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WHEAT PURCHASES BY THE COMMUNIST COUNTRIES AND
SOVIET GOLD SALES ON THE FREE WORLD MARKETS

Note by the Chairman of the Committee of Economic Advisers

A previous report(1) by the Committee of Economic Advisers on wheat purchases by the Communist countries and on Soviet gold sales on the Free World markets in 1963/64 has already been noted by the Council last year(2). Since then, both the wheat purchases and the gold sales have continued. In October 1965, their importance was emphasised by several Permanent Representatives when the Council(3) examined a report by the Committee of Economic Advisers on economic developments in the Soviet Union(4).

2. In the attached report, information has been collected on the wheat purchases and the gold sales in 1965/66. An attempt has been made to assess their magnitude, and to set out the causes of such transactions and their economic implications for the USSR and for the Free World. Longer term prospects are also outlined.

(Signed) F.D. GREGH

OTAN/NATO,
Paris, (16e).

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- (1) C-M(65)21
 - (2) C-R(65)14
 - (3) C-R(65)45
 - (4) C-M(65)81

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WHEAT PURCHASES BY THE COMMUNIST COUNTRIES AND SOVIET GOLD
SALES ON THE FREE WORLD MARKETS

Report by the Committee of Economic Advisers

I. SUMMARY

1. In 1965, as in previous years, Communist countries bought from the Free World substantial quantities of wheat for delivery during the crop year 1965/66. These have been estimated at 9.4 million tons for the Soviet Union, 6.2 million tons for Communist China and 3.3 million tons for the Eastern European countries.

2. These large-scale imports of wheat followed poor grain harvest in a number of Communist countries notably the Soviet Union. In the latter the 1965 grain crop has been estimated at about 100-110 million tons compared with 120 million tons in 1964. In Communist China the 1965 grain crop, estimated at 185 million tons, was no higher than in 1964. This generally poor performance is the consequence of errors in agricultural policy and of unfavourable weather.

3. The cost in convertible currency to the Soviet Union of wheat purchases from the Free World will be about \$ 600 million. Part of this amount will probably be settled in gold and it can be expected that the Soviet Union will sell gold to the value of \$ 450 to \$ 500 million. In order to avoid excessive depletion of their gold reserves, the Soviets may, at least in the short run, reduce their imports of industrial goods from the Free World.

4. The wheat purchases also entail certain consequences for the West. Not only the surplus stocks of wheat have been reduced, but freight rates have been firmer during the past few months and Soviet gold sales provide a useful contribution to total Free World reserves.

5. As to the future, both Communist China and the Eastern European countries are likely to continue to import appreciable quantities of grain from the Free World, even in normal years. Forecasts are more difficult in the case of the USSR, but in the light of her present difficulties, the possibility of recurring Soviet purchases, even on a substantial scale, cannot be excluded.

II. FACTUAL BACKGROUND

6. Following the precedent of the last few years, in 1965 Communist countries have bought on the Free World markets substantial quantities of wheat. In particular, purchases by the Soviet Union have been of the same order of magnitude as the huge

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imports of 1963/64(1). On the basis of the information available, notably that provided by certain delegations(2), the following estimates of wheat imports by Communist countries during the 1965/66 crop year(3) can be made(4):

Soviet Union	:	9.4 million tons	
Eastern Europe	:	3.3	" " (5)
Communist China	:	6.2	" "

7. The disappointing performance of agriculture in Communist countries is due largely to the shortage of agricultural equipment and the lack of interest of a peasantry deprived of real economic incentives. This is a consequence of forced collectivisation, lack of investment in the farming industry, measures restricting the right of private ownership and the freedom of action of the farmers, and the often inopportune intervention of the central bureaucracy. Adverse weather was an important factor in the Soviet Union, and there were other reasons which vary from one country to another.

8. In Communist China, the 1965 grain crop has suffered from a protracted drought in the northern provinces although the rice crop in the southern provinces was probably more or less normal. Estimated at 185 million tons, the grain crop has been no higher than in 1957 and in 1964. For a number of years now, the growth of the Chinese population (15 million persons annually) has not been accompanied by a corresponding increase of agricultural production. Consequently, wheat imports by Communist China have become a permanent feature of her foreign trade, as proved by the very substantial purchases of the last few years and by the recent agreement with Canada, which provides that she will import from 3 to 5 million tons of wheat between 1st August, 1966, and 31st July, 1969. In addition, by common agreement deliveries may be increased to a minimum of 4.5 million tons and a maximum of 7.5 million tons over the same 3-year period. Alternatively, the agreement may be extended to 5 years and deliveries to a minimum of 7.5 million tons and a maximum of 12.5 million tons(6)

(1) See C-M(65)21

(2) AC/89-WP/169, AC/127-WP/168/4 - Notes by the German Delegation
AC/89-WP/170, AC/127-WP/168/3 and 6 - Notes by the Canadian
Delegation

AC/89-WP/172, AC/89-WP/174,) - Notes by the United Kingdom
AC/127-WP/168/2 and 5) Delegation

AC/89-WP/173, AC/127-WP/168/1 - Notes by the United States
Delegation

(3) In this context the 1965/66 crop year means the period from July 1965 to June 1966, except in the case of Canada where it covers the period August to July.

(4) See table at Annex.

(5) The United Kingdom Authorities estimate that purchases of wheat by Eastern Europe may amount to about 4 million tons in the current crop year.

(6) AC/89-WP/178

9. The situation in the Eastern European countries is much more complex. Even if the structural weaknesses of their economies were put right, it is very unlikely that Czechoslovakia and the Soviet-occupied zone of Germany would be able to meet the demand for grain through domestic production. The fact that these countries buy some of their imports in the West rather than in the Soviet Union can be considered as an indication of the dwindling Soviet wheat surplus available for export even when production has been normal. As regards the other countries of Eastern Europe, the production of which should normally meet the local demand, their imports are in the main attributable to the inadequate progress of their agriculture. In 1965, according to available estimates, 5% to 15% less grain than in 1964 has been harvested in the Soviet-occupied zone of Germany and in Czechoslovakia. The Hungarian and Bulgarian crops are likely to have remained unchanged at their 1964 level. On the other hand, Poland reports its best crops since 1961, and very good results can also be expected in Rumania (increase of 10% to 15% as compared with 1964). Eastern European countries' grain imports average 7 to 8 million tons a year. During 1960/63, 4 to 5 million tons were delivered annually by the Soviet Union, but owing to the latter's poor harvest in 1963 supplies from this source dropped to 2.7 million tons in 1964. In view of the general success of this year's crop in most Eastern European countries and its failure in the Soviet Union, these countries will probably reduce even further the Soviet Union's share in their grain imports.

10. In the Soviet Union, although the Seven-Year Plan (1959-1965) provided for a 70% increase in gross agricultural output, in fact, according to official data, the actual increase has been less than 10%. As regards the 1965 grain harvest it has been estimated at about 100 to 110 million tons(1) compared to 120 million tons in 1964 and 95 million tons in 1963. This disappointing result can be attributed largely to the unfavourable weather conditions which have affected most grain-growing regions; storms and excessive rainfall in the Ukraine and the Caucasus and exceptional drought in the Virgin Lands. The present shortage of grain has been aggravated by the following factors:

- (i) increasing domestic requirements as a result of demographic expansion (the population is increasing by some 3 million a year);
- (ii) the recovery of livestock herds combined with a rise in the price of meat (20-50% for beef, 30-70% for pork, 10-70% for lamb), effective from 1st May, 1965, which has encouraged farmers to divert bread grains(2) from their normal purpose in order to use them as fodder;

(1) The United States estimates correspond to the lower figure, and those of the United Kingdom to the higher.
(2) A high proportion of the bread grain harvest in 1965 was in any case unfit for human consumption.

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- (iii) commitments to export wheat to other countries: the countries of Eastern Europe, Cuba, the United Arab Republic and other developing nations;
- (iv) the cumulative effect of past errors in Soviet agricultural policy.

11. The recent wheat purchases confirm the necessity and the urgency of the measures taken in the spring of 1965 by the Soviet leaders in favour of agriculture: a rise in the price paid for compulsory deliveries of wheat and rye to the State(1), a substantial rise in the price paid for above-quota deliveries of grain, for which the State will henceforth pay 50% more than the normal price, a reduction in the volume of compulsory deliveries (reduced from 68 million tons in 1964 to 56 million tons in 1965) which should permit an increase in above-quota deliveries, a rise in the incomes of collective farmers, a general moratorium on collective farm debts to the State, a substantial increase in investment in agriculture (\$ 79 billion are to be invested from 1966 to 1970, i.e. almost as much as has been invested in this sector of the economy since 1945).

III. IMPLICATIONS FOR THE USSR AND FOR THE FREE WORLD

12. From the point of view of the Soviet Union, imports of wheat from the West might have the following consequences:

- (i) an increase in sales of gold. A rough calculation(2) suggests that the cost of the wheat purchases will amount to at least \$ 590 million to which must be added transport costs payable in hard currency, estimated at about \$ 60 million. However, since 1 million tons of wheat from the Argentine has been bartered for Soviet petroleum products, the total amount which the Soviet Union will be called upon to pay in convertible currency for the wheat delivered to her during crop year 1965/1966 will probably reach about \$ 600 million. Following their wheat purchases during the second half of 1963 and the first half of 1964, total sales of gold by the Soviets amounted to \$ 550 million in 1963 and \$ 450 million in 1964, compared with an annual average of \$ 235 million during the years 1960, 1961 and 1962. According to provisional estimates by the American Authorities, Soviet gold reserves in August 1965 totalled \$ 1,500 million(3). These are being increased from indigenous gold-mining at an annual rate of \$ 150-175 million according to figures

(1) This increase amounted to more than 10% for deliveries from collective farms. In the case of State farms where the prices paid by the State are generally lower than those paid to the collective farms, the difference has been reduced and even abolished altogether for deliveries from certain regions.

(2) See table at Annex.

(3) AC/127-R/162, Item I.

published in January 1964. According to various Western estimates, it seems that the Soviets will be obliged to sell a total of \$ 450-500 million worth of gold in order to finance the wheat purchases during the crop year 1965/1966. Various press reports indicate that Russian sales of gold in September, October and November 1965 amounted to about \$ 225 million. These were undertaken through the London and Paris markets and partly direct with the Bank for International Settlements in Basle;

- (ii) a continuation during the coming months of the constriction of orders for industrial goods placed with Free World suppliers, which has persisted since the time of the wheat purchases in 1963/64. The Soviet Union will no doubt endeavour to arrange its foreign trade in such a way as to release the resources necessary to pay for part of her wheat imports.

13. The Soviet wheat purchases also entail certain consequences for the Western world:

- (i) a more buoyant market in freight rates(1) and the re-entry into service of a certain number of laid-up bulk carriers and oil tankers which can also be used for transporting grain;
- (ii) a reduction in the surplus stocks of the traditional wheat exporting countries and consequently some rise in the level of world prices; the size of United States and Canadian wheat stocks is, however, such as to inhibit any prolonged upsurge;
- (iii) a recovery of the Canadian trade balance and a reduction in that country's balance of payments deficit. Greater prosperity in the agricultural sector will have favourable repercussions on other branches of the Canadian economy;
- (iv) a significant addition to the gold reserves of the Free World. The rate of increase of gold output in the Free World has in fact fallen steadily since 1962, from 6.6% to 3.9% in 1964. Soviet sales amounting to some \$ 450 million in 1965 would represent nearly 30% of Free World gold output (\$ 1.4 billion in 1964); they should therefore somewhat ease the pressure of world demand for gold;

(1) For example, maximum and minimum freight rates per ton for the St. Laurent-United Kingdom crossing were as follows in s. and d.:

July 1964	: 33s. 0d.,	32s. 9d.
July 1965	: 42s. 6d.,	41s. 3d.
August 1964	: 36s. 6d.,	36s. 6d.
August 1965	: 48s. 6½d.,	45s. 0d.

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- (v) industrial countries from the Free World might well experience in the next few months a continued constriction of their exports of manufactured and capital goods to the USSR.

IV. LONGER-TERM PROSPECTS

14. As regards longer-term prospects:

- (i) Communist China will in all likelihood continue, at least within the foreseeable future, to import appreciable quantities of grain from the Free World. This policy is dictated by the failure of domestic agricultural production to keep up with population growth, and also, to a lesser degree, by the fact that to some extent it pays Communist China to grow rice for export rather than wheat for internal consumption;
- (ii) in the Soviet Union any policy aimed at improving the agricultural situation will inevitably take time to yield results. In the meantime, it is likely that imports of grain from the West will continue, at least in bad years, especially as with the growth of the population and the rise in the standard of living the requirements are increasing. It may be safely assumed that the Soviet policy goal is to be largely independent from grain supplies from the West as soon as possible; this is indicated, i.e., by their announcement of a programme of huge investment in agriculture during the period from 1966 to 1970. If this programme were successfully implemented, by 1970/71 the Soviet Union would be rendered practically self-sufficient in both good and bad years. However, at this early stage, it is difficult to forecast how much of it will in fact be carried out, and doubts can be reasonably entertained as to the possibility of its completion within the next five years;
- (iii) the Eastern European countries, which in the past have normally obtained the main part of their grain imports from the USSR may have to turn to an increasing extent to Western markets for alternative sources of supplies. However, the possibility also exists that in the longer run the Soviet Union becomes again a net exporter of grain and contributes rather more to Eastern Europe's imports of grain than in the last few years. This development will, of course, depend upon climatic factors and the success of current Soviet plans to foster their agricultural production. As regards Western grain supplies, the Eastern European countries will be faced with the problem of finding ways and means of paying for them. If they do not succeed in stepping up their exports to the Free World, they may have to put a brake on their imports of industrial goods from it.

ESTIMATED COMMUNIST COUNTRIES' WHEAT IMPORTS FROM THE
FREE WORLD DURING THE 1965/66 CROP YEAR(1)

Importing country	Exporting country	Quantities (in metric tons)	Approximative(7) fob value (in million US \$)
Communist China	Canada(2)	2,158,000	\$ 142.3
	Australia(3)	1,840,000	\$ 107.5
	Argentina	2,200,000	\$ 117.0
		<hr/> 6,198,000	<hr/> \$ 366.8
USSR	Argentina(4)	2,200,000	\$ 117.0
	Australia(3)	600,000	\$ 36.4
	Canada(2)	6,031,000	\$ 397.7
	France(5)	600,000	\$ 34.9
		<hr/> 9,431,000	<hr/> \$ 586.0
Eastern Europe	Canada(2)(6)	1,159,000-	\$ 76.4-\$ 84.5
		1,281,000	
	France(6)	1,800,000	\$ 102.1
	United States(6)	45,000	\$ 2.6
	Mexico(6)	300,000	\$ 18.0
		<hr/> 3,304,000- 3,426,000	<hr/> \$ 199.1-\$ 207.2

- (1) For a definition of 1965/66 crop year see footnote (3), page 2
- (2) Shipment figures given by Canadian Authorities, see AC/127-WP/168/3
- (3) Data furnished by the United Kingdom (see AC/89-WP/172 and AC/127-WP/168/5)
- (4) Of which \$ 53.2 million represent the fob value of one million tons of wheat bartered for Soviet gas-oil following an agreement concluded in April 1965.
- (5) The USSR has so far failed to contract for 100,000 tons of the original French offer.

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(6) As regards sales to Eastern Europe, lack of sufficient data makes it impossible to give a breakdown by country; the figures are those furnished by the Canadian Delegation (AC/127-WP/163/3) and United States Delegation (AC/89-WP/173). Canadian wheat sales, estimated at a possible 1.2 - 1.3 million tons, are made up of a minimum of 210,000 tons ordered by Czechoslovakia to date under their long-term agreement with Canada; and a possible 1.0 - 1.1 million tons representing deliveries which could be made in 1965/66 under long-term contracts concluded in 1963 and 1964 between Canada, Bulgaria, Poland, Hungary and the Soviet-occupied Zone of Germany. It should be noted that deliveries of the amounts mentioned could extend to October or November 1966, beyond the end of 1965/66 crop year. French wheat sales are composed of 300,000 tons sold under contract to Poland and 1.5 million tons to be delivered under agreements with the Soviet-occupied Zone of Germany, Bulgaria, Poland and a tentative arrangement with Hungary (likely to cover the sale of 170,000 tons). United States wheat sale is for shipment to the Soviet-occupied Zone of Germany. The exact destination of Mexican wheat exports, to Eastern Europe is not known.

(7) Average fob prices per metric ton used to calculate approximate value of Communist countries' wheat imports:

Canada: US \$ 65.93 (source: note by Canadian Delegation, AC/127-WP/168/6).

France: US \$ 58.23 for sales to USSR (source: French Delegation) and US \$ 56.70 for other sales (average price of Francs 280 per metric ton quoted by Assemblée Générale des Producteurs de Blé).

Australia: US \$ 60.66 for Soviet purchases and US \$ 58.45 for Chinese purchases (source: note by United Kingdom Delegation AC/89-WP/172).

United States: US \$ 58 (source: note by United States Delegation AC/127-WP/168/1).

Argentina: US \$ 53.20 (source: Soviet-Argentina agreement as reported in the Press).

Mexico: US \$ 60 (estimated).