profitable, prestige projects—often duplicative of projects in other republics—and to ignore new or small enterprises with higher profit potential. In addition, investment strategy has stressed import substitution rather than export promotion. Investment priorities also have favored heavy industry rather than sectors such as light industry and agriculture in which Yugoslavia has traditionally had a comparative advantage.

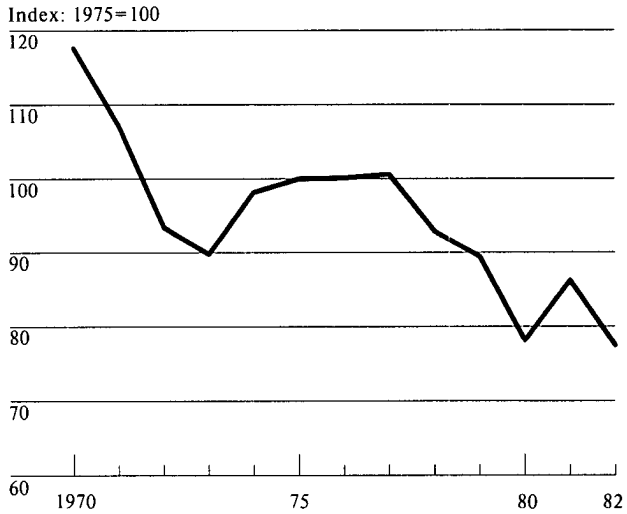
Decentralization gave authorities in the republics considerable autonomy in making economic decisions. These officials encouraged the use of foreign credits to finance major industrial projects within their regions. Not only did they adopt more protectionist and isolationist policies, they also pursued similar development plans. This led to redundancy in major investment projects and boosted the demand for capital goods imports. The republics also discouraged the flow of goods, capital, foreign exchange, and labor to other republics.

Croatia, the most financially troubled republic, provides a good example of the problems caused by poor judgment in the use of foreign credits. During the 1970s, Croatia borrowed abroad to increase its oil-refining capacity (even though excess capacity already existed in the Yugoslav oil-refining industry), Croatia also built a synthetic fertilizer plant, an aromatic chemical plant, a petrochemical plant, and—with Slovene participation—a nuclear power plant. Although some of these projects may have economic potential, they do not generate sufficient foreign exchange earnings or save enough on import outlays to enable Croatia to pay its debts without help from the federation. Croatia's payments problems played a major role in precipitating the recent debt crisis.

What Role Has the Exchange Rate Played in the Crisis?

In the crucial period following the first oil price shock in 1973, Yugoslavia failed to adjust its exchange rate to offset differences between its inflation rate and those of its trading partners. In fact, the real effective exchange rate appreciated by 12 percent between 1973 and 1977 (see figure 1). Declining external competitiveness hurt export performance, encouraged imports, and further widened the trade deficit. Instead of taking necessary adjustment measures to deal with balance-of-payments problems, Belgrade continued to increase foreign borrowing to maintain import levels and support ambitious development plans.

Figure 1
Yugoslavia: Trends in Real Effective Exchange Rates, 1970-82[a]



[a] Trade weighted against a basket of 16 competitors.

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How Did the Collapse of the Yugoslav Foreign Exchange Market Contribute to the Debt Crisis?

Until 1980 a foreign exchange market existed at the national level in the form of interbank meetings between the National Bank and commercial banks involved in foreign exchange operations. The market collapsed that year when the National Bank stopped selling foreign exchange after its reserves were halved the previous year to $1.2 billion. Thereafter, firms and banks refused to part with hard currency at the official rate because it was so underpriced and they feared they could not repurchase it when needed.

The firms and banks then had to find other ways to obtain foreign exchange. In many cases, firms were unable to generate enough hard currency earnings, and banks had insufficient reserves. Yugoslav banks

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Yugoslavia: Key Questions and Answers on the Debt Crisis

An Intelligence Assessment

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EUR 84-10011
January 1984

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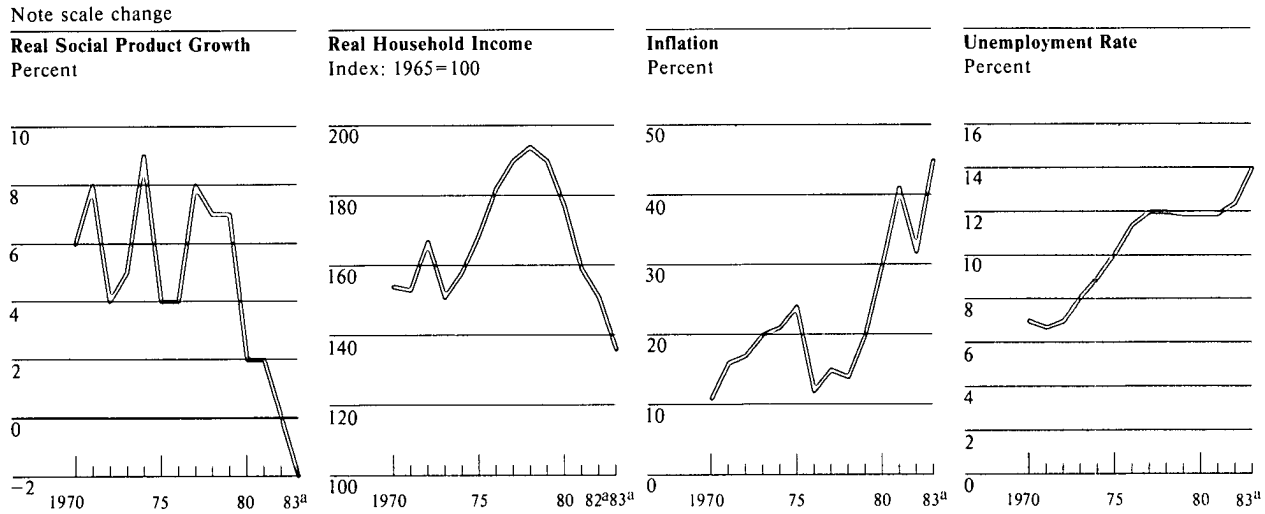
Figure 3
Yugoslavia: Domestic Economic Indicators, 1970-83



[a] Estimated, as of December 1983.

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bank refinancing; and $1 billion in supplier credits. Belgrade has already begun negotiations with the IMF and its government and bank creditors

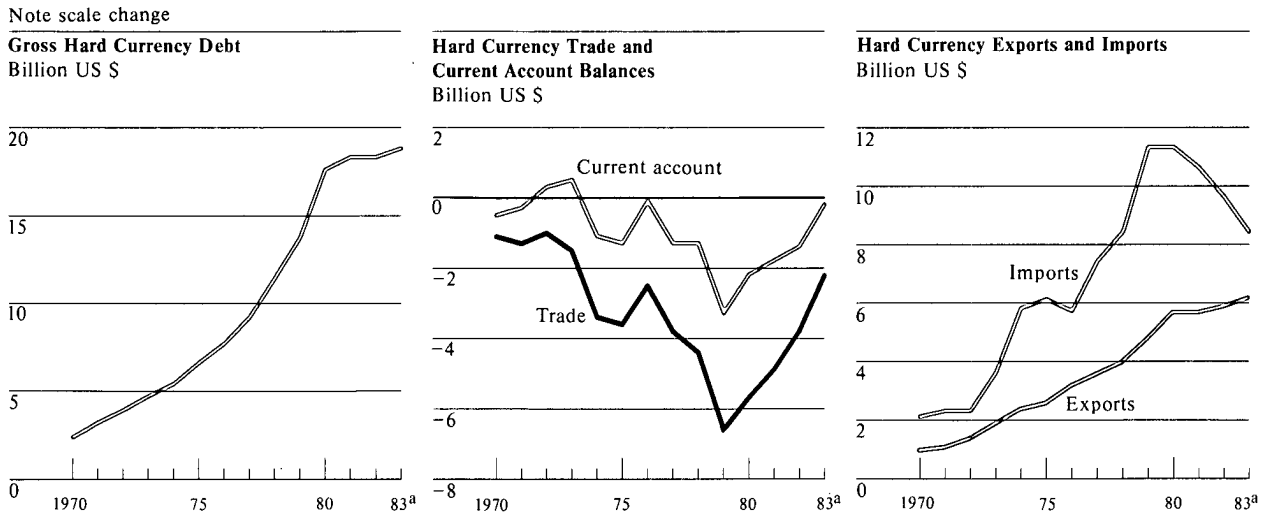
Beyond 1984, we believe that Yugoslavia will need still more debt relief and financial assistance. In 1985 and 1986, the National Bank of Yugoslavia projects that $3.0 and $2.8 billion, respectively, of medium- and long-term debt will mature, as compared with $2.9 billion in 1984. Generating the large current account surpluses needed to restore lender confidence and to reduce debt will be difficult. Imports have already been cut drastically, and it will take time for exports to grow enough to reduce the trade deficit substantially.

What Are the Attitudes of Major Creditors Toward Another Financial Assistance Package for 1984? Bankers and Western governments have already offered to reschedule 1984 maturities.

Yugoslavia will not need new loans and because they are concerned that a new money cushion may ultimately be used to finance capital outflows that have shown up as a $1.2 billion turnaround in the errors and omissions category. The IMF has dropped its request that bankers provide new loans. Government creditors have agreed to carry over into 1984 undisbursed "Friends of Yugoslavia" export credits. Governments probably will not make specific pledges on new export credits, but most indicated a willingness to extend short-term cover and many were willing to extend some new medium- and long-term export credits

Both offers are contingent on Yugoslavia's reaching agreement with the IMF on a standby program for 1984. IMF negotiating teams have visited Yugoslavia twice but have failed to resolve differences over how quickly to increase interest rates to real levels and

Figure 2
Yugoslavia: External Economic Indicators, 1970-83



[a] Estimated, as of December 1983.

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measures passed (including the new foreign exchange law) do not represent fundamental changes in the economic system and in some cases (a price freeze, for example) they even run counter to the Commission's recommendations.

Given the encumbrances and inertia of the political system, we doubt that the Commission's work will lead to meaningful changes in the economic system. The economic costs of true reform—rising unemployment and bankruptcy—are probably too high to be politically feasible. The only "reforms" likely to be implemented will involve modifications of the current system—that is, new methods of allocating foreign exchange and greater scope for foreign investment, small enterprises, and private activities. Political constraints probably will preclude any major steps to alter self-management, to reverse the process of political decentralization, or to introduce true markets. Moreover, effective bankruptcy rules are needed to force firms to act in a financially responsible manner and to prevent subsidization of inefficient firms. Without these kinds of reforms, we believe there is no hope of controlling underlying inflationary forces and rationalizing investment decisions.

What Is the Financial Outlook for Yugoslavia?
Yugoslavia started 1984 in marginally better financial shape than 1983, but it will need additional debt relief. If Belgrade can achieve a surplus of $350 million this year and banks maintain their short-term exposure at current levels, Yugoslavia will face a financing requirement of approximately $3.1 billion (see table). We estimate that Yugoslavia will have approximately $4.3 billion available to meet this requirement—$1 billion from the IMF and World Bank; $1 billion in government refinancings, new export credits, and export credits left over from the 1983 "Friends of Yugoslavia" package; $1.2 billion in

Although concern for the balance of payments occasionally led Belgrade to tighten monetary policy; devalue the dinar; and impose import, credit, and price controls, these policies only resulted in temporary improvements. After brief periods of adjustment, foreign borrowing rapidly expanded to finance the capital imports necessary to revive the pace of domestic investment. By the end of the 1970s, hard currency debt had soared to $17.6 billion, inflation was running at a 30-percent annual rate, and Belgrade was trying to cope with a hard currency current account deficit that had reached a record $3.3 billion in 1979, representing some 5 percent of gross social product.

Workers' self-management (see inset) added to the country's strong inflationary bias. Worker involvement in the allocation of "profit" (in Yugoslav usage—the difference between revenues and costs exclusive of labor) tends to favor payments to workers rather than investment. Therefore, instead of financing investment out of retained earnings, enterprises relied heavily on credits from domestic banks (which fueled inflation) and from lenders abroad (which added directly to the foreign debt). Some other problems that prominent Yugoslav economists blame on the self-management system are higher than necessary administrative costs, declining business initiative, and slowing growth in labor productivity. These have combined to make Yugoslav goods less competitive in world markets, thus compounding the balance-of-payments problem.

The investment allocation process has proven incapable of directing resources to the most profitable industries, leading to an increasing redundancy in industrial capacity and a growing number of firms requiring subsidization. The banking system in Yugoslavia, as in many developing countries, has played a key role in financing investment. In Yugoslavia's decentralized banking system, the National Bank (the central bank) controls the overall level of domestic bank credit and Federal authorities have an indirect role in its use through their designation of priority sectors in five-year and annual economic plans. Commercial banks, however, are directly involved in deciding which investments to fund, and commercial banks and enterprises can borrow directly on international capital markets. Because the demand for credits is very high, banks have turned to nonprice rationing techniques in allocating credit. In the self-management system, the bank's policies are heavily influenced by large companies (which set up banks and are often major borrowers) and local politicians (who often serve on the board of directors at banks and enterprises). Partly because of their influence, the banks have tended to favor large, not necessarily

Workers' Self-Management: Theory and Reality

In 1950, Tito created the workers' self-management system primarily to complete his political and ideological break with the USSR and Stalinism. By introducing a worker-managed economy radically different from the Soviet model, he also wanted to create a system that would generate genuine popular support for his regime.

In theory, the self-managing enterprise consists of a series of cooperatives with ultimate authority lying in their members—the workers. Workers participate in management through workers councils, which select and fire enterprise directors, set wage and labor policy, and allocate enterprise earnings.

The real influence of workers on enterprise decisions falls short of these constitutional rights. Members of workers councils complain that managers and their teams of experts dominate the highly bureaucratized and time-consuming meetings that set enterprise policy. Frequent strikes over wages demonstrate that the system does not ensure high morale or improve labor-management relations.

Firms are divided into smaller work units in order to maximize worker involvement. However, greater worker participation has not translated into higher productivity. Fragmentation within enterprises complicates and raises the cost of developing and implementing enterprise policy. As for personal motivation, Yugoslav workers are rarely fired for cause and their pay usually is not linked directly with their productivity.

Milka Planinc, president of the Federal Executive Council. *Echo*

approach involves a two-stage process. The first phase focuses on stabilizing the economy by reducing domestic demand, promoting exports, and improving the flow of hard currency by changing the foreign exchange system. More substantial economic reforms will follow in the second stage. It is unclear what form these reforms will take but presumably they will be aimed at increasing the role of market forces. These policymakers have worked closely with Yugoslavia's Western creditors and have also accepted some IMF policy recommendations, including tight monetary and credit targets and a real depreciation of the dinar. Well-informed US Embassy sources report that the FEC, at the behest of critics in the top leadership and Federal Assembly, has drawn up a draconian go-it-alone "Black Option" for use if negotiations with Western creditors and the IMF collapse. This option, however, is in the interest of neither Yugoslavia nor its creditors, and we believe its use is unlikely.

Under Yugoslavia's decentralized system, FEC policymakers do not enjoy the authority their positions might suggest, and they must seek consensus on their decisions. To achieve this, the FEC works closely with the nine-member State Presidency in formulating economic policy and in pressing the Federal Assembly for legislation. But republic and provincial representatives in the Assembly work equally hard to defend the particular interests of their constituents. Assembly members do not accept all FEC initiatives and, in our judgment, are becoming increasingly assertive in policy formulation. For example, in fall 1983 the FEC quickly withdrew an anti-inflationary budget after meeting intense opposition in the Federal Assembly.

What Policy Tools Has Belgrade Used To Deal With the Crisis?

Belgrade has relied on policy options similar to those used in market-type economies to improve the balance of payments and stabilize the economy. It has tightened both monetary and fiscal policies and devalued the dinar. Belgrade has also increased the prices of key goods to reduce price distortions.

The tighter monetary policy, however, has been ineffective—undercut by the rapid growth of interenterprise credits and by the increasing dinar value of foreign currency savings deposits as the exchange rate has depreciated. Federal fiscal policy is largely ineffective as well because the bulk of government spending and revenues are controlled by local governments. In response, Belgrade has tried to strengthen its adjustment effort by administrative controls on prices, imports, and foreign exchange.

What Political Pressures Has the Crisis Created?

Most Yugoslavs, judging from a broad variety of media reports and Embassy contacts, are unhappy to some extent with Belgrade's adjustment measures. Although serious unrest or major acts of economic sabotage have not occurred so far, strike activity is increasing as real wages continue to fall. There are also demands for a purge of "those responsible for the current mess" although the politicians so far are operating on the stand-together or hang-together principle. Another source of pressure is the Yugoslav military establishment, whose leaders are openly urging the civilian leaders to work responsibly.

rapidly increased short-term borrowings from Western banks, but this source dried up in 1982 when Western banks slashed lending to Eastern Europe. Payment arrears began to accumulate, most notably at Croatia's major bank (Privedna Banka, Zagreb). Although other republics and banks—for example Slovenia and its major bank, Ljubljanska Banka—were able to cover their service obligations, the difficulties of some banks tarnished the image of all.

How Does the Collective Leadership System Affect Belgrade's Ability To Deal With the Crisis?

The policymaking institutions bequeathed by Tito—the ruling Communist Party and State Presidency—are led by collective bodies with annually rotating leaderships. This collectivity inhibits bold policy initiatives. Moreover, because the members of these collective bodies in many cases represent rival regional interests, their search for consensus tends to drag out policy debate. Once passed, policy decisions—particularly unpopular administrative controls that go against the interests of particular republics or enterprises—are difficult to enforce without the support of republic and local officials. Regulations are ignored or loopholes are used to avoid their intent. Yugoslav firms, for example, have been lax in following rules that require them to turn over foreign exchange to the National Bank and to repatriate earnings to Yugoslavia.

Belgrade has therefore found it difficult to implement crucial debt management and stabilization policies. Belgrade often has felt constrained to wait until it could use the pressure of foreign creditors and the fear of rescheduling to force passage of needed legislation. The most recent example is the debt repayment law that was passed in July 1983 over the strenuous objections of regional interests only because of this pressure

How Does the Banking System Complicate Federal Government Attempts To Deal With the Crisis?

The National Bank is unable to exert effective control over the total supply of liquidity, a fact that has complicated efforts to dampen domestic demand. The problem lies in the willingness of enterprises to exchange credits with each other to maintain overall liquidity in the face of a more restrictive National Bank monetary policy. In addition, enterprises have fallen behind in repaying credits granted by domestic banks. Although net domestic assets (as defined by the IMF) increased by only 4.5 percent in the first six months of 1983, total liquidity (defined as net domestic assets plus expansion of interenterprise trade credits and the rise in the dinar value of foreign exchange savings deposits) increased by about 22 percent.

What Steps Has Belgrade Taken To Ensure That Scarce Foreign Exchange Is Used for Debt Repayment and Essential Imports?

To compensate for the lack of a foreign exchange market, Belgrade increasingly has used administrative measures to improve the flow of foreign exchange between earners and users. Under temporary measures instituted in October 1981 and May 1982—made permanent by legislation enacted at the beginning of 1983—Yugoslav firms are required to turn over 25 percent of their foreign exchange earnings to the National Bank to pay for energy imports, to help repay foreign debts, and to allow the National Bank to rebuild its reserves. These measures proved insufficient to ensure timely debt repayment, and enterprises and banks fell behind in their payments. The resulting buildup in arrears became a serious problem toward the end of 1982

In July 1983, the Federal Assembly enacted additional legislation to strengthen the National Bank's ability to ensure debt repayment. The new regulation allows the National Bank to tap the foreign exchange resources of commercial banks, to stop imports by blocking the use of a bank's foreign exchange, and to require foreign exchange earners to turn over an additional 5 percent of their earnings to a National Bank fund to support banks with liquidity problems. The new regulation has been effective so far in clearing up arrears, an important condition of the 1983 agreement between Yugoslavia and Western banks. The law also appears to provide an effective mechanism for ensuring timely debt repayment and controlling foreign borrowing

over changes in the newly adopted foreign exchange law. The US Embassy in Belgrade is "guardedly optimistic" that a compromise can be hammered out. Nonetheless, the delays in reaching agreement with the IMF probably will postpone conclusion of the 1984 refinancing until April. Further delays could complicate completion of the agreements as the Yugoslav leadership rotation takes place in May.

What Are the Arguments Against a Formal Rescheduling of Yugoslavia's Debt?
On economic grounds, there are no objective reasons why Yugoslavia should not reschedule its debt. In fact, the 1983 agreement with commercial banks did reschedule privately held debt. Moreover, given the size of Yugoslavia's debt obligations and its inability to raise enough funds to cover its financing requirement, some type of orderly debt relief is necessary. But Belgrade objects on political grounds to a debt-relief package called "a rescheduling" that would be carried out through formal Paris Club arrangements. The leadership argues that a formal rescheduling would be destabilizing, presumably because it would discredit the Titoist model of socialism by placing Yugoslavia in the East European basket case category with Poland and Romania.

We think the government's key economic leaders are nervous because they used up much of their prestige in getting the Federal Assembly to approve the 1983 agreement with Western banks. If they cannot sell a refinancing package this year, a government crisis could follow; Premier Planinc has already threatened to resign several times. Scapegoating could occur, and, more serious in terms of Yugoslavia's future, such a crisis could affect the selection of personnel for this year's rotation of the State Presidency. Finally, some hardliners in Belgrade argue—unconvincingly, in our view—that a formal and open rescheduling would make the leaders appear too tied to the West and compromise their position in the Nonaligned Movement.

What Is the Likely Impact of Yugoslavia's Debt Crisis on Foreign Relations and Political Stability?
Assuming a rescheduling outside the Paris Club takes place, we believe the repercussions in Yugoslavia will be minimal. We believe that the leadership will conclude that it is in greater danger from the general deterioration of the economic situation than from accepting debt relief on Western terms. Indeed, an early, quick, and quiet handling of the debt problem could aid the economic leadership by helping to avoid a repetition of the sharp drop in imports that occurred in early 1983 and the strain caused by long, drawn-out negotiations for debt relief.

We believe it is unlikely that debt relief on Western terms would cause a major realignment of Yugoslavia's economic or political relations with other countries. Yugoslavia will almost certainly continue a policy of nonalignment and maintain good relations with the United States and the Soviet Union, although it will continue to be critical of both countries on specific issues. There is no attractive Eastern option available to Yugoslavia, and any change in balance between the East and West is likely to be marginal in nature. Nor is Yugoslavia likely to risk disruption of its economic ties with the West by refusing to repay its debt obligations.

Yugoslavia: Hard Currency Financing Requirement and Borrowing Sources

Million US $

	1982	1983 [a]	1984 [b]	1985 [b]
Financing requirement	**3,550**	**3,941**	**3,075**	**3,108**
Current account balance	−1,420	125	350	75
Trade balance	−3,781	−1,800	−1,750	−2,025
Exports	5,854	6,150	6,450	6,775
Imports	−9,635	−7,950	−8,200	−8,800
Net services and transfers	2,361	1,925	2,100	2,100
Of which:				
Interest payments (net)	−1,733	−1,690	−1,860	−2,000
Repayment of medium- and long-term loans	−1,853	−2,566	−2,925	−2,983
Repayment of short-term loans (net)	−506	−600	0 [c]	0 [c]
Credits extended by Yugoslavia (net)	−183	−150	−200	−200
Errors and omissions	412	−750	−300	0
Borrowing sources [d]	**2,538**	**4,385**	**4,255** [e]	NA
IMF	563	604	500	NA
International Bank for Reconstruction and Development	NA	330	505	NA
Government loan	NA	801	1,050	NA
Financial credits and rollovers	NA	471	500	NA
Export credits	NA	330	550	NA
Banks	NA	1,620	1,200	NA
New loans	NA	600	0	NA
Medium- and long-term rollover	NA	1,020	1,200	NA
Other	NA	1,030	1,000	NA
Changes in reserves	**−1,012**	**444**	**1,180**	NA

[a] Estimated.
[b] Projected.
[c] Assume short-term credit lines maintained.
[d] The borrowing sources part of the table is set up to reflect the 1983 rescue package. Data for 1982 do not conform to this format.
[e] The main uncertainty in this estimate of borrowing sources is the amount of supplier credits. We have used a level similar to that used in 1983, but it could actually be as low as $500 million, which would halve the projected increase in reserves.

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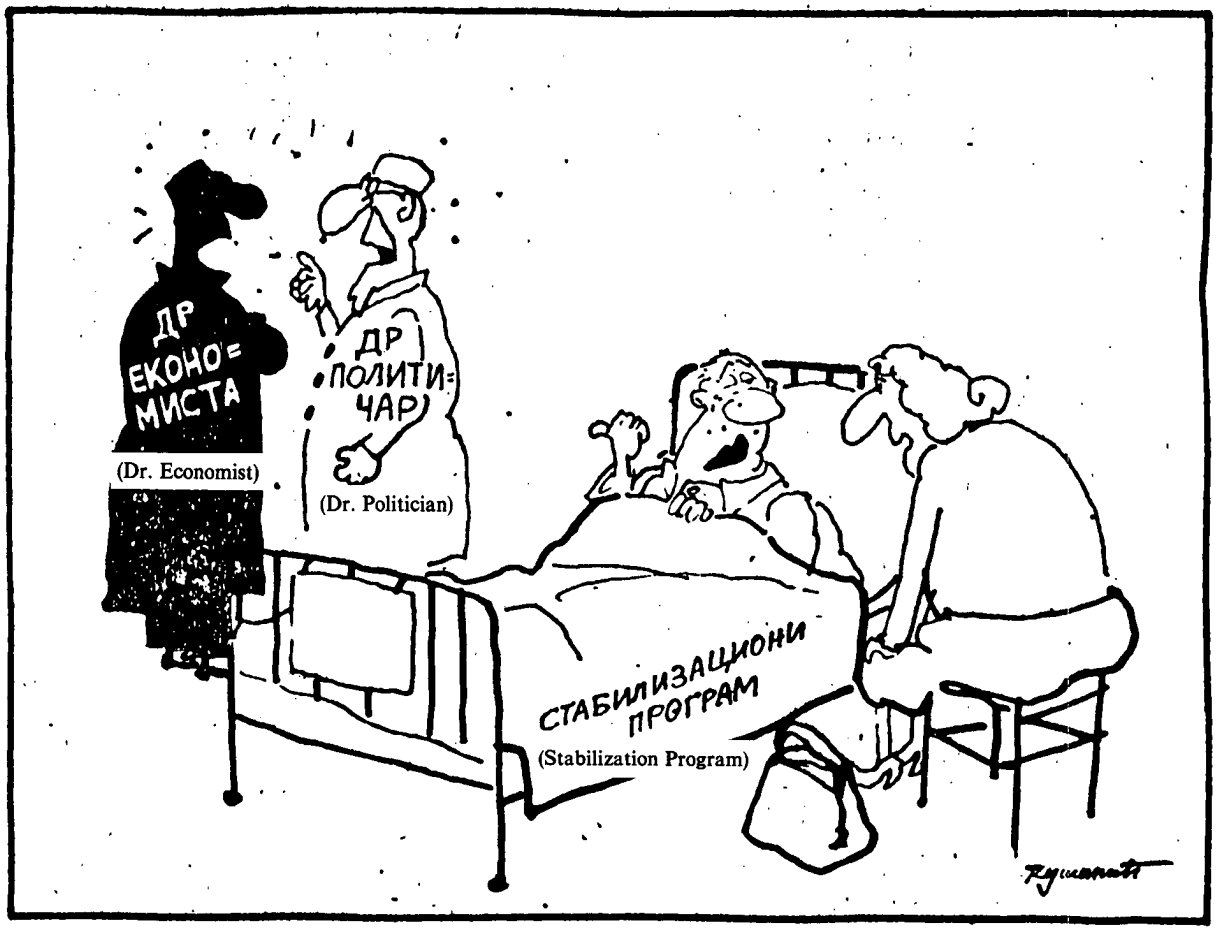

— How are you feeling?
— How do I know? The doctors still are not agreed.

Politica

At the end of 1983, the Federal Assembly again modified the foreign exchange system. Exporters are now required to sell all foreign exchange—in excess of their needs for imported production inputs and for repayment of foreign obligations—to their banks for inclusion in a domestic foreign exchange market. Firms unable to earn foreign exchange but dependent on imported goods will have access to this market for their foreign exchange needs. It remains to be seen what effects these new regulations will have on foreign exchange allocation, but we doubt they will lead to a functioning foreign exchange market because hard currency reserves are too low to give foreign exchange earners confidence in the viability of the market and because the dinar remains overvalued. In addition, in our view, the new regulations do not represent a significant improvement over the previous system because the system remains one of forced sale and administered disbursement of foreign exchange.

What Are the Views of Key Yugoslav Policymakers on Solving the Financial Crisis?

Premier Milka Planinc (president of the Federal Executive Council) and two other FEC members—Zvone Dragan and Janko Smole—are the chief architects of Yugoslavia's current economic strategy. Their

Yugoslavia: Key Questions and Answers on the Debt Crisis

Introduction

Yugoslavia is in the midst of its worst economic crisis since 1948 when, as it was being expelled from the Soviet Bloc, an Eastern trade embargo forced it to reorient its foreign trade and abandon its first five-year plan. Belgrade faces large debt service payments over the medium term and—to avoid domestic political problems—is seeking debt relief and credits outside the traditional creditor clubs. The country's debt problems have forced the government to take belated and politically difficult adjustment measures to deal with chronic current account deficits, an overheated economy, and uncontrolled inflation.

Although these measures have had some ameliorative effect, Belgrade has been able to do little about the causes of the debt crisis, which are imbedded in Yugoslavia's decentralized political structure and in the country's unique system of workers' self-management. In the meantime, the population continues to suffer falling living standards, shortages of energy and some staples, and rising unemployment. The belated and slow progress in solving economic problems and the need to make repeated demands on the population for sacrifice are increasing the strain on the cumbersome collective leadership system.

This paper attempts to answer some of the key questions surrounding Yugoslavia's debt difficulties. Because some of these questions concern economic policy while others address the weaknesses of Yugoslavia's complex economic and political systems, we have chosen a question and answer format in the hope that the issues can be more clearly understood. A more detailed examination of the financial aspects of the crisis can be found in Intelligence Assessment EUR 83-10216, September 1983, *Eastern Europe: Facing Up to the Debt Crisis.*

What Are the Causes of Yugoslavia's Financial Crisis?

The major cause of Yugoslavia's debt crisis was the overexpansionary economic policies of the Tito era, including heavy reliance on foreign borrowing. The problems these policies precipitated were compounded by Yugoslavia's unique system of workers' self-management, which encourages inflation, prevents rational allocation of investment, and makes it difficult for the federal government to come to grips with the country's external financial problems. Political and economic decentralization led to an autarkic pattern of growth and redundancy in major investment projects. Moreover, regional and ethnic rivalries have led to serious political disagreements about the way to deal with the country's debt crisis. As a result, little progress has been made in building a consensus to correct the systemic causes of financial problems.

Rapid economic growth was the main goal in the 1970s of Tito's economic policy, which sought to minimize unemployment, improve living standards, narrow income differentials, and promote development of the poorer regions of the country. Rapid growth of domestic demand was accommodated by generally easy monetary and credit policies. In the 1970s, the money supply grew at an average annual rate of 29 percent and domestic credit by 24 percent, while real interest rates remained negative. Rapid growth of bank credit enabled enterprises to boost both investment and wages. For example, from 1970 to 1979, real gross fixed investment increased at an average annual rate of about 7 percent and its share in Yugoslavia's gross social product [1] reached a peak of 35 percent in 1978. Real private consumption expanded at an average annual rate of almost 6 percent. However, demand-led growth accelerated inflation and widened the trade deficit as imports were stimulated while potential exports were diverted to the domestic market.

[1] Gross social product differs from the gross national product measure of economic activity in that the nonmaterial component of services rendered to the population and to the government is excluded. According to Organization for Economic Cooperation and Development (OECD) measurements the social product is about 95 percent of the gross national product.

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Yugoslavia: Key Questions and Answers on the Debt Crisis

An Intelligence Assessment

Information available as of 18 January 1984 was used in this report.

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January 1984

Liberal dissidents and ethnic nationalists from non-Serb regions privately say they want to use the economic crisis as a tool for reforming the system and moving toward de-Titoization. But their highly diverse objectives—according to their own admissions—have blocked agreement on a common program. Moreover, because their political goals are "counter-revolutionary," they work under the serious threat of police suppression similar to that already applied in Kosovo and Croatia

There is a more cohesive group that the regime says wants a recentralized power structure committed to preservation of their prerogatives at all costs. This "firm hand" alternative draws most support from party hardliners and from the Serbs, Yugoslavia's largest ethnic group, who want to reverse decentralization because it has eroded their influence. This group enjoys a tactical advantage because they can cloak their centralist goals in Yugoslav patriotism. But they have lackluster leaders whose economic recentralization proposals run counter to non-Serbs' aspirations. Moreover, in our view, they offer no credible hope for economic recovery

How Much Success Has Belgrade Had in Dealing With the Debt Crisis and Stabilizing the Economy?
Yugoslavia has made some progress, but much remains to be done. The 1983 financial package, involving Western banks, 15 Western governments, the IMF, the World Bank, and the Bank for International Settlements, provided enough hard currency to meet last year's financial needs but not enough to allow a substantial rebuilding of reserves. Yugoslavia cut its current account deficit from $3.3 billion in 1979 to an estimated surplus of $125 million in 1983 (see figure 2), and this year it will also show a surplus. Although current account improvements are primarily the result of import cutbacks, Belgrade's policy of steady depreciation of the dinar has enabled Yugoslavia to increase exports by about 5 percent last year despite stagnating industrial output. The costs, however, have been high. The falling dinar has made it difficult for Belgrade to control rising inflation, which had accelerated to approximately 42 percent for 1983 and was rising at an annualized rate of 90 percent in December. Stabilization measures have slowed economic growth, boosted unemployment, and cut living standards (see figure 3).

What Is the IMF's Role in Yugoslavia?
IMF credits and support are crucial to Yugoslavia. From 1981 to 1983, a standby arrangement provided $1.8 billion in credits. In addition, the IMF has been active in encouraging Western banks to continue the flow of credits to Yugoslavia. Yugoslavia has started discussions with the IMF on a standby agreement for this year and counts on IMF help in arranging new financial assistance from commercial and government sources. Prospects for the 1984 agreement have been clouded by disagreements over interest rate levels and changes in the foreign exchange system.

In the first two years of the program, IMF conditions were not strict enough to bring about necessary adjustments in the economy. In 1983, the IMF stressed tighter monetary-credit targets, a policy of real effective exchange rate depreciation, interest rate hikes, price adjustments, and limits on public-sector revenue and spending. Even though Yugoslavia has met IMF performance criteria, the program has not dampened inflationary pressures. We believe the IMF should increase the effectiveness of its program by broadening its definition of net domestic assets to include interenterprise trade credits and the dinar value of foreign exchange deposits. It could also encourage Belgrade to liquidate insolvent firms, both to free financial resources for more efficient enterprises and to curtail demand for credit

Has Belgrade Made Any Changes in the Economic System To Correct Systemic Factors That Compounded the Current Crisis?
Not yet. In October 1981, Yugoslavia set up a blue ribbon panel, known as the Kraigher Commission, to study the country's economic problems and to develop a strategy for addressing them. The panel's recommendations, including a call for the introduction of more market forces, were endorsed by the Federal Assembly and the party hierarchy in July 1983. Parliamentary debate on specific measures began in fall 1983, but it was not until December that any legislation was passed. We believe, however, that the