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Yugoslavia: Prospects for Stability and Economic Recovery

An Intelligence Assessment

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~~August 1987~~

Yugoslavia: Prospects
for Stability and
Economic Recovery [REDACTED]

Scope Note

This paper assesses Yugoslavia's prospects for stability and economic recovery over the next few years. It expands on and updates the most recent assessment of the Yugoslav political system—DI Intelligence Assessment [REDACTED] May 1985, *Yugoslavia: Five Years After Tito*. Like that paper, this one concludes that Yugoslavia will face serious problems but remain fundamentally stable for the foreseeable future. However, this paper asserts that Yugoslavia's highly decentralized system is more durable than previously anticipated, and that decentralization serves US policy interests by promoting stability, encouraging political pluralism, and offering the best relative prospect for economic recovery and good relations with Western creditors. This paper will be followed by studies of Belgrade's economic relations with the USSR in the Gorbachev era and prospects for Soviet-Yugoslav relations [REDACTED]



Yugoslavia: Prospects
for Stability and
Economic Recovery [REDACTED]

Key Judgments

*Information available
as of 6 July 1987
was used in this report.*

Yugoslavia, in our view, is in the midst of a halting evolution—unprecedented in the Communist world—toward important elements of Western-style political pluralism and, in some regions, more liberal economic policies. We believe that continuation of this trend offers the best chance in the long run for Yugoslavia's internal stability and economic recovery. The country's current economic decline and fragmentation of political power, however, mean that continued evolution is not a foregone conclusion and that, under certain conditions, Yugoslavia might revert to greater authoritarianism or collapse into instability. [REDACTED]

The country's political course is the subject of major controversy among Yugoslavs who are hotly debating the system bequeathed by Tito. Virtually all agree that the current system, which grants the regions near-veto power over many national policies, is working poorly. Longstanding ethnic tensions persist, inflation and unemployment are at record highs, and powerful regional leaders are sharply divided over possible solutions. [REDACTED]

The core dispute for the next several years will be over how much power the central government and party should have in comparison with their regional counterparts. The debate comprises two intertwined dimensions:

- *Economic Centralization Versus Decentralization.* Many leaders—especially Premier Branko Mikulic and officials of the large, southern Republic of Serbia—argue that some centralization of economic policy making is essential in order to establish stronger market-oriented institutions necessary to rekindle economic growth. Others, generally from the wealthier northern regions of Slovenia and Croatia, and fast-developing Bosnia-Herzegovina, insist on retaining economic authority at the regional level. The latter argue—correctly, we believe—that recentralization would increase inefficiency and lessen Yugoslavia's economic potential.
- *Political Centralization Versus Decentralization.* The advocates of economic recentralization are waging a parallel battle to strengthen the central party apparatus and government. Northern leaders oppose these moves for fear of losing their political, economic, and cultural autonomy. Some, like Slovenia, believe recentralization would at a minimum end, and probably reverse, the process of political liberalization that has taken place in several regions since Tito's death. We believe they are probably right. [REDACTED]

The debate is inflamed and somewhat shadowy because the 'centralizers' rhetoric of reform cloaks their hidden agendas:

- Serbia would like to use recentralization to reestablish its dominance over a unified Yugoslavia.
- The poorer southern regions calculate that a more powerful center would help them gain additional northern economic support.
- Frustrated federal officials, such as Premier Mikulic, want to strengthen their power to force policies on the recalcitrant regions.

We believe the centralists will fail in their efforts to make major changes in Yugoslavia's political and economic systems in the near future unless they gain the pretext of more serious public unrest, which we consider possible but unlikely. Constitutionally, the regionalists have a virtual veto over most key issues and can block or dilute policies with which they disagree. For Yugoslavia in the near term this would mean:

- Policymaking in general will remain a slow, grinding, frustrating process of consensus seeking.
- The League of Communists of Yugoslavia (LCY) will be further eclipsed because government bodies and regional Communist parties will increasingly shape policy positions.
- The regime will probably be unable to implement a coherent economic reform program on a nationwide basis, although some regions will adopt more liberal economic policies.

The resulting near gridlock in Belgrade's macroeconomic policy presents the United States with the disquieting prospect that the central government at best will continue to move glacially in resolving the country's economic problems, including servicing its \$19 billion foreign debt. Nonetheless, the alternative—granting federal authorities greater power over the economy—would probably prove even more damaging.

The positive aspects of this political stalemate, we believe, are that, in the longer run, the Yugoslavs stand a good chance of managing their differences, coping with their economic morass, and evolving further from the Soviet model. At the same time, Yugoslavia most likely will experience a further modest, untidy evolution toward the political pluralism and region-by-region experimentation with more liberal economic policies advocated by the regionalist faction. Two other possibilities are that Yugoslavia will fall back toward some variant of stronger central control

and authoritarianism or lapse into increasingly open strife and chaos, possibly leading to real fragmentation. The second path is unlikely, in our view, and the third even less likely. [REDACTED]

We believe the most likely scenario—continued decentralization—offers the best chance for even a modest economic recovery:

- Most foreseeable economic advances will be thanks to the economically more dynamic advocates of decentralization—Slovenia, Croatia, and Bosnia-Herzegovina.
- Slovenia, and to a lesser extent Croatia, are the best available models to the other regions of the utility of more liberal economic policies. Given the lack of a real commitment to a market economy by the central authorities, emulation is the most plausible long-term hope for wider adoption of more liberal economic policies.
- The defenders of decentralization on balance can best constrain any premier tempted, as Mikulic has been, to abandon market-oriented measures in favor of state intervention. [REDACTED]

Decentralization also serves US strategic and political goals:

- It tends to promote political stability—a key US concern for decades—by allowing the many rival ethnic groups a reason not to question their coexistence as parts of one country and by keeping disgruntled workers divided enough to avoid national strikes.
- Regionalism will continue to promote elements of political pluralism. Lacking centrally mandated policy on ideological, cultural, and political reform, some regions—including Slovenia, Croatia, and Serbia—will continue to foster increased freedoms of speech and press as well as wider public participation in decisionmaking.
- Regionalism has tended to further strengthen Western-style institutions such as the federal government cabinet and the parliament at the expense of the LCY. [REDACTED]

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Moscow, for its part, probably will become increasingly concerned if, as we expect, the regionalists hold their ground. The Kremlin is already alarmed at the declining vigor and role of the national Yugoslav party and growing Western influence on Belgrade's economic policy making. Moscow probably will try to ensure its interests by closer economic ties, including concessionary trade arrangements, as well as cultivation of ties to individual regions and private criticism [REDACTED]

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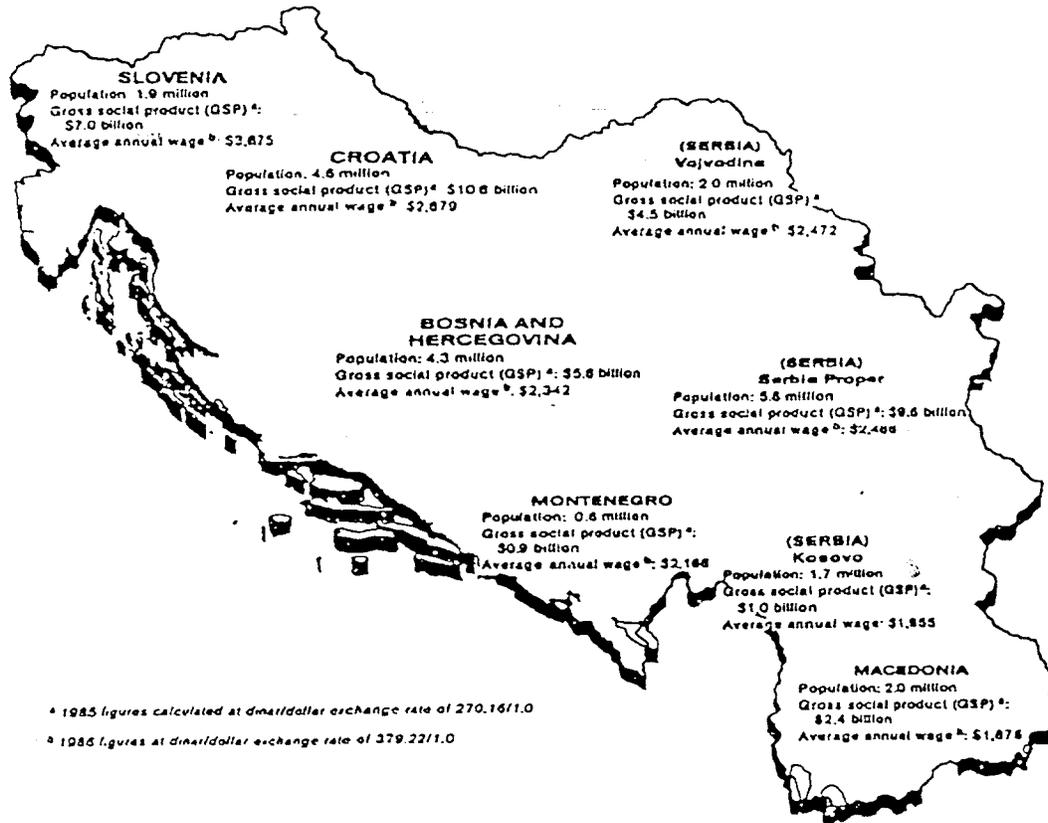
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Yugoslavia's Regions



* 1985 figures calculated at dinardollar exchange rate of 270.16/1.0

* 1986 figures at dinardollar exchange rate of 379.22/1.0

Source: Federal Statistic Institute

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Yugoslavia: Prospects for Stability and Economic Recovery

Introduction: Debating the Post-Tito System

Yugoslavia is in the throes of a wrenching debate focusing on proposals to modify its unique Communist system. Many of the proposals are advertised as "reforms," but the core issue, in our view, is the perennial Yugoslav question of how much authority the central government and Communist Party (the League of Communists of Yugoslavia, or LCY) should exercise over the eight ethnically diverse and highly autonomous regions. The outcome of this debate will determine which regions will make gains at the expense of others, and ultimately whether Yugoslavia will become a tighter or looser federation, or possibly even break apart.

The debate is the latest reassessment of the system in line with those following the break with Stalin in 1948 and the downfall of Security Chief Alexander Rankovic in 1966. This one is fueled by three overlapping problems:

- The decentralized political system has hobbled national policymaking.
- Tensions between the rival ethnic groups persist, and in some cases are growing.
- Despite some modest success at economic stabilization, inflation is more than 100 percent a year, the foreign debt is \$19 billion, strikes are taking place in record numbers, and the unemployment rate of 14 percent is one of the highest in Europe.

This debate, like those before it, could lead to changes in the country's political and economic course that would affect US and Soviet interests. A serious aggravation of political, economic, or ethnic tensions—an ever-present possibility—could lead to increased authoritarianism, state economic intervention, or even self-destructive internal conflict. Overall, however, we believe the Yugoslavs stand a good

chance of managing their differences, coping with their economic morass, and evolving even further away from the Soviet model.

The debate over the system's evolution and degree of centralization has pitted two loosely knit groups of leaders against each other. The main proponents of decentralization—the "regionalists"—are leaders from the more industrialized, prosperous northern Republics of Slovenia and Croatia, and from fast-developing Bosnia-Herzegovina. The main proponents of centralization include:

- The leadership of the large, southern Republic of Serbia.
- The Premier for the next three years, Branko Mikulic.
- The federal bureaucracy and the Army, which are heavily staffed by Serbs.
- Leaders of the three underdeveloped regions in southern Yugoslavia: Serbia's autonomous Province of Kosovo, and the Republics of Macedonia and Montenegro.

The Centralists' Motives

The centralists assert that stronger federal authority over economic matters is essential to implement fundamental, market-oriented reforms. They maintain—correctly, we believe—that regional autonomy has produced economic distortions and inefficiencies by preventing the development of national capital, labor, and product markets. These officials argue that:

- Federal authorities must break the power of regional leaders, who are resisting market measures that would weaken their power, before systemic economic reform can produce integrated national markets.
- The regions now simply refuse to implement federal legislation, and the federation lacks the power to force implementation.

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- Even Western governments exert macroeconomic control through fiscal and monetary authority now lacking in Belgrade.

We believe each of these arguments has merit but that the centralists all have hidden agendas beyond economic reform that suggest successful recentralization would be damaging to the economy.

Serbian Leaders

Serbia's leadership argues that its goal is to strengthen the unity of the country against centrifugal forces threatening to tear it apart. We believe, however, that it is trying to use the reform debate to reestablish the dominance over the federation that Serbia exercised between the two world wars. Even if the Serbians had no ulterior motives, other Yugoslavs would still distrust their plans because of longstanding fears of Serbian ethnic nationalism—an impression the republic leadership has done little to overcome:

- Serbia wants greater political centralization in order to gain greater power for itself, most immediately to reallocate economic wealth produced by the northern regions.
- Its professed commitment to market-oriented reform is particularly suspect because the republic has failed to implement the economic reforms it preaches.

Serbs and other Yugoslavs have good reason to equate greater centralization and power for Belgrade with increased Serbian influence:

- Belgrade is the Serbian as well as the national capital.
- Serbs dominate the federal bureaucracy and they have disproportionate influence in the national Army.

Southern Fellow Travelers

The southern regions—Macedonia, Montenegro, and, to a lesser extent, Kosovo—support the centralists largely for economic reasons. Even more than the Serbians, southern leaders want a stronger federal government because they anticipate that it would shift more resources from the wealthier north to them.

Southern press commentaries, for example, complain that northern regions now delay or neglect mandatory aid payments to

poorer regions because of weak federal oversight. Backward, debt-ridden Macedonia and Montenegro are the most supportive. Serbia's autonomous Province of Kosovo, the nation's poorest region, favors greater economic authority because it also anticipates benefiting from this broader redistribution. Kosovo's support is muted, however, because its largely ethnic-Albanian leadership is even more concerned to block continuing Serbian efforts to reassert control over Kosovo. We believe that all three of these southern regions oppose real market reform because it would force painful restructurings of their highly subsidized economies.

Federal Officials

Federal officials, to the extent they are independent of the regional governments that appoint them, favor recentralization out of frustration over their inability to implement policies that they believe are needed to draw Yugoslavia out of its economic morass. Some probably believe a stronger federal government would move the country toward a more market-based system. But most are simply tired of being blamed for the economy's troubles with no prospect of putting recovery plans into effect. Federal officials who genuinely favor market reform probably believe that, if the central government had greater power, it would implement some reforms, notwithstanding the goals of those who want only greater power for Serbia or economic redistribution.

The nonreformers appear to hold most of the levers of power. Premier Mikulic—in power since May 1986 and now the dominant national official—comes from Bosnia-Herzegovina, a region whose leadership has long resisted surrendering control over the economy to the market. Since taking office, he has all but abandoned market-oriented policies in favor of central administrative measures, which he usually presents as emergency stopgaps. Regional resistance to and circumvention of these policies appears to have only increased his desire to expand central authority. In recent speeches, Mikulic has even hinted at the need to remove local officials for refusing to implement his government's policies.

The Pluralistic Post-Tito System

The system that is now so hotly debated was introduced in stages by Tito before his death in 1980. While this system has continued to evolve and become more pluralistic during the past seven years, it has kept almost all its basic features, including:

- **Collective Leadership.** To keep the country stable, Tito chose to introduce collective leadership bodies rather than risk appointing a single successor, who probably would have been unacceptable to some faction or ethnic group. These collective bodies are composed of representatives of each of the eight regions, generally according to a strict formula. The nine-man State Presidency includes an official from each region plus the LCY chief. The 23-member Party Presidium and the 165-member Central Committee also allot seats proportionally and include designated positions for the military. The state and party chiefs rotate annually. By contrast, the government head (premier) in practice is chosen by the State Presidency and serves a four-year term, while seats on the cabinet are chosen by a less rigid nationality formula.
- **Consensual Decisionmaking.** Unanimous agreement of the eight regions is needed in the national assembly to adopt any laws affecting regional prerogatives. Other national leadership bodies that do not require consensus—such as the Communist Party Central Committee and Presidium—often use it in practice, thus giving each region a virtual veto over national policy.
- **Indirect Party Rule.** In breaking from the Stalinist model, Tito ended direct party control over governmental policies. While the LCY is still the only constitutionally recognized political party, it provides general policy guidance and intervenes only occasionally on specific issues—for instance, when government bodies have become gridlocked. Party bodies play a more assertive role in some regions, however, particularly Montenegro and Bosnia.
- **Regional Sovereignty.** Tito devolved considerable power to the regions during his lifetime, a trend that continued after his death. Under the last constitution, approved in 1974, the regions have ultimate authority over matters such as education, cultural policy, and enforcement of most federal laws.
- **Mixed Economy.** Tito also transformed the Stalinist command economy into a hybrid, combining elements of market forces and state intervention. His main innovation was introducing "workers' self-management socialism," by which workers legally have decisionmaking authority over their enterprises. In practice, however, regional and local officials continue to wield strong influence over business decisions.
- **Nonalignment.** Tito left his heirs a foreign policy of nonalignment, his main justification for independence from the Soviet Bloc. Most Yugoslavs support this position, even if they disagree on many aspects of domestic policy.

The national Army and nine-member State Presidency, in our view, support the government's efforts to increase its authority. The Army, heavily staffed by Serbs, has long feared that decentralization would lead to increased disunity. The Presidency contains some of the country's remaining old-line leaders in the Titoist mold; most have a weak regional power base and a Pan-Yugoslav orientation. [REDACTED]

The Regionalists' Motives

The regionalists are divided over the need to introduce real market reforms, but they all favor the status quo over increasing Belgrade's authority. They argue that:

- Their own regions have proved economically successful by Yugoslav standards because they have been relatively free from federal control.
- Economic reform can only be introduced from the bottom up, not through political interference from the center.
- The Serbian program ultimately would steer the economy back to a tightly controlled command model. [REDACTED]

The regionalists also have a veiled agenda, albeit one more openly stated than that of the centralists: they want to protect the relative success of their republics' economies from federally managed raids on their coffers. Beyond this one unifying theme, the northern regions do not share a common agenda, but rather are highly divergent socially and politically. Like most political allies in Yugoslavia, they cooperate as a loose, issue-oriented coalition rather than a permanent political bloc. [REDACTED]

Slovenia: Internal Reform Without Federal Control

The Slovenes, Yugoslavia's most economically advanced ethnic group, appear genuinely committed to experimenting with liberal economic policies. They view federal power as a roadblock and the centralists' argument as a throwback to a command economy. They argue that economic incentives—not federal controls—should direct the economy. They have gone further than the rest of the federation in giving free rein to market forces and private enterprise, and their foreign trade is oriented heavily to the West. [REDACTED]

Yugoslavia's Economic Powerhouses

The Republics of Slovenia, Croatia, and Bosnia-Herzegovina wield considerable economic clout that adds to their already strong political influence:

- They generate most of the country's critical hard currency earnings. In 1985, the last year for which we have figures, nine of Yugoslavia's 10 leading exporters were enterprises located in these republics. Last year, Bosnia also led the country in export growth, with a 13-percent increase compared with a national average of about 3 percent.
- Slovenia and Croatia account for 43 percent of national output while having only 29 percent of the population. The figures for Bosnia are 13 percent and 18 percent, respectively.
- Each republic dominates a critical economic sector. Bosnia contains most of the country's defense industries. Slovenia leads in high-tech industries such as electronics and communications. Croatia is the main player in the petroleum industry and tourism, the most important domestic source of net hard currency earnings. [REDACTED]

Slovenes also believe that greater federal authority would stifle their Western-oriented culture. For centuries, Slovenia was part of the Austrian Empire, where its evolution more closely paralleled Catholic Central Europe than the Ottoman-dominated Balkans. Even today, Slovenia's ethnic homogeneity, distinctive language, and strong cultural identity continue to nurture political unity and isolationism in the face of the country's Serbo-Croatian-speaking majority. [REDACTED]

This isolation has helped Slovene leaders expand the usual bounds of acceptable Yugoslav Communist behavior. Slovenia has the country's best human rights record and freest cultural climate, which it sometimes flaunts to the dismay of more orthodox Yugoslavs and the military:

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- Slovenia tolerates, and at times encourages, an almost Western degree of public discussion and press freedom. Unlike elsewhere in Yugoslavia, the regional authorities jail virtually no citizens for antiregime political statements.
- It has allowed large public gatherings by a youthful, iconoclastic Greens-style "Alternative Movement" against nuclear power, compulsory military service, and the training of foreign military students.
- It promotes a role in the political system by groups not under the direct control of the local Communist Party, such as the business community, the regional legislature, and the regional "front" organization (the Socialist Alliance of Working People), which includes a wide spectrum of non-Communists, clergy, and special interest groups.

Croatia: Following the Slovene Road

Croatian views on central authority increasingly parallel those of the Slovenes because of growing similarities between the two regions' economic and political interests. Perhaps even more than the Slovenes, historically Catholic Croats have their own cultural distrust and fear of Eastern Orthodox Serbia and Belgrade—Serbs and Croats killed each other by the thousands in a grisly civil war conducted during the World War II resistance to the Germans.

In a major turnover in leadership last year, a "young Turk" grouping largely replaced a band of conservative officials who had run the republic since the 1971 liberal-nationalist disorders. This new leadership is now publicly committed to cautious implementation of a Slovene-style, more liberal economic program. Like the Slovenes, it too views federal authority as a roadblock and is exploiting decentralization to liberalize the political environment, albeit more slowly than in Slovenia:

- The republic has led the country in experimenting with democratic procedures, such as requiring secret balloting and multiple candidates in both government and party elections.
- The press and radio have become somewhat more open.

- Dissidents are receiving milder treatment. A Zagreb court this year handed down only a suspended sentence on Dobroslav Paraga, an outspoken critic of prison conditions.

Croatian leaders probably also are resisting federal economic authority because they fear Belgrade would lack Zagreb's cautious approach to closing Croatia's many unprofitable firms. Despite Croatia's being the second-wealthiest region per capita (behind Slovenia), it is saddled with many "white elephants" in sectors such as petrochemicals, metalworking, power generation, food, and chemicals. The newly installed Croatian leaders favor more rational economic practices, but they also want to retain control over any economic restructuring, and cushion the resultant joblessness and threats to their key political constituencies. Officials say, for example, they are prepared to face the problem of 10,000 to 15,000 workers who will be fired in the first round of plant closings under new bankruptcy legislation. At the same time, however, they want to try to move workers to areas in the republic now experiencing labor shortages.

**Bosnia: Centralism,
But at Republic Level**

Senior Bosnians have little sympathy for liberal economic policies, but they fear federal authority over their republic's tightly controlled economy. They believe planning and control by the republic leadership is the best tool for economic development, according to many sources, and that the republic's economic priorities should take precedence over those of the federation. At the same time, in recent years they have allowed relatively extensive small-scale private enterprise.

Bosnian leaders also apparently favor the concentration of power in the republic because they believe their cliquish control has kept Bosnia stable. In contrast to all the other regions, none of Bosnia's ethnic groups (Croats, Serbs, and the officially recognized "Muslim" nationality) constitutes a majority.

Bosnian leaders are so concerned to control latent ethnic tensions that they mete out some of the country's harshest punishments for even mild displays of nationalism or antiregime sentiment:

- Yugoslav media report sentences of several years' imprisonment for outspoken religious leaders and dissidents.
- Prominent dissident Milovan Djilas recently called Bosnia an exception to the country's generally improving human rights climate.

Notwithstanding their differences with Mikulic, Bosnians are loath to criticize him publicly because of his local roots [REDACTED]

Likely Battlegrounds

The centralists and regionalists will continue over the next several years to sharply debate a half dozen or more key national issues bearing on centralization versus decentralization. In the economic arena, they will argue about the appropriate degree of federal control over foreign exchange, pricing, and tax policy. Politically, they will debate whether to return to the national government and LCY some of the power that has devolved to the regions since the late 1960s. How the game is played and the outcome of these debates will determine the degree of Yugoslavia's stability, the balance of forces between Belgrade and the regions, and the prospects for further political liberalization and the introduction of more market-oriented reforms [REDACTED]

Economic "Reform"

Yugoslavs have grown increasingly gloomy about their country's economic prospects since the early 1980s, when an era of fast growth and improving living standards fueled by foreign borrowing ended abruptly. In 1983, with Western support and prodding, Belgrade adopted an economic stabilization program that calls for greater use of incentives, real interest rates, and profitability. But, like earlier attempts at economic liberalization, this latest program has been only partly implemented, owing to regional autarky and federal officials suspicious of market measures [REDACTED]

Following are some of the main economic issues that will most likely be debated during the next few years. On most issues, the centralists are promoting stopgap, administrative fixes, not the market-oriented reforms needed to restructure the economy and promote an export-led recovery. The regionalists are trying to block or water down measures that would strengthen federal control over economic activity in their republics [REDACTED]

Control Over Foreign Exchange. Yugoslavia's system for apportioning foreign exchange is likely to resurface as a politically hot issue, thanks in part to misconceived "reforms" pushed through by centralists nearly two years ago. The distribution of hard currency is a longstanding controversy between northern regionalists and southern centralists. The northerly exporting regions jealously guard access to hard currency, while the southerners believe it should be more evenly distributed. In 1971 Croatian nationalists took to the streets partly to protest central controls over the republic's foreign exchange earnings. [REDACTED]

The issue reappeared in 1984-85 when the federation, led by Serbia and its southern allies, sought to require firms to turn over their foreign exchange earnings to the central authorities. Exporters up to then could keep roughly half of their hard currency earnings. In late 1985 the federal government took control over all foreign exchange earned by Yugoslav firms, despite vigorous opposition in parliament and the party from the northern republics [REDACTED]

The southern regions and centralists may have won a Pyrrhic victory. The system, at least initially, has depressed exports by weakening incentives for the major hard currency earners in the north while failing to generate enough hard currency to help the poorer south:

- [REDACTED] Slovenia and Croatia continue to criticize the new laws.

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- The southerners have maintained a public silence, but debate between the regions probably is going on behind the scenes and may intensify.
- Premier Mikulic last year said the government would consider unspecified changes if necessary.

the foreign exchange system remains potentially the most disruptive issue facing the leadership because of deep polarization and a belief among many actors that unusual risk taking is justified.

National Price Controls. Conflict over federal price policies will probably sharpen if, as we expect, Mikulic continues to broaden national controls in a desperate effort to stem inflation. The government has steadily expanded its power over prices during the past year by moving more products and product types into controlled categories, extending the time they are controlled, and lengthening notification periods required for price rises.

Slovene and Croatian officials have publicly criticized Mikulic for his price policies. They charge that such controls distort the market and promote greater inflation. But their concern in part also reflects a fear that Belgrade—rather than the republic capitals—is determining the solvency of local enterprises. Bosnian officials in recent years have indicated that they oppose federal price authority almost exclusively for this reason.

The southern regions, by contrast, support Mikulic's moves to aggressively control prices. Faced with record-level business losses in their economies, southern leaders hope federal price controls will brake a decline in living standards and ease pressure for wage increases. They probably also fear that unrestrained price rises work to the advantage of northern industries, which have more influence on the market than those in the south.

Federal Tax Authority. Federal moves to standardize and centralize the tax system are also galvanizing regionalist resistance. The national government earlier this year gained a greater share of the sales tax

collected: 75 percent, as compared with 50 percent previously. Serbia is now agitating for even greater federal tax authority at the expense of the regions.

The Slovene assembly last November charged that the federation was attempting to exceed its constitutional authority, while the leading Slovene newspaper *Delo* has said that the republic must hold onto this key source of revenues in order to keep Belgrade dependent on regional funds. Croatian officials similarly have advocated better regional coordination rather than increased federal authority. Bosnia also seems to be dragging its feet; at a Bosnian party plenum last fall only the federal party representative supported giving Belgrade greater tax authority.

Political "Reform"

Debate probably will also sharpen in the next several years over political "reform," especially since many centralists argue that greater central political authority is needed to overcome economic problems. The centralists' targets will most likely continue to be the key documents regulating political authority in the federation—the Constitution, the LCY's statutes, and the Associated Labor Law that governs Yugoslavia's unique "workers' self-management" system of decentralized economic decision making.

Changing the Constitution. The centralists will continue their efforts to change the 1974 Constitution, the last of four put forth under Tito, because it allows each of the eight regions political rights that make strong central control legally impossible. centralists have already proposed amendments that would greatly restrict the effective veto on federal policy that each region now holds in the Assembly. They also have proposed creating a new assembly house, with delegates controlled by enterprises rather than by regions. They show no signs of giving up their efforts despite numerous setbacks in the last two years.

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Leaders from the northern republics are against these changes because of the loss of power they consequently would suffer. They have publicly rejected any but decorative amendments. [REDACTED] the amendments will be debated, as required by the Constitution, in the federal and regional assemblies over the next year and a half [REDACTED]

Reducing Workers' Rights. Another key proposal that will probably spark northern resistance is the federal government's continuing attempt to alter Yugoslavia's unique "workers' self-management" system. Instituted after the break with Stalin in 1948 and enshrined by Tito's theorist Kardelj in the lengthy Associated Labor Law of 1976, self-management gives workers the right, in theory at least, to make virtually all decisions in their enterprises. In practice, workers have more participation than in the Soviet Bloc but less than the law provides, as plant managers and local politicians continue to make most key decisions. [REDACTED]

Mikulic, publicly backed by Serbia, has proposed amendments to the labor law that would reduce the independence of enterprises on matters such as wage policy. Both Mikulic and Serbia undoubtedly seek to use such changes to narrow the authority of local officials. [REDACTED]

The northern republics strongly oppose changes that would increase federal administrative authority over enterprises:

- [REDACTED] opposition to major changes is widespread in Slovenia and Croatia.
- Bosnia has maintained a public silence on the issue, signaling to Mikulic that he lacks the republic's support. [REDACTED] even Serbia's traditional southern allies are uncomfortable with major changes in the self-management system, partly on ideological grounds. [REDACTED]

Restoring Central Party Authority. Conflict over the party statutes is likely to flare as the next party congress, set for 1990, nears. Centralists probably will contend that the federal party must be given greater means to require regional parties to comply with agreed positions and directives. Their concerns may

grow because the national party apparatus, since the last congress in June 1986, has been as weak and ineffectual as at any time in recent years. [REDACTED]

The dispute could be complex and heated if debate before the last congress is any guide. In that instance, Serbia spearheaded a drive to recentralize authority by means such as transferring selection of Central Committee members from the regions to the national party congress. The northern regions then publicly defended regional party autonomy and threw the party into a convoluted theoretical debate. While the northerners agreed to modest statutory changes, including a watered-down version of the proposal to elect Central Committee members, they succeeded in retaining broad regional party autonomy, and the centralists have been unable to exploit the few gains they made. [REDACTED]

Prospects

We believe that stalemate over most major issues will continue for the near term. Over the longer run, however, Yugoslavia is likely to continue its halting evolution toward Western political and economic norms. We believe a return to authoritarianism or growing systemic instability are possible, but less likely, alternatives. [REDACTED]

The regionalists for now probably will be able to stalemate the centralists on virtually all the above issues by resorting to their unit veto on decisionmaking. Those measures that they do allow will be diluted of consequence, with several short-term implications:

- Policymaking will remain a slow, grinding process of consensus seeking that will frustrate many Yugoslavs eager for solutions. Centralists will continue to exploit this frustration to push their agenda, and the debate will ebb and flow.
- The LCY, as a coherent national institution, will continue its slide into the background while government bodies and regional Communist parties shape

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key policies. This will make nationwide policy implementation more difficult but promote greater openness and elements of pluralism.

- The regime will be unable to implement a coherent economic reform program on a nationwide basis, even in the unlikely event that the Mikulic government shifts to more market-oriented policies. Some regions, however, will continue to experiment with more liberal economic policies.

Our judgment on longer run developments is made with the near certainty that Belgrade will face years of economic problems, tenuous foreign liquidity, labor discontent, ethnic hostilities, and periodic human rights abuses. Moscow, moreover, will find ample opportunity to meddle while it remains anxious about the outcome for its interests in the Yugoslav course.

Pluralist Evolution—The Most Likely Course

We believe Yugoslavia is most likely to continue to develop modest elements of a Western-style pluralist political system while moving haltingly and on an ad hoc, region-by-region basis toward greater economic liberalization. This prognosis assumes that:

- The regionalists continue to stave off the broad thrust of centralist advances, even if they give ground on some issues.
- The economy muddles along but does not precipitately deteriorate.
- Ethnic tensions, labor unrest, and regional conflict continue, but at containable levels.

Under this scenario, we would expect the three regionalist-minded Republics of Slovenia, Croatia, and Bosnia to continue their relative economic progress vis-a-vis the other regions and prevent an even more serious slide in the national economy and external financial picture. A growing disparity in per capita income between north and south will probably add to political tensions, but northern leaders probably will continue to be willing to ease the problem through moderate economic aid through the existing national program.

We believe Slovenia, and to some extent Croatia, will also continue to experiment with more liberal economic policies. In the absence of federal-level support for real national reforms, they will serve as the best available role models to other regions. Officials in Macedonia and Montenegro, for instance, already are tentatively following the Slovene example by easing legal restrictions on private enterprise in a desperate bid to reduce unemployment and increase output. But any process of emulation will probably be slow, and Serbia and the southern regions will see the north more as "an ox to gore" than as a model.

On the political side, too, regionalism will probably promote at least a spotty evolution toward greater pluralism, openness, and individual freedoms. In the absence of centrally mandated ideological, cultural, and other policies, some regions—including Slovenia, Croatia, and even centralist-minded Serbia—probably will further improve their human rights records and continue to liberalize their political systems. We believe that moderately strong economic ties to Moscow have not and probably will not substantially affect this trend. Gorbachev's emphasis on *glasnost*, if anything, will make moderates feel even less constrained in promoting further democratization.

Nationally, we expect the parliament and government to become stronger at the expense of the LCY, even if a nominally one-party state remains in place for years to come. Debate over national issues probably will further expand to include more previously taboo topics, including sensitive foreign policy issues. The premier, with his four-year term, is likely to further emerge as the most identifiable and influential national leader—a break with the practice of the Tito era and of almost all other Communist states.

Decentralization will be accompanied by many signs of conflict—such as strikes and public protests—but they will represent more a venting of political and economic demands than genuine threats to the system. Decentralization is more likely to contain such shocks than recentralization, which would tend to

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encourage dramatic outbreaks by discontented factions. [redacted] the mutual deterrence built into Yugoslavia's system contributes strongly to stability. While sporadic repressions and abuses remain likely on the local level, decentralization will present ideologues with major hurdles should they try to impose crackdowns on human rights or reimpose Communist orthodoxy. [redacted]

Implications for the United States. This scenario entails costs for the United States, but on balance the benefits seem more significant. On the negative side, slow, uneven progress with economic reforms promises more demands for greater Western financial support by Yugoslavia. We believe these problems would persist under any realistic alternative, however. [redacted]

On the positive side, further Yugoslav decentralization probably offers the best long-term chance to promote US interests, both political and economic:

- In our view, such an evolution represents Belgrade's only plausible path to improved economic performance. The centralists' path offers little hope because their hidden agendas promise an end to progress toward market reform should they triumph. Moreover, return to a centrally planned economy—even one modeled on the relatively successful East German system—would probably be unworkable given Yugoslavia's societal diversity, firmly established political decentralization, and the absence in most regions of a work ethic like that in East Germany (a key difference between East Germany and the less successful majority of Bloc countries).
- Decentralization serves the longstanding key US interest in promoting political stability by localizing discontent, granting maximum self-rule to hostile ethnic groups, and not allowing the domination of one major ethnic group by another.
- The growth in political pluralism—including more open acceptance of competing interest groups, broader political participation, and expansion of individual liberties—further differentiates Yugoslavia from the Warsaw Pact countries and strengthens its ideological orientation toward the West. [redacted]

Concerns Ahead for Moscow. Moscow probably will become even more concerned than it is now if, as we expect, the regionalists hold their ground. Moscow believes it stands to lose considerably more than it could gain from even a halting Yugoslav evolution toward Western norms. [redacted] the Soviet leadership is highly critical of the declining vigor and role of the national Yugoslav party and heightened Western influence in Belgrade's economic policy making:

- Soviet chief Gorbachev last December privately attacked visiting Yugoslav party head Milanko Renovica over Belgrade's internal policies. [redacted] Gorbachev asserted that Yugoslavia's system is a failure and the party's laxity is to blame.
- Soviet media continually stress the need for greater Yugoslav party unity and insinuate that Belgrade has become too dependent on the West. [redacted]

Moscow's ability to influence Yugoslavia's course is limited, however:

- Most Yugoslav leaders, including the most ideologically orthodox, distrust Soviet motives.
- The fragmented political system complicates Soviet efforts to recruit pivotal clandestine agents of influence in Belgrade.
- The Yugoslavs devote considerable effort to monitoring Soviet activities in Yugoslavia. [redacted]

Moscow probably will rely increasingly on its already close economic relations with Belgrade in pursuing its interests, and may have some success given Yugoslavia's weak economic prospects. For example, despite continuing disagreements over trade terms, Moscow will most likely continue to accept Yugoslav goods below Western standards in exchange for petroleum and other raw materials to demonstrate it is a cooperative economic partner at a time when Belgrade is having problems with Western creditors. The Soviets, meanwhile, will continue to press the Yugoslavs to purchase manufactured goods and military hardware to increase the economic linkage. [redacted]

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Politically, the Soviets will also play on the knowledge that Belgrade believes a good relationship with the USSR—or at least not overly antagonizing Moscow—is critical to Yugoslav security interests. Moscow probably will increase current efforts to co-opt regional power brokers by cultivating formal ties between Soviet and Yugoslav regions. Moscow could even exploit regional developmental differences by granting greater economic concessions to the poorer south and by cultivating Serbia and Montenegro in particular. Meanwhile, the Soviets will continue their tradition of tough talk with senior Yugoslav officials during bilateral exchanges.

A Possible Alternative—Return to Authoritarianism

A temporary or even long-term return to some variant of increased centralism and authoritarianism is plausible, but only under some combination of the following conditions, which we believe is unlikely:

- Major labor or ethnic violence strengthens the hand of centralist-minded party hardliners, backed by the Army and internal security services.
- The economy (particularly production and living standards) precipitately worsens and the population and regional elite react by demanding tough federal measures. The Serbian camp could exploit a rapid decline to try to convince the regionalists it is serious about market reform and win support for at least temporary recentralization.
- Over the long run, continued problems begin to generate a national consensus that more central control of the economy is the only solution. Gorbachev could reinforce the trend should he succeed in revitalizing the Soviet system and thereby strengthen the legitimacy of more traditional Communist economic policies in the eyes of many Yugoslavs.

In this scenario, regional leaders would agree, or be forced, to give up some sovereignty to prevent wider unrest and keep other elements of the Yugoslav system intact. At a minimum, the federal government would seek to impose interventionist measures, possibly by invoking special constitutional provisions to

override minority factions in parliament.¹ In an extreme situation, the nine-man State Presidency could exercise its authority to impose some form of martial law. In either case, we would expect little real movement toward economic recovery while such measures were in effect because recentralization would leave the country's underlying economic problems—above all, market inefficiencies—unresolved. Moreover, we believe the Yugoslav system over time would most likely revert once again to more open debate and factionalism, as it did following periods of tightened controls imposed by Tito.

Under this scenario, the United States would witness at least a temporary halt to Yugoslavia's progress toward democratic forms. As in some past crack-downs—following the Croatian upheavals in 1971, for example—Belgrade would perceive US and other Western criticism of such action as an attack on its national security. The West probably would have little choice but to wait out the crisis and hope for an eventual "normalization."

Moscow would stand to gain some ground under this scenario, particularly if Belgrade could prevent widespread civil unrest. Moscow probably would welcome a more centralized regime with tighter government control over the economy as a demonstration that a highly decentralized Communist regime is a contradiction in terms. In contrast with probable Western displeasure, the Soviets would view developments in Yugoslavia as vindicating the correctness of a Soviet-style regime and economy for other Communist states and would most likely offer public support to Belgrade. The Soviets probably would take advantage of a confrontation between Belgrade and Western creditors over extensive backsliding on economic reform, possibly by offering new favorable trade terms, and by seeking to tie Yugoslavia closer to the USSR economically.

¹ Article 136 of the Federal Constitution allows the cabinet, in consultation with the State Presidency, to impose legislation temporarily by decree in the event of an impasse with regional representatives in parliament.

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Least Likely Scenario—Serious Systemic Instability
The least likely scenario, in our view, is that the growing debate in Yugoslavia ultimately will pull the federation apart. We believe that only a combination of several of the following highly improbable developments would push Yugoslavia toward such chaos:

- The Army leadership, traditionally united in the face of unrest or antiregime activity, fragments along ethnic lines and refuses to back the national political leadership in keeping restive workers or ethnic groups in check.
- Leaders in several regions, such as Slovenia or Kosovo, go well beyond their current levels of assertiveness and demand secession, or at least the formal creation of a confederation system.
- Antiregime protest expands and forms links across regional lines.
- A global economic downturn or domestic economic mismanagement creates such widespread shortages and disruptions that a coalition of Army generals, federal bureaucrats, regional leaders, and the populace attempt to overthrow the leadership.
- Ethnic confrontation flares between Slavic groups—rather than between Slavs and Albanians, as is now the rule—and national leaders side with their own ethnic group rather than defend Yugoslav unity.

US interests would suffer the most under a scenario of collapse. Washington would have little influence on the key actors—regional leaders, the Army command, the internal security services, and party hardliners. Moderate leaders would lose influence or be purged in a successful imposition of order by the military and security services, and human rights would probably be widely abused. At the same time, a debt moratorium probably would be declared and new Western aid would be sought to get the country moving again. In the worst case—widespread social disorders, civil war, or even the country's actual breakup—Washington could face Moscow in a confrontation as the two sides struggle to exert influence and protect their interests.

Systemic collapse would threaten Moscow's interests as well. The Soviets would be at least as concerned as the West about losing influence in Yugoslavia and would try to use whatever levers it had to gain what it could. The Soviets would be deeply concerned that they could lose their remaining influence and that turmoil could spill over into neighboring Warsaw Pact countries. The Soviets probably would try to influence the Yugoslav Army and security forces by publicly backing the imposition of tough measures aimed at reimposing order. Failing that, Moscow would probably try to formalize links to several regional leaderships to advance its interests among the federation's remnants.