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ECONOMIC DEVELOPMENT OF EASTERN EUROPEAN COUNTRIES
AND THE SOVIET-OCCUPIED ZONE OF GERMANY, AND
PROSPECTS FOR NATO COUNTRIES' TRADE WITH THEM

Report by the Committee of Economic Advisers

In the light of recent developments in the Communist countries of Eastern Europe(1), it has been thought desirable to improve the pooling within NATO of information on the current economic situation of these countries for the purpose of arriving at an agreed assessment of their future economic development and trade prospects. The Sub-Committee on Soviet Economic Policy was instructed to examine the economy of each of these countries on the basis of reports prepared by NATO countries having a special interest in a particular Eastern European country.

2. A consolidated report reviewing the results of these country studies(2) was discussed in the Council in Permanent Session on 24th November, 1965, where it was agreed that the attached summary including the conclusions of this report should be brought to the attention of Ministers at the meeting in December 1965.

(Signed) F.D. GREGH
Chairman

OTAN/NATO,
Paris, XVIe.

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- (1) Throughout this study this expression excludes the USSR, Albania and Yugoslavia.
(2) C-M(65)88

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Report by the Committee of Economic Advisers

1. The economies of the five Communist countries of Eastern Europe and the Soviet-Occupied Zone of Germany have all developed quickly during the post-war period but, since the beginning of the 1960s, the high growth rates of industrial production have declined, most markedly in the more advanced countries of the region. Recognising that a system of strict centralised planning and control works less efficiently the more sophisticated production becomes, the Eastern European leaders began to introduce some market elements into their economies. The most far-reaching reforms have recently been introduced in the two most industrialised countries of the region, Czechoslovakia and the Soviet Zone(1), while the others are still discussing and experimenting along the lines of the Liberman proposals of 1962. Though it is yet too early to judge the effectiveness of these reforms and experiments, it cannot be excluded that they might one day improve economic performance. Attempts are also being made in some countries to make agriculture more productive by improving incentives for collective and state farmers.

2. The Soviet Union is the predominant trading partner of all the countries under review, but the share of NATO countries in their trade is also quite important and much greater than that of Communist countries in NATO countries' trade. According to Eastern European statistics - which are believed to under-estimate the importance of the countries' trade with the West - the share of the Soviet Union and of NATO countries in the Eastern European countries' foreign trade turnover in 1963 was:

	<u>Share of</u> <u>Soviet Union</u>	<u>Share of</u> <u>NATO countries</u>
Bulgaria	55%	13%
Soviet-Occupied Zone of Germany	48% (53%)(2)	18% (7%)(3)
Rumania	42%	20%
Czechoslovakia	40%	10%
Poland	34%	20%
Hungary	34%	15%

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- (1) The use of the word "country" with respect to the Soviet-Occupied Zone of Germany does not imply that the Zone is considered an independent state like the other Communist countries of Eastern Europe.
- (2) 48% if intra-German trade is included, 53% if it is excluded from the Zone's total foreign trade turnover.
- (3) 18% if intra-German trade is included, 7% if it is excluded.

3. Each Eastern European country's own economic and political aspirations are, of course, an essential factor in Eastern European trade policies towards NATO countries. On the one hand, all Eastern European countries wish to expand their trade with the West and to have greater access to Western technology; on the other hand, none of these countries wants to risk a shift of trade of such a magnitude that it might provoke Soviet countermeasures. Each is, in a varying degree, inhibited by the fear of advancing, to its own or the Communist camp's detriment, Western political objectives, either world-wide or in Eastern Europe itself. Also, account has to be taken of the military co-operation between the USSR and the Eastern European countries and of the presence of Soviet troops in some of the latter. In addition, some countries (Poland and Czechoslovakia) may consider close ties with the Soviet Union indispensable as long as the problems arising out of the absence of a peace treaty ending World War II have not been settled. In the light of these various considerations, at present Rumania, with its active national self-interest policy, is clearly the least constrained. Poland, with its approach to the EEC and initiative in the Kennedy Round, and in progressively lesser degree Czechoslovakia, Hungary and Bulgaria, also appear ready to contract for a further increase in the West's share of their trade. Although active in attempting to promote Western economic contacts, the Soviet-Occupied Zone of Germany is primarily interested in gaining international status and recognition as a separate German state.

4. None of the Eastern European countries is fully satisfied with the benefits derived from COMECON, but they cannot be expected to leave this organization; the urge for such a step has probably weakened as, for the time being at least, the organization has abandoned its more ambitious plans.

5. As past developments have shown, a mere expansion of trade between NATO countries and the Communist countries of Eastern Europe does not automatically reduce the share of the Soviet Union in the latter's trade. During recent years, this has only been the case for Rumania, whereas in the case of Hungary a substantial increase in the USSR's share was accompanied by a considerable reduction of the share of NATO countries - i.e. Rumania and Hungary seem to be the only countries where an expansion of NATO countries' trade would contribute directly to a loosening of these countries' economic ties with the Soviet Union. All the other countries seem to expand their trade with NATO countries simultaneously with their trade with the Soviet Union - a phenomenon which is comprehensible, given the great interdependence of their economies with the Soviet economy: the demand for Soviet raw materials and energy grows together with these countries' exports of finished and semi-finished goods to NATO countries.

6. Though the commodity structure of the Eastern European countries' exports to the West is changing, trade relations with the West will continue to be limited by the small range of goods these countries have to offer, the poor quality of these goods, the inadequate servicing facilities, etc. and also by the quantitative and other restrictions which hamper the entry of these countries' exports into Western markets.

7. As far as the economic policy of NATO countries is concerned, the Committee feels that, in spite of the various obstacles hampering trade with the Eastern European countries and the fact that a mere expansion of NATO countries' trade with these countries will not necessarily reduce their economic dependence on the Soviet Union:

- (i) NATO countries should continue to encourage trade relations with the Eastern European countries; indeed, in the absence of such encouragement, their present share in these countries' trade might significantly decrease; in addition, there may be a link between trade with the West and the extent to which economic reforms are introduced in Eastern Europe: on the one hand such reforms, as they leave greater freedom to the individual enterprises in the choice of their suppliers and customers, may in the future favour an expansion of trade with the West; on the other hand this expansion of trade, even when accompanied by an increase of trade between Eastern Europe and the Soviet Union, may help in making new economic measures work smoothly and thus contribute towards introducing in Eastern Europe an element of freedom which may grow and even have a liberalising effect on the political life of these countries;
- (ii) they should endeavour to facilitate the access of Eastern European products to their markets by whatever measures they feel appropriate, taking care, however, not to damage the legitimate interests of other countries, especially those of the free world which are still in the course of development. In particular, they might explore the possibility of removing quantitative restrictions on goods imported from Eastern European countries on condition that these countries undertake to avoid any action likely to disrupt Western markets. In addition, Western European countries should give close consideration to the approaches made by some Eastern European countries to international economic organizations such as GATT; it appears, indeed, that the outcome of the contacts made by Poland with GATT, in the framework of the Kennedy Round, and with the European Economic Community,

will strongly influence the attitude of other Eastern European countries towards Western economic organizations. Western countries should also further examine the problem of extending credits to Eastern European countries, taking account of the need to avoid giving state-trading countries the opportunity of playing off one Western firm against another; in the view of a number of delegations, NATO countries should aim at co-ordinating their credit policy towards these countries, a problem which has not been fully discussed in the course of this exercise; in general, Western countries should pursue an economic policy flexible enough to allow them to exploit any opportunity that future economic developments in Eastern Europe may offer, bearing in mind the numerous differences among individual countries with respect to such factors as their size, geographical situation, history, stage of development, dependence on the Soviet Union, etc.;

- (iii) they should continue to study, in NATO, economic developments in the individual Eastern European countries and also to consult on the economic policies which may be applied to Eastern European countries with a view to furthering the interests of the Alliance.