

GAO

## Testimony



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Status of GAO's Review of Estimates of the  
Soviet Economy

Statement of  
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Before the  
Committee on Foreign Relations  
United States Senate



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Dear Mr. Chairman and Members of the Committee:

I am pleased to be here today to discuss the status of our ongoing review of estimates and analyses of the size of the Soviet economy. We have focused our work to date on (1) identifying key estimates and assessments of the economy and (2) outlining, on a preliminary basis, the key issues and areas of debate with respect to these estimates. I should note at the outset that we have encountered difficulty in obtaining information from the Central Intelligence Agency, which prepares a key estimate.

#### ESTIMATES OF SOVIET GNP

Within the U.S. government, the Central Intelligence Agency (CIA) has responsibility for preparing annual estimates of the Soviet Union's gross national product (GNP). These estimates are perhaps the most widely used and detailed alternative to the Soviet Union's problematic official estimates, which have been consistently discounted by Western economists. There also exist a number of critiques of the CIA's methodology and calculations, as well as some alternate estimates, including those most recently voiced by Soviet economists.

To date, we have concentrated on the CIA's estimate and the methodology on which it is based. The CIA estimates Soviet GNP for a base year (currently 1982) and then calculates real growth rates

for other years using data on changes in the various GNP components. As described by the CIA in various publications, the agency follows a number of steps in developing the base year estimate, including

- constructing national income accounts showing incomes and expenditures for the public and household sectors, from which total GNP in official (or "established") ruble prices is calculated;
- disaggregating total GNP by sectors of origin (such as agriculture and industry) as well as by end use (e.g., consumption and investment); and
- adjusting established prices to "factor cost" prices<sup>1</sup> by eliminating the distortions caused by turnover taxes and subsidies, and replacing arbitrarily set profit margins with uniform rates of return on capital.

Using this methodology, the CIA produces estimates of GNP in both official and factor cost prices for the base year. Real growth in GNP for other years is computed from component growth rates weighted by the value added of these components in the base year. The growth rates are generally estimated using quantity data, but

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<sup>1</sup>Using these adjusted factor costs provides a better measure of real resource allocations among the GNP components.

in some cases rely on ruble values. For 1989, the CIA estimated Soviet GNP at factor cost to be 745.8 billion rubles (in constant 1982 rubles)--representing a growth rate of 1.4 percent over the preceding year.

The CIA also estimates the comparative size of the U.S. and Soviet economies. This estimate involves constructing purchasing power parity ratios. These ratios are computed by comparing the amount of rubles relative to dollars required to purchase the same quantities of comparable goods and services in the Soviet Union and the United States. A weighted average of these ratios becomes the exchange rate used to compare the two countries' GNP estimates. Using this methodology, the CIA estimated that the Soviet economy was about half the size of the U.S. economy in 1989.

#### ISSUES AND QUESTIONS CONCERNING METHODS OF ESTIMATING SOVIET GNP

The CIA itself has highlighted a number of problems and uncertainties with respect to calculating Soviet GNP; others have challenged specific elements of the CIA's methodology. These concerns include

-- the quality of Soviet official statistics, which the CIA uses in constructing its estimates;

- the difficulty in accurately measuring quality changes;
- the problem of measuring the "second economy"--the variety of private and/or illegal activities that may contribute to GNP;
- the problem of limitations in applying purchasing power parity methodology to centrally planned economies such as the Soviet Union, in which shortages exist and are not reflected in the price statistics;
- the appropriateness of the methodology used to compute adjusted factor cost prices; and
- the variety of potential biases in the data used to construct the sector indexes that could influence the growth rate calculations both upwards and downwards.

#### AVAILABILITY OF INFORMATION

#### ON CIA ESTIMATES OF THE SOVIET ECONOMY

The CIA and the Joint Economic Committee have published a substantial body of work describing the agency's methodology. The CIA has also, through conferences and discussions with outside experts and scholars, made efforts to refine its methodology and remain sensitive to the need to make changes, where necessary, to improve its ability to calculate Soviet GNP. CIA analysts have

raised many of the concerns cited above in an effort to provide a necessary context within which to understand the limits of the agency's GNP calculations.

Our own work to date has concentrated on collecting and analyzing the information published by the CIA and others in order to better understand the basis for the estimates the U.S. government produces and uses. To improve our understanding of the CIA's estimates, we have asked the CIA for additional information, including unclassified publications and the names and written analyses of experts that we understand the CIA has employed to critique its methodology. We have also requested a series of meetings to discuss the CIA's methodology in greater detail.

However, the CIA has declined to make available to us any critiques or evaluations of its methodology, and has been unwilling to provide the names of experts it has used to assess its methodology. Moreover, the agency has, to date, provided none of the requested publications, although it did agree, late last week, to send us two documents. We were able to obtain other requested publications elsewhere. The CIA has also refused to meet with us or provide any briefings; its position is that it will provide briefings on this topic to its congressional oversight committees as requested. Because we are still in the process of analyzing the available data, we cannot yet tell how severely the

CIA's unwillingness to cooperate will limit our efforts to respond to your request that we analyze estimates of the Soviet economy.

Mr. Chairman, this concludes my statement. I will be happy to try to respond to any questions you may have.