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Yugoslavia: A Year Without Tito [redacted]

An Intelligence Assessment

Information available as of 7 April 1981
has been used in the preparation of this report.

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April 1981

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Yugoslavia: A Year Without Tito [redacted]

Key Judgments

The year-old leadership is demonstrating that it can maintain Yugoslavia's unique brand of socialism and govern without Tito's guiding hand. Despite adjustments and inevitable problems since his death last May, the party and state succession machinery has functioned smoothly. [redacted]

Much of the leadership's attention has focused on the troubled economy. Stabilization measures in 1980 reduced the trade deficit and slowed the growth of domestic demand. Belgrade also secured financing from the IMF and Western governments and banks despite some initial difficulty. The improvement in the balance of payments and IMF endorsement of the stabilization program will increase the confidence of foreign lenders and make it easier for Yugoslavia to borrow in 1981. [redacted]

The collective leadership, nonetheless, still has to fight high inflation. Other economic problems persist: low productivity, stagnating living standards, and unemployment. Weaknesses in an economy based on self-management and decentralization impede both efficiency and policymaking. Failure to make progress on these problems could have political repercussions. The leadership is stressing the need for a long-term commitment to austerity and is allowing more open discussion of the causes and cures for Yugoslavia's economic ills. [redacted]

Tito's heirs face potentially serious political problems as well:

- Continuing nationalism in the country's six constituent republics and two regions, particularly among the large Albanian minority in Kosovo Province.
- Indications that the Serbs may press for disproportionate authority at the federal level and thus upset the sensitive nationality balance in the party and state machinery.
- Growing signs of assertiveness by the intellectuals. [redacted]

These centrifugal forces and domestic rumblings are endemic to the Yugoslav system, but the members of the collective leadership have been willing to compromise regional and personal interests for the good of the federation as a whole. The compromises have weakened policy initiatives, however, especially in the economic area. And policies decided at the federal level have been difficult to carry out in the republics. Nevertheless, any perceived external threat to Yugoslav independence would tend to silence the centrifugal impulses and unite the nation. [redacted]

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Doubts About the Future

When Josip Broz Tito died last year, both the political and the economic viability of Yugoslavia were in doubt because the country had so long depended on his leadership to develop effective policies at the federal level. [redacted]

Despite Tito's strenuous efforts, deep-rooted nationality rivalries prevented the development of a Yugoslav national consciousness. Indeed, the struggle of non-Serbs against Serbian dominance, which is at the heart of the problem, was barely controlled, even under Tito's dominant leadership. The strong rivalries among Yugoslav nationalities led Tito to fashion a decentralized political system made up of competing, sometimes antagonistic, regional parties. The collegial executive system introduced in the fall of 1978 was in large measure an attempt to bridge the gap separating these disparate interest groups and to ensure that each had a voice in federal affairs. So that each would get a turn at running the federal party and the state bureaucracy, party and government leaders—at all levels—were organized into committees whose executives held office for one year. [redacted]

In economic policy, rapid growth had long been the overriding goal. The competing regional interests encouraged policies to reduce unemployment in the poorer regions of the country while narrowing income differentials among the regions. Tito from time to time had to accept slower growth to restrain inflation and deal with rising current account deficits. But policy shifts became increasingly difficult to carry out, in large part because of the nature of the self-managed Yugoslav economy and because of the decentralized decisionmaking Tito introduced in the 1970s. In the year before his death, the inflation rate was again climbing and hard currency trade deficits were mounting. The central government's ability to manage its internal and external economic difficulties without Tito was at best questionable. [redacted]

[1] This assessment deals with the domestic factors facing the current leadership. Foreign policy considerations will be covered in a future paper. [redacted]

Cvijetin Mijatovic ends one-year term as State President in May [redacted]

The Succession in the Government and the Party

Collective leadership in the State Presidency proved to be surprisingly resilient in its first year. Within hours after Tito's death, the Presidency[2] installed Vice President Lazar Kolisevski as President. Less than two weeks later, Kolisevski's tenure ended as scheduled. The Presidency, according to the established formula of rotation, named Cvijetin Mijatovic, a Serb from Bosnia-Hercegovina, as the new President, and Sergej Kraigher, a Slovene, as Vice President. The strict observance of the rules of collective leadership as laid down by Tito was calculated to project an air of confidence and continuity and succeeded in doing so. [redacted]

[2] The *Presidency* of the Socialist Federal Republic of Yugoslavia is a nine-member government body. Representatives of the republics make decisions on a collegial basis, and the posts of president and vice president are passed from member to member. [redacted]

During the year, however, some proposed constitutional amendments to legalize the collective leadership system for state bodies aroused public criticism. The amendments would:

- Make each member of the collective executive body responsible for his own portfolio and for collective decisions by the body.
- Set a four-year term of office for members of the collective bodies.
- Establish a one-year term of office for the President and Vice President of the Federal Assembly and rotate the two among representatives of the six republics and two provinces.
- Give the presidents of the Chambers of the National Assembly a one-year term (although a two-year term is being discussed also).
- Limit Cabinet ministers to four-year terms, and the Premier's term to either four years, two years with option of another two years, or a single year.
- Fix an eight-year single term of office for Constitutional Court judges.

[redacted] debate has been heated in the Federal Assembly's Commission for Constitutional Questions over the issue of the one-year term for executive positions like Premier, Cabinet members, and judges. The amendments have only recently cleared the committee for Assembly action. [redacted]

The succession within the party has proceeded less smoothly than that in the government. Tito established a one-year mandate for the President of the 23-member Presidium of the League of Communists of Yugoslavia (LCY). He alone, however, chose the two persons who filled the job during his lifetime. The only statute relating to candidates for the post is that no republic or province can be represented more than once until all have had their turn. Unlike the state presidency, there is no established order of rotation among the republics and provinces. A committee now makes the selection, and last October it chose Lazar Mojsov, a Macedonian. Yugoslav press coverage of a Presidium session last June candidly admitted that because of conflicting views within the leadership only a temporary modification in the party rules could be worked out. [redacted]

Lazar Mojsov, a Macedonian serving a term as President of Party Presidium [redacted]

Progress in Stabilizing the Economy

The Final Year of Tito's Reign. Following two years of rapid growth, the economic situation deteriorated drastically in late 1979, Tito's last full year in power. Halfhearted stabilization measures failed to curb domestic demand and the inflation rate climbed above 20 percent, the highest rate in four years. Substantially higher oil prices coupled with buoyant import demand and weak demand for Yugoslav exports helped boost the current account deficit to a record $3.7 billion, almost triple the 1978 level. Foreign bankers turned bearish, forcing Belgrade to short-term borrowing and to draw down official reserves to the equivalent of only five weeks of imports by the end of the year. This compares with reserves worth more than three months of imports at the end of 1978. [redacted]

Upset by the 1979 results, Belgrade entered the new year determined to stabilize the economy. Economic plans for 1980 set lower growth targets and emphasized certain restraints:

- Fiscal policy was tightened with public expenditures slated to grow less rapidly than social product.
- Tighter credit was intended to force enterprises to rely on internal savings, thereby curtailing investment growth.

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Table 1

Selected Economic Indicators

	1975	1976	1977	1978	1979	1980 [a]
Trade balance (billion US $)	−3.6	−2.5	−4.6	−4.6	−7.2	−6.1
Exports	4.1	4.9	5.2	5.8	6.8	9.0
Imports	7.7	7.4	9.8	10.4	14.0	15.1
Current account balance (billion US $)	−1.0	0.2	−1.4	−1.3	−3.7	−2.3
Official reserves, yearend (billion US $)	0.9	2.0	2.1	2.5	1.3	1.5
Convertible currency debt outstanding, yearend [b] (billion US $)	5.6	6.8	8.1	10.0	12.3	13.1
Convertible currency debt service ratio [c] (percent)	18.4	15.9	15.0	16.9	19.5	22.0

[a] Preliminary.
[b] Medium- and long-term; excluding borrowing from the IMF.
[c] Ratio of debt service to exports of goods and services.

[redacted]

- A legally binding incomes policy was imposed to slow the rise in consumer spending.

The government's emphasis on the economy was underscored by the Presidency's unprecedented use of emergency legislative powers to require a lower ceiling on the 1980 balance-of-payments deficit than the republics wanted. [redacted]

Despite Belgrade's intentions, 1980 began badly. Inflationary pressures inherited from 1979 were increased by the lifting of the temporary price freeze, by a reduction in price subsidies on some consumer goods, and by a steep jump in the price of imported crude oil. During Tito's illness, uncertainty about Yugoslavia's stability also prompted some capital flight. Consumer demand surged in expectation of higher prices, and enterprises went ahead with new investment projects before further restrictions could be implemented. With Tito still in the picture, the new leadership remained tentative. Its only significant action in the first few months of 1980 was to impose additional restrictions on investments in the public and service sectors of the economy. [redacted]

After Tito. The stabilization program embodied in the late 1980 Plan began paying off by mid-1980—aided by growing confidence in the leadership's ability to govern without Tito. Economic activity slowed as the growth of industrial production and new fixed investment slackened. Even the inflation rate showed some signs of decelerating, and the trade deficit was slightly less than a year earlier. [redacted]

The new collective leadership pushed ahead with further stabilization measures at midyear. In early June—just a month after Tito's death—the government devalued the dinar by 30 percent, imposed a partial price freeze, and reduced planned growth targets. These measures were to have been supplemented at the end of July with another stabilization package—including measures to restrain investments and imports—but it was never introduced. Meanwhile, the release of the plans for 1981 and 1981-85 slipped behind schedule, reflecting interrepublic and leadership conflicts over economic policies. [redacted]

Belgrade had to alter its economic program later in the year as severe shortages of key consumer goods and industrial materials developed. Some steps were

Table 2 — Average Annual Percent Growth

Real Trends in the National Accounts

	1977	1978	1979	1980 [a]	1976-80 [a]	1981-85 [b]
Private consumption	7.0	7.0	6.0	0	4.9	3.0
Public consumption	7.4	5.3	7.9	3.4	5.3	3.3
Gross fixed investment	11.7	13.4	4.6	−1.5	6.8	1.5
Export volume	−4.4	−1.9	3.4	10.0	3.4	8.0
Import volume	12.5	−1.3	9.8	−11.0	0.6	1.5
Gross social product [c]	8.0	6.8	7.0	3.0	5.6	4.5

[a] Preliminary.
[b] Plan.
[c] GSP differs from GNP in that the nonmaterial components of services rendered to the population and to the government are excluded.

[redacted]

consistent with reducing domestic demand. The government, for example, sought to decrease demand for goods in short supply by increasing some prices and by lifting controls on others, including a wide range of important consumer and industrial products. This signaled a partial victory for advocates of greater reliance on market forces. To dampen the inflationary impact of the price rises and further restrain demand, the government also raised down-payment requirements on consumer goods bought on credit. At the same time, however, the leadership offered consumers some relief—at the expense of improving the balance of payments—by temporarily curtailing exports of some foodstuffs and by authorizing sales of some items from commodity reserves. [redacted]

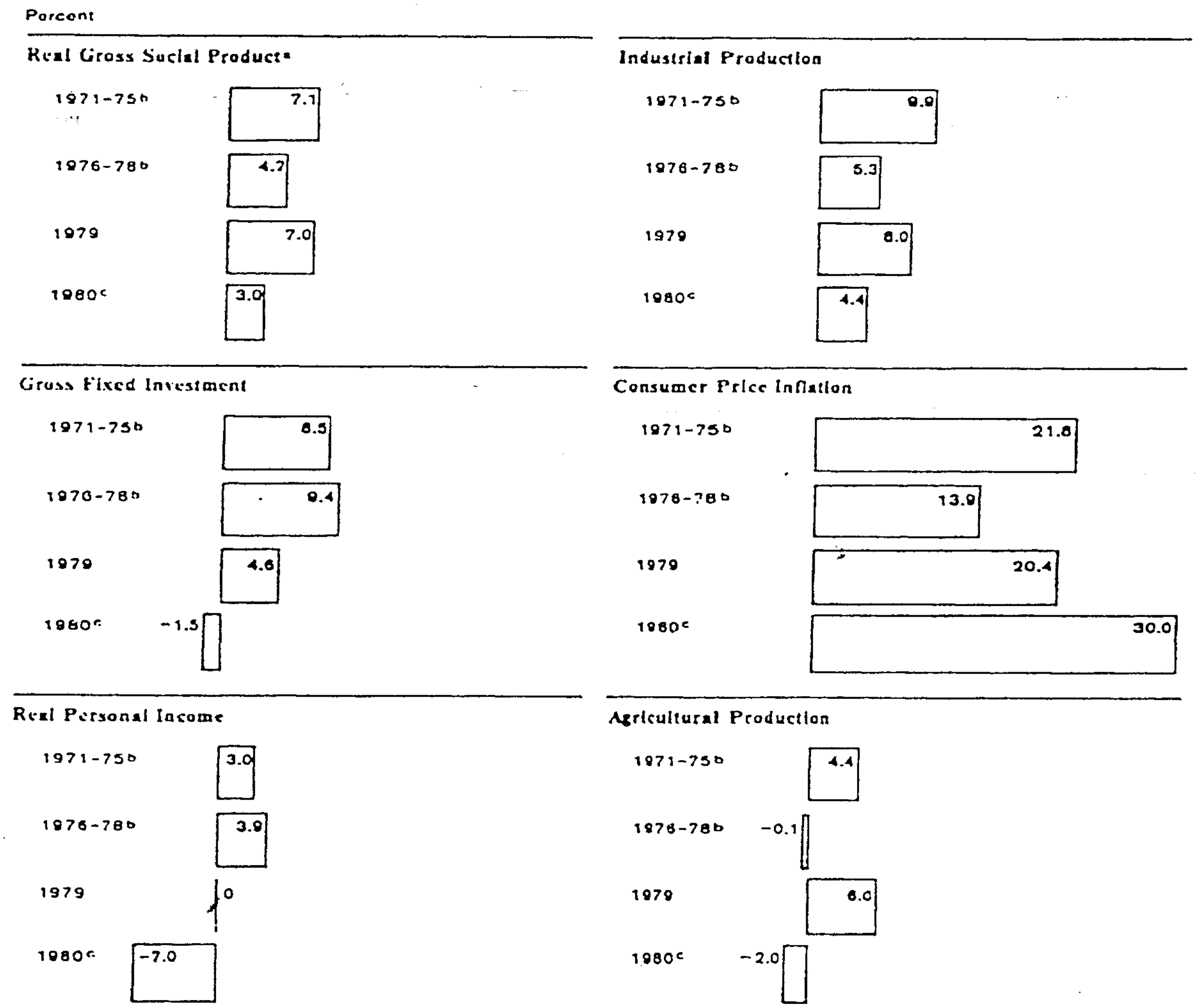
The 1980 Outturn. The stabilization program was successful in redirecting production from domestic uses to exports. The growth of domestic demand was curbed as real GSP (gross social product) growth fell to 3 percent—less than half the rate of growth in 1979 and the lowest since the late 1960s. After a first-quarter surge, investment growth slackened considerably by the end of the year, private consumption stagnated, and real incomes fell 7 percent below their 1979 level. [redacted]

Belgrade's greatest achievement in 1980 was to improve its foreign economic position. Slower growth of domestic consumption and investment and the June devaluation helped to reduce the trade deficit in 1980 by more than $1 billion compared with 1979. Exports were up more than 30 percent (10 percent in real terms) compared with the corresponding period in 1979 while imports increased by less than 10 percent (a decline of more than 10 percent in real terms). Recovery in receipts from Yugoslav workers abroad and increased receipts from tourism contributed to a reduction in the current account deficit—to $2.3 billion in 1980, about $1.4 billion lower than in 1979. Official reserves rose somewhat, climbing to $1.5 billion by the end of December after reaching a low of $800 million in May. [redacted]

But inflation continued to accelerate—prices were rising at an annual rate of 40 percent by the end of 1980 despite the slowdown in economic activity. Although part of the rise can be attributed to underlying inflationary forces, other special factors share much of the blame:

- The 30-percent devaluation of the dinar in June.
- The 95-percent increase in oil-product prices to encourage conservation.
- The lifting of price controls on a broad range of industrial and consumer goods.
- The raising of prices still under federal control in order to balance supply and demand. [redacted]

Figure 2
Growth of Selected Economic Indicators



[a] GSP differs from GNP in that the nonmaterial component of services rendered to the population and to the government is excluded.
[b] Average annual.
[c] Preliminary.

[redacted]

Consumers, unaccustomed to lengthy periods of austerity, clearly felt the pinch in 1980. Several minor incidents of labor unrest were reported, possibly over wage demands. Furthermore, trade union officials began calling for an even more active role for workers in economic decisionmaking. Though Belgrade remained committed to stabilization, the leadership became cautious about introducing measures that would impinge further on real incomes. [redacted]

Moreover, despite the improvement in its external accounts, Yugoslavia's borrowing ability was in question during much of the year. In the first half of the year, Belgrade had difficulty getting medium- and long-term financial credits and was forced to use official reserves and to borrow short term. Bankers were uncertain about Yugoslavia's stability during Tito's illness and harbored lingering antagonisms over Belgrade's overbearing tactics in refinancing a number of loans in 1979. A $600 million Eurocurrency loan was undersubscribed by almost $200 million. [redacted]

After Tito's death, the new leadership embarked on an aggressive campaign to raise funds, playing heavily on Western fears that a lack of support might destabilize post-Tito Yugoslavia. Since mid-1980, Yugoslav borrowing has been aided by the International Monetary Fund's endorsement of the 1980 stabilization program, the June devaluation of the dinar, and renewed party and government commitment to austerity. A $400 million Eurocurrency loan signed in late December, coupled with several bilateral loans, helped Belgrade to get through the year. [redacted]

Politics, Economics, and Regional Rivalries

In the main, regional rivalries have not resulted in confrontations, with the exception of the recent trouble in Kosovo Province. External developments over which Belgrade had no control—notably the impact on Yugoslavia of the Soviet invasion of Afghanistan and the threat of a Warsaw Pact intervention in Poland—probably to a large extent account for the surprising degree of domestic cohesion in the face of varying political and economic interests. Nonetheless, the basis for interregional jealousies over economic development is as solid as ever; the relative differences among the republics in terms of per capita GNP have hardly changed in the past 20 years. Nationalism remains a serious problem as well, and a number of disputes have surfaced over the past year. [redacted]

The Albanians. Violent demonstrations in March and April by the country's large Albanian minority in Kosovo Province presented the post-Tito leadership with its most serious crisis. At first the protests centered on unemployment among school graduates but then they took on nationalistic overtones. The regime responded quickly and strongly to clashes between students and the police. A limited form of martial law was declared around Pristina, the provincial capital; additional security forces were sent to the province; and foreign journalists were banned from the area. [redacted]

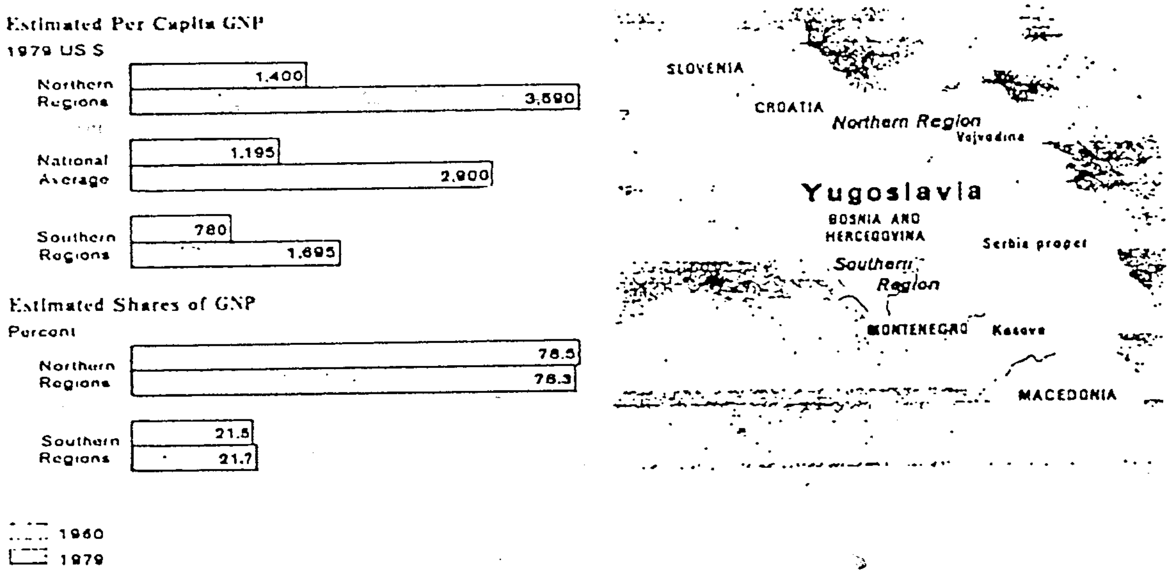
These measures have restored calm for the moment, but the political coloration of the demonstrations may heighten the hostility between the Albanian and Serb communities in Kosovo. The regime is further worried that events in Kosovo could touch off a chain reaction among Yugoslavia's other highly volatile nationalities, eventually upsetting the delicate balance in the collective leadership system. [redacted]

The Serbs. Serbian nationalism, always strong, has been more pronounced than usual for over a year. In particular, the Serbs chafe over the concessions the federal government has forced them to make to the Albanians in Kosovo Province, part of the Serbian republic.[3] Serbs claim they have been forced to emigrate from the province because of the discriminatory practices of the local Albanian leadership. Moreover, although Kosovo has a voice in the Serbian parliament, Serbia has none in the Kosovo provincial assembly. Serbian discontent was particularly apparent following the outbursts of Albanian nationalism in Kosovo in October 1979 and has probably been rekindled by the recent demonstrations. [redacted]

Serbs also have been active in maneuvering behind the scenes at the federal level. For example, Defense Minister Ljubicic, a Serb, apparently has gotten the leadership to agree that high-level military appointments will be made only on his recommendation. Early last year,

[3] The Serbs view the area as hallowed ground because it is the site of the first Serbian Orthodox patriarchy and the last major battleground between Serbs and Turks in 1389. [redacted]

Figure 3
Regional Disparities in Per Capita GNP and GNP



[redacted]

the Serbs reportedly thwarted efforts by the backers of Vladimir Bakaric, the most prominent Croat member of the party Presidium, to make him either the new State President or the next President of the Presidium. [redacted]

Slovenian Grievances. Jockeying for political power was well under way among the regions during the months of Tito's final illness. The most notable member of his former inner circle to be hurt by this maneuvering is Stane Dolanc, a Slovene and a leading party Presidium member. [redacted]

Dolanc played a central political role in Yugoslavia throughout the 1970s, and many observers viewed him as Tito's heir apparent. His prominence, more than any other factor, may have led other members of the collective leadership to curb his power and relegate him to what may now be a less prominent position in the collective leadership. For example, Cvijetin Mijatovic, a Serb, charged Dolanc—[redacted]—with responsibility for some of the shortcomings in the collective leadership system. [redacted]

Continuing Slovenian dissatisfaction with federal economic policy also has contributed to demands that limits be placed on Slovenia's financial contribution to Yugoslavia's underdeveloped regions. Slovenia proposed during Tito's last days that Kosovo alone be defined as an underdeveloped region and that the

Stane Dolanc[redacted]

individual constituent republics negotiate assistance programs directly with Kosovo rather than with the federal government. The unfortunate timing of the initiative—when Tito's political heirs were trying to maintain unity—cast doubt on the premise that the Slovenes would put regional interests aside, at least in the immediate succession period. [redacted]

Slovenia's challenge was also significant because it had heretofore played a leading role in the nation's development. Slovenes are among Yugoslavia's most prominent businessmen and bankers and, more than any other nationality, have helped make the complex political system work. Historically, the push for change and innovation in the federal political and economic system has come from Slovenia. [redacted]

The Croats. Although they continue to be a potential source of disruption, Croatian nationalists have kept a low profile since Tito's death and are not strongly pressing their positions. A recent exchange of polemics between the Croatian Republic leadership and the Catholic Church, however, is symptomatic of the leadership's nervousness over latent Croatian nationalism, which the regime charges is being encouraged by the Church hierarchy. The decision early this year to try Croatian author Franjo Tudjman and other nationalists is further evidence of this apprehension. [redacted]

The surge of terrorist activity by numerous Croatian emigre groups throughout the world that the Yugoslav leadership feared would occur after Tito's death failed to materialize. Nevertheless, concern continues over the potential terrorist threats. [redacted]

Regional Interests and the Economy. The issue of how Yugoslavia should resolve its economic problems has already led to political maneuvering, and two rival groups have emerged. A reformist group—which includes Presidium member Grlickov and Prime Minister Djuranovic—is pressing for change. It has pushed through measures giving greater play to market forces, and it supports stronger macroeconomic decisionmaking power at the federal rather than the republic level. The group has met counterpressure from a conservative faction—including Presidium members Dragosavac and Mikulic—that resists change and fears reliance on capitalist economic methods. The conservatives want to enlist the support of regional leaders—themselves jealous of their hard won autonomy—and of workers and managers who see their positions at risk in a free market system. [redacted]

But differences over how the economy is run have not been nearly as damaging as the paralysis in policy implementation that regional differences encourage. For example, a senior Presidium member [redacted] complained last month that the government cannot accomplish anything, although compromise is usually reached during meetings of the Presidency: "When the members go home [to the republics] nothing happens and everything remains the same." The senior member added that decisions made at the federal level are still ineffective because no one can force enterprises in the republics to follow federal policy. [redacted]

Political Dissidence

Following Tito's death, the regime also encountered growing restlessness among the intellectuals:

- The country's leading dissident, Milovan Djilas, continues to criticize the Yugoslav system as a whole.
- Sixty Slovene intellectuals have petitioned the government for greater artistic freedom, and 100 intellectuals from a number of republics have petitioned for legal guarantees of free speech.
- Approximately 40 Croats have requested amnesty for all political prisoners.

• At least two groups of intellectuals have petitioned the authorities for permission to publish new literary magazines not subject to censorship. [redacted]

Milovan Djilas presents the collective leadership with a special problem. His writings have long attacked the socialist system Tito developed, but more recently he has been debunking aspects of the partisan effort during World War II—particularly in his book, *Tito: The Story From Inside*. Because members of the collective leadership owe their legitimacy to their ties with Tito and to the system he devised, they cannot permit Djilas's attacks to go unanswered. [redacted]

Although the regime hinted recently that Djilas is not living up to his 1961 agreement to refrain from political activity, it probably will try to avoid a showdown. Last year, when Djilas ran into trouble because of an article he wrote for the underground journal *The Clock*, he was tried and fined. When he refused to pay the fine, the court shied away from imprisoning him and took deductions from his pension until the fine was paid. There are limits, however, to how far Djilas can go, and the regime's response will depend on how seriously it views Djilas's actions. [redacted]

Twenty of the signatories of the Slovenian petition for greater artistic freedom are party members in good standing, and most of the rest are prominent artists. This almost certainly worries the republic leadership, which remembers that neighboring Croatian intellectuals played a major role in the 1971 outburst of nationalism in Croatia. The Slovene petition is the latest in a growing list of student and intellectual protests which, in addition to those already mentioned, have included (a) a plea by 36 Belgrade intellectuals for amnesty for all persons convicted of "verbal" political abuse, (b) a call by Croatian students for an end to federal economic aid to underdeveloped regions of Yugoslavia, and (c) Croatian criticism of political restrictions on literary and other cultural activity at a writers' conference in Zagreb last May. [redacted]

Since Tito's death, debate has intensified within the leadership over the degree to which dissent is to be tolerated. The pragmatic reformers have urged continued "differentiation" between legitimate criticism and antiregime dissent that threatens the socialist self-management system. The reformers, including party Presidium members Bakaric and Dolanc, appear to have succeeded in moving Yugoslavia toward more open criticism, debate, and decisionmaking. With an eye on its relations with the West, Belgrade evidently wants to allow an open dialogue but to keep it under control. It hopes that a balanced policy of drawing clear but relatively wide limits to the criticism it can tolerate will preclude the need for stronger measures. [redacted]

Outlook

Despite having to work within an inherently cumbersome collective system, the new Yugoslav leadership has managed well without Tito. The continuing Soviet presence in Afghanistan and the possibility of a Warsaw Pact intervention in Poland—both perceived by Belgrade as potential threats to Yugoslavia's independence—should continue to help unify the new leadership. Nonetheless, there are signs that this tranquility may be shortlived. The economy is far from being under control, debate over economic issues is becoming louder, and political dissidence is likely to be more of a problem in the 1980s than it has been. [redacted]

Austerity and Living Standards. While 1980 marked a step in the right direction, Yugoslavia still must accept a prolonged period of economic austerity coupled with improvement in the system of self-management in order to correct current economic shortcomings. [redacted]

The draft plan for 1981-85 implies that the new leadership is unified on the goals of slowing inflation and further reducing the current account deficit. These goals are to be achieved by continued efforts to hold the growth of domestic demand below that of aggregate output in order to free resources for export. The annual growth of real gross fixed investment is expected to drop sharply in 1981-85, to only 1.5 percent. The plan projects a slight increase in per capita real personal incomes for the nation as a whole, with the emphasis on improving living standards in the poorer republics. Private consumption is targeted to grow by 3 percent annually, down appreciably from the 5-percent growth rate of the last five years. [redacted]

Belgrade's stabilization efforts will not be limited to demand restraint measures, however. The leadership is also stressing "supply-side" improvements, increased labor productivity, export promotion, import substitution, production of more of the commodities in short supply, a more realistic exchange rate policy, and a restructuring of investment. Efforts to implement these goals will be monitored by the IMF over the next several years. [redacted]

A reordering of investment priorities to accentuate efficiency is the heart of the program. To help overcome shortages, funds are to be directed away from the low-yielding sectors of the economy toward such priority areas as agriculture, energy, and raw materials. Belgrade will depend heavily on credit rationing, Yugoslavia's traditional tool of monetary policy. The high-priority sectors are to receive preferential domestic financing and 80 percent of the receipts from foreign borrowing. Nonpriority sectors will encounter more restrictive borrowing conditions as well as outright cutbacks in investment plans. At the same time, Yugoslavia plans to use other instruments of monetary policy that have been largely neglected in the past. Belgrade plans, for example, to push interest rates up to more realistic levels. The only step in this direction so far has been to raise rates paid on deposits in financial institutions, forcing higher lending rates. [redacted]

Fiscal measures are also planned to help push investment into the right channels. Import taxes will be reduced and tax exemptions increased for enterprises in the priority sectors. Belgrade also hopes that the freeing of some prices from federal control and the raising of other administered prices will help promote more efficient investment allocations. [redacted]

Economic Policy in the Near Term. Before the policies of the 1981-85 plan can be expected to have substantial results, however, Tito's successors will have to manage a difficult transition marked by high inflation, consumer grumbling, and political contention over economic policy. [redacted]

Table 3 Percent

Growth of Selected Indicators

	1980 Plan	1980 Actual	1981 Plan
GSP	5.0	3.0	3-3.5
Industrial production	6.0	4.4	4
Agricultural production	6.0	−2.0	4
Gross fixed investment	6.0	−1.5	−5
Export volume	6.0	10.0	7
Import volume		−11.0	−3

[redacted]

Belgrade's short-term strategy—as reflected in the 1981 plan—continues the austerity imposed in 1980 and stresses improvements in the key agricultural and energy sectors. The 1981 plan also reflects a more realistic view of Yugoslavia's prospects. Goals for gross social product (GSP), industrial production, and farm output are less ambitious than the original 1980 targets. The plan, moreover, did not set a goal for the inflation rate or ceilings for increases in money incomes as was done in previous years, suggesting the prevailing uncertainty in these areas. Instead, prices are to rise "more slowly" than in 1980, with the 70 percent of prices still subject to control of the self-managing interest groups left to be determined by social compacts. The income policy calls merely for personal incomes to increase with enterprise net incomes, modified by differential productivity growth and the need to protect the living standards of low-paid workers. [redacted]

The new leadership, however, has been prompted to take additional steps against inflation in response to continuously surging prices—the cost-of-living index rose by 11 percent in the first two months of this year. A new self-management agreement on prices was signed in early March—nearly three months after the previous price control legislation had expired. The new pricing measures establish the broad outline for pricing policy, specifically a 30-percent target for the cost-of-living increase this year. As a short-term emergency measure, the new agreement reasserts federal price controls over key items such as food staples, energy, and some services. In addition, self-managing price bodies are to review all price hikes since the beginning of the year and can authorize price rollbacks for increases that are inconsistent with the new agreement. The anti-inflationary drive was buttressed at the end of the month with new credit restrictions. Belgrade halted credit sales for automobiles and a wide range of luxury goods and increased the minimum cash downpayment required on all other items not subject to the ban with the exception of children's clothing and footwear. [redacted]

Despite the recent flurry of activity, the specifics of price policy still have to be hammered out over the next few months by federal and republic authorities and by the new self-managing price bodies. Because the new pricing policy is to be implemented through self-management agreements, it is subject to the usual pitfalls that confront such legislation. A major stumblingblock in achieving a strong anti-inflationary policy is the loss of federal power over prices. Following the recent liberalization of prices, Belgrade may be reluctant in the near future to recentralize power over pricing policy. [redacted]

On the positive side, Belgrade's foreign borrowing situation looks encouraging. Although its official borrowing plans are undecided, its needs should be down this year because the current account deficit is projected to be lower. Belgrade has already concluded loan agreements with West Germany and an Arab consortium, and negotiations are under way for a loan from the Swiss. More importantly, the IMF's recent award of a $2 billion loan to Yugoslavia (covering three years) will reduce Belgrade's borrowing requirement and increase the confidence of foreign lenders who otherwise might be reluctant to lend to Yugoslavia. [redacted]

Belgrade's borrowing cutback could still go awry should the new leadership fail to hold the line on the trade deficit. Attempts to hold down real import growth may prove incompatible with the projected growth in GSP. And another OPEC price boost could also upset this year's import target. Belgrade's crude oil bill is currently running close to 20 percent of the value of total imports. Belgrade must also worry about the effect of accelerating inflation on exports. Rising domestic prices are bound to make the domestic market more attractive to producers and, at the same time, encourage imports. The benefits resulting from the June devaluation could well vanish quickly, prompting Belgrade to devalue the dinar again this year. Real exports have already decreased by nearly 15 percent during the first two months of the year. In an effort to stimulate exports, supplementary credits for exports have been granted for the remainder of 1981, and proposals have been introduced for increasing imports of goods needed by export sectors. [redacted]

Despite the improvements made in the external sector in 1980, Belgrade still has much to do to restore some balance to the internal economy. Curbing the growth of domestic demand while stimulating production will require a high order of cooperation and compromise among leaders who represent different regional interests and who only recently ended months of bickering over the broad outlines of future policy. In addition, the federal authorities may have to recentralize some of the power needed to execute sound policy after years of gradual erosion of their power through decentralization of decisionmaking to the republics. Such a move is likely to encounter stiff opposition not only from regional authorities but also from bureaucrats and workers who have a vested interest in preserving the present system. To date, the only significant change made in the post-Tito economy is some decontrol of prices. [redacted]

Belgrade must also worry about how workers will react to a prolonged period of slow economic growth. Spot shortages of consumer goods and a further decline in real incomes are distinct possibilities again this year. Continued austerity could exacerbate regional tensions if the poorer republics feel that they are once again bearing the brunt of Belgrade's policies. Nonetheless, the Yugoslav leadership appears confident that it will not face the level of worker unrest that has plagued Poland. Although not legal, strikes have been tolerated for years, and most grievances are settled in favor of the workers. Although an imperfect system, self-management [a] does give the workers a sense of participation in decisionmaking. The leadership has shown its sensitivity to potential worker discontent by enhancing the trade unions' image as protector of workers' interests, stepping up visits to factories, and co-opting the top labor leader into the Central Committee. It has also assured the public that real incomes, which dropped roughly 7 percent last year, would not be allowed to drop further. [redacted]

Conflict Within the Leadership. Arguments within the leadership over ideopolitical and economic issues have been kept in check although the opposing posi-

[a] This and other uniquely Yugoslav institutions are described in the appendix. [redacted]

tions of key players are becoming more pronounced. Thus far, those calling for reforms in the economic system and a more open dialogue have the upper hand. The conservatives, however, will continue to stand firm and show no sign of caving in to the liberals. Debate is likely to become more pronounced as the 12th Party Congress, scheduled for June 1982, approaches. We may see significant personnel shakeups at all levels prior to or during the congress if proponents for change find themselves in positions of strength. [redacted]

Meanwhile, no member of the top leadership has shown any tendency to exploit regional differences to enhance his personal power. The temptation to articulate issues in nationalistic terms is inherent in the Yugoslav system, however, and this could become a factor if the struggle over top party positions becomes heated. The next test for the leadership will come in May when a new party secretary will be selected to serve a one-year term. [redacted]

Appendix

Economics of the Tito Era

While some of Yugoslavia's current economic problems result from forces beyond Belgrade's control—such as rising world prices and sluggish demand in the West for Yugoslav exports—many are of domestic origin:

- An ambitious development strategy.
- Slow and often inadequate adaptation of policies to changing economic conditions.
- Institutional problems largely associated with the unique features of the self-managed Yugoslav economy and the decentralizing reforms introduced by Tito in the 1970s. [redacted]

Emphasis on Rapid Growth

The major goal of economic policy in the Tito era was rapid economic growth. Political needs gave impetus to expansionary policies aimed at minimizing unemployment, improving living standards, narrowing income differentials, and promoting development of the poorer regions of the country. During Tito's last decade in power, Yugoslav economic growth was impressive. Gross social product rose by about 6 percent a year with the upswing interrupted only twice, in 1972-73 and again in 1975-76. Excess demand arising largely from buoyant investment fueled by expansionary monetary policy and rapid advances in wages and the prices of goods that Yugoslavia must import generated rapid inflation as consumer prices rose by an average of 18 percent a year during the seventies. [redacted]

On the external side, poor export performance combined with surging imports to widen the foreign trade deficit. Some exogenous shocks contributed to the growing deficit—the Montenegro earthquake in 1978 and the various OPEC oil price boosts are two—though Yugoslavia fared better than many nations after the 1973/74 oil price jump. Moreover, export performance was hindered by sluggish economic growth in the West and increasing Western trade protectionism—especially in the EC—that affected commodities representing a significant portion of Yugoslav exports. [redacted]

Belgrade's rapid growth policy, however, must shoulder much of the blame for the poor foreign trade performance in the latter half of the decade. Strong domestic demand fostered strong import demand, particularly for raw materials and semifinished goods. Sharply rising domestic prices also provided Yugoslav enterprises with attractive markets, thus diverting goods from the export market. Indeed, buoyant domestic demand over the years has essentially dulled incentives to develop a major export sector. [redacted]

Rising receipts from tourism and from funds sent home by Yugoslav workers abroad provided some cushion against the worsening trade deficit, but substantial recourse was made to foreign borrowing to finance rapid growth. Increased liquidity in international capital markets meant that Yugoslavia had reasonably easy access to funds. As a result, Yugoslavia's convertible currency debt increased almost sevenfold over the decade of the 1970s, from $1.6 billion at the end of 1969 to $12.3 billion at the end of 1979. [redacted]

Stop-Go Adjustment Policy

Despite chronic economic overheating—as evidenced by accelerating inflation in the 1970s—Belgrade was slow to introduce stabilization measures. The government responded only when external financial imbalances became severe, slamming on the brakes when foreign borrowing was not sufficient to cover current account deficits and when Yugoslavia's international reserves were drawn down to uncomfortably low levels (as in 1970, 1975, 1979). With prodding by the party apparatus and Tito, Belgrade tightened import controls, imposed credit controls, and froze prices. These restraints reduced real growth abruptly and also slowed inflation. Belgrade also devalued the dinar twice during the decade, in 1971 and late 1974, in order to help reduce trade deficits. As soon as the balance of payments improved, however, Belgrade resumed rapid growth policies. Inflation would then accelerate, eroding the benefits of the devaluation. [redacted]

These brief periods of restraint restored bankers' faith in Yugoslavia's creditworthiness, and lending activity revived. But reliance on this stop-go approach did not permit resolution of the fundamental problems contributing to domestic and external imbalance. Moreover, the stop-go approach was costly, disrupting production and causing the bottlenecks that inevitably accompany sudden shifts in policy. [redacted]

Institutions Impede Adjustment

The decade of the 1970s was also a period of institutional change as Tito continued his efforts to build a political and economic system that would survive him. He hoped to lay the foundations for an orderly succession and to provide solutions to economic and political problems by further adaptations of Yugoslavia's unique form of worker self-management and market socialism. In the economic sphere, this led to further decentralization and to a transfer of policymaking authority from the federation to the republics. [redacted]

Decentralization compounded longstanding weaknesses in macroeconomic policy tools, making it difficult for Yugoslav policymakers to implement effective adjustment programs. The scope for fiscal policy, for example, has been considerably reduced because most fiscal power has been transferred from the federation to the republics and to new public sector bodies at the local level. Federal budget expenditures, for example, now account for only one-fifth of total public-sector spending. The federation must obtain republic consent to changes in tax policy, a time-consuming process. Fiscal policy is therefore not an effective countercyclical tool in Yugoslavia. [redacted]

The capacity of the authorities to control and influence prices and incomes is limited by certain features of the Yugoslav economic system. In a worker-managed economy the tendency of workers to direct firms' net income toward wages rather than retained earnings is reinforced by the willingness of banks—owned by enterprises—to finance a large share of investment (banks financed 47 percent of fixed investment in 1979). Reliance on cost mark-up pricing in a climate of buoyant demand has led management to raise prices even faster than the rapidly increasing labor costs. The interplay of these factors has added a strong wage-push element to inflationary forces. [redacted]

Monetary policy—the main instrument left to federal policymakers—also suffers from institutional weaknesses. Given the absence of a developed capital market and the problem of regional barriers to capital mobility, the central bank has played a major role in the selective allocation of credits to various sectors of the economy. The central bank establishes selective credit commitments on an annual basis for priority sectors and purposes. But once committed, it has proven difficult for the bank to cut back on credit to serve the larger goal of restricting aggregate demand. Therefore, the central bank has frequently found its hands tied, and monetary policy has accommodated the upward pressure on prices arising from both cost and demand forces. Quarterly credit ceilings remain the main tool of monetary policy. The central bank has been reluctant to use reserve requirements, and there has been considerable opposition to raising interest rates, which are considerably below the inflation rate. [redacted]

A no less worrisome problem lies in the area of foreign trade policy. The establishment of republic-level bodies to make balance-of-payments projections for each republic has further fragmented the Yugoslav market along regional lines and hindered the mobility of capital for foreign exchange. These problems are aggravated by attempts to force individual republics, as well as groups of enterprises within a given sector, to limit the value of goods that they import to the value of their foreign exchange earnings. Although the federal government retains important powers over trade and foreign exchange policy, the new system impedes formulation of national policy, inhibits rational decisionmaking on foreign trade, and fosters hoarding of hard currency. [redacted]

Trying To Develop a Coordinated Policy

To cope with decentralization, central authorities have relied on an array of institutional innovations. Agreement among republics (as well as among government organizations, enterprises, and trade unions) on economic policy matters is accomplished in "social compacts." [1] These are used in combination with "self-

[1] These are statements about policy objectives in certain areas such as planning, prices, income distribution, international trade, and employment. They are a substitute for government laws and, although not legally binding, obligate the parties signing the compact to take measures to implement the policy objectives. [redacted]

management agreements,"[2] which legally bind the signatories (government organizations, enterprises, and trade unions) to take certain measures in order to achieve economic policy objectives. [redacted]

Social compacts require lengthy negotiation. Because specific policy measures were often not part of the compacts, republics enjoy considerable discretion, resulting in a patchwork of measures differing from republic to republic. Investment decisions have been poorly coordinated, and considerable overinvestment has occurred because self-management agreements (between enterprises in the same branch) are used instead of efficiency criteria in allocating investment. Some self-management agreements may indeed have led to monopolization of certain markets along product lines and within individual republics. [redacted]

The basic problems impeding rational investment decisions, however, continue to be the lack of a developed capital market, the reliance on bank credits to finance a high proportion of investment, and negative real interest rates. A combination of central bank controls and agreements among banks and enterprises has kept interest rates below those that would result from the interaction of market forces. If lending rates are too low, worker-managed enterprises tend not to save and instead scramble for bank credits. Low interest rates also discourage saving by workers, widening the imbalance between savings and investment in the economy. Use of social compacts for setting prices has allowed firms to pass on their higher labor costs, thus hindering efforts to curb the inflationary wage-price spiral. [redacted]

[2] Self-management agreements are signed by government organizations, enterprises, and trade unions for the realization of specific policy objectives. If one or more participants fail to meet their contractual obligations, the others can seek recourse in a special court. [redacted]

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