(thousand tons)

| | 1959 | | | 1960 | | | 1961 | | | 1962 | | |
|---|---|---------------|---------|--------------|---------------|---------|--------------|---------------|---------|--------------|---------------|---------|
| | Bread Grains | Fodder Grains | Total | Bread Grains | Fodder Grains | Total | Bread Grains | Fodder Grains | Total | Bread Grains | Fodder Grains | Total |
| I. EXPORTS | | | | | | | | | | | | |
| (a) to USSR | - | - | - | - | 100.5 | 100.5 | 162.0 | 3.8 | 165.8 | 5.0 | - | 5.0 |
| (b) to Western Europe | 117.8 | 129.9 | 247.7 | 169.6 | 399.0 | 568.6 | 159.5 | 832.6 | 992.1 | 136.8 | 801.5 | 938.3 |
| TOTAL EXPORTS | 117.8 | 129.9 | 247.7 | 169.6 | 499.5 | 669.1 | 321.5 | 836.4 | 1,157.9 | 141.8 | 801.5 | 943.3 |
| II. IMPORTS | | | | | | | | | | | | |
| (a) from USSR | 4,696.5 | 128.5 | 4,825.0 | 4,676.2 | 208.1 | 4,884.3 | 3,448.5 | 592.6 | 4,041.1 | 3,640.5 | 1,260.5 | 4,901.0 |
| (b) from Western Europe and North America | 485.6 | 540.2 | 1,025.8 | 1,358.4 | 486.5 | 1,844.9 | 1,370.7 | 203.2 | 1,573.9 | 1,332.4 | 288.2 | 1,620.6 |
| (c) others | unknown but thought to be insignificant | | | | | | | | | | | |
| TOTAL IMPORTS | 5,182.1 | 668.7 | 5,850.8 | 6,034.6 | 694.6 | 6,729.2 | 4,819.2 | 795.8 | 5,615.0 | 4,972.9 | 1,548.7 | 6,521.6 |
| NET IMPORTS | 5,064.3 | 538.8 | 5,603.1 | 5,865.0 | 195.1 | 6,060.1 | 4,497.7 | -40.6 | 4,457.1 | 4,831.1 | 747.2 | 5,578.3 |

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ANNEXTABLE VIIISatellite Grain Imports from the West 1963/64

| Importing Country | Exporting Country | State of negotiations | Type of Grain | Quantity (000 tons) | Value (million US \$) | Conditions |
|-------------------|-------------------|-----------------------|---------------|---------------------|-----------------------|--|
| Bulgaria | Canada | Contract Concluded | Wheat | 100-150 | approx. 7.5-11.2 | 10% cash at date of Shipment. Remaining 90% after 24, 30 and 36 months. |
| Hungary | United States | Contract Concluded | Maize | 65 | 4.4 | Unknown |
| | " | " | Wheat | 100 | approx. 7.5 | " |
| Czechoslovakia | Canada | Contract Concluded | Wheat | 176 | approx. 14.5 | Unknown. For immediate delivery. |
| | " | " | " | 120 | approx. 10 | For delivery in Summer 1964, presumably at then prevailing market price. 10% cash at date of Shipment. Remaining 90% after 24, 30 and 36 months. |
| Poland | Canada | Contract Concluded | Wheat | 400 | 29.3 | 10% cash at date of Shipment. Remaining 90% after 24, 30 and 36 months. |
| TOTAL | | | | 961-1011 | approx. 73.2-76.9 | |

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