

# GENERAL AGREEMENT ON TARIFFS AND TRADE

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## REPORT OF THE COMMITTEE ON BALANCE-OF-PAYMENTS RESTRICTIONS ON THE CONSULTATIONS WITH YUGOSLAVIA

1. The Committee has conducted the consultation with Yugoslavia in accordance with its terms of reference. It had before it the basic document for the consultation supplied by the Government of Yugoslavia (BOP/53 and Corr.1) and documents provided by the International Monetary Fund as noted in paragraph 3 below.
2. In conducting the consultation, the Committee followed the plan of discussion for consultations recommended by the CONTRACTING PARTIES (BISD, Seventh Supplement, pages 97-98). The consultation was completed on 27 October 1965. This report summarizes the main points made during the discussions.

### Consultation with the International Monetary Fund

3. Pursuant to the provisions of Article XV of the General Agreement, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation. In accordance with the agreed procedure the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Yugoslavia. The statement made was as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision<sup>1</sup> and background material from the last consultation with Yugoslavia under Article XIV of the Fund Agreement.

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<sup>1</sup>Annexed to this document.

"The Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of July 23, 1965 taken at the conclusion of its last consultation with Yugoslavia under Article XIV of the Fund Agreement. On July 23, 1965, the Fund also concurred in a new par value for the Yugoslav dinar and approved a 12-month \$80 million standby arrangement with the Government of Yugoslavia in support of a reform of the country's economic organization and foreign exchange system. It is noted that the Executive Board decision reads, in part, as follows:

'As part of the reform, the Yugoslav authorities will eliminate quantitative restrictions on imports of raw materials and spare parts, and will liberalize restrictions on imports of capital goods. Some liberalization will also be made in the field of invisible payments.'

The Fund is remaining in consultation with the Yugoslav authorities regarding the implementation of the reform."

Opening statement of the representative of Yugoslavia

4. The representative of Yugoslavia noted that this was the second appearance of his country before the Committee to conduct consultations on restrictions maintained for balance-of-payments reasons in conformity with Article XVIII of the General Agreement. He recalled that in the course of the previous consultation in 1963 questions relating to Yugoslavia's economic system were considered and closely examined. He went on to outline trends in the Yugoslav economy since that time and to point out certain facts which require the further maintenance of certain foreign trade restrictions.

5. He said that the rate of growth in the Yugoslav economy in 1961/62 had been moderate and that measures had therefore been taken early in 1963 to intensify economic activity. Investment and personal consumption had been stimulated by the expansion of resources out of which investment credits were granted and by the easing of conditions for the granting of consumer credits.

6. These measures had had a positive impact on the Yugoslav economy in 1963 and had been retained until July 1964. For instance, the total national product in real terms increased by 12 per cent in the period 1963-64. Industrial production had increased by 34 per cent and agricultural production by somewhat over 16 per cent during the last two years. The high level of investment influenced the growth of production in general and of industrial production in particular. Thus the volume of investment in 1964 had been 30 per cent greater than in the previous year, whilst the physical volume of industrial production had increased by 16 per cent in both 1963 and 1964. The increased economic activity during these two years contributed to an accelerated growth in the rate of employment and to the increase of personal income, which was 25 per cent higher in 1964 than in 1963.

7. However, certain unfavourable effects, such as an increase in total consumption above the level of supply particularly towards the end of 1963 and in 1964, and an increase in prices, had also been noted during this period. These unfavourable effects had been reflected in particular in the foreign trade balance. Increased prices and high demand had made the domestic market more attractive for Yugoslavia's export industries and a great part of goods produced found an even better market in the country. This had contributed to a relative decline in the rate of growth of exports and had at the same time facilitated an increase in imports. Thus, imports in 1963 had increased by 19 per cent as against 14 per cent in the case of exports, whilst in 1964 imports had increased by 25 per cent as against an increase of only 13 per cent in exports. Natural disasters such as earthquakes and floods had also created additional demands for imports in 1963 and 1964.

8. This imbalance became more accentuated during 1964 and it became necessary to take measures to slow down domestic consumption and to remove the causes of inflation. To this end measures had been taken in the second half of 1964 to cut

down investment and personal consumption primarily by decreasing the total volume of credits. Meanwhile, the preparatory work for the economic reform was already being carried out. This reform was based on the Resolution on basic guidelines for the further development of the economic system and on the Resolution on guidelines for the working out of the Social Plan for Yugoslavia up to 1970. These Resolutions had been passed by the Federal Assembly in 1964. In the same way the Social Plan of Yugoslavia for 1965 provided for the maintenance of measures already taken and the introduction of additional measures designed to have a stabilizing effect on the economy. It was also designed to bring about an improvement in the balance-of-payments situation. This improvement was expected to result from measures designed to stabilize the market and those to bring about a change in the relations within the economy and the economic system as a whole. A decision had also been taken to freeze prices of industrial products. This measure, as well as others taken in 1964, fell within the programme of economic reform introduced on 26 July of this year.

9. Too short a time had elapsed since that time to enable the Yugoslav Government to estimate the effect of this reform. The representative of Yugoslavia nevertheless indicated some trends which had been noted in the first eight months of 1965. Industrial production had shown a more moderate increase and was 9 per cent greater than in the corresponding period of 1964. A better supply of raw materials and other reproduction goods had also been observed. Stocks of these goods had in fact shown an increase in comparison with the same period of last year. Stocks of finished goods had also increased. Investments had increased by about 5 per cent against an increase of about 30 per cent for the whole of 1964, the slowing down of investments being particularly characteristic for the end of the first half year. The foreign trade balance had also improved, exports having increased in the first eight months of this year by 17 per cent and imports having decreased by 5 per cent in relation to the same period in 1964, as a result of decreased demand.

10. The representative of Yugoslavia outlined in brief the measures comprising the economic reform. He pointed out that the essence of these measures would be explained in more detail in a document to be submitted to the CONTRACTING PARTIES in connexion with Yugoslavia's request for accession. He mentioned firstly the fixing of a new par value for the dinar on the basis of D1,250 for \$1. As from 1 January 1965, one hundred present dinars would be converted into one new dinar. The new par value represented a uniform exchange rate and was being applied to all payments without exception. Further, export subsidies had been abolished and a greater degree of liberalization of imports was to be introduced especially in the case of imports of raw materials and spare parts. For all other imports global quotas would be introduced and a more liberal policy applied to imports of equipment. All these measures would be introduced gradually, depending on the balance-of-payments situation and the level of monetary reserves which it was felt should be increased up to 25 per cent of total annual payments. At the same time a new law on the customs tariff had been passed. The duties in the new tariff were considerably lower than those in the existing provisional tariff, the average incidence of duties in the provisional tariff being 23.29 per cent compared with an average of only 11.7 per cent for the new tariff. Fiscal elements had been eliminated from the tariff to the maximum extent possible. Details of the new customs tariff would be submitted to the CONTRACTING PARTIES in a separate document. The essence of these and of the other measures taken within the framework of the economic reform consisted in the decentralization of decision making in the economy, in the elimination of price distortions, and in the strengthening of market criteria in price formation with the greater impact of foreign competition. Thus, conditions were created for a more complete inclusion of Yugoslavia in the international division of labour.

11. The representative of Yugoslavia went on to summarize developments in the foreign trade of his country during the last two years. The negative trade balance had increased considerably in 1964 as compared with 1963, rising from

\$207 million to \$429 million. Certain basic causes of this development had already been mentioned. Provisional data for the first six months of 1965 showed that exports had risen from \$417 million to \$481 million and that imports had decreased from \$660 million to \$621 million, compared to the same period of 1964. The representative of Yugoslavia recalled that the greater part of Yugoslavia's foreign trade was with GATT countries, which took 74 per cent and 71 per cent of total Yugoslav exports in 1965 and 1964 respectively and accounted for 81 per cent and 79 per cent of total Yugoslav imports during the same years. The greatest part of Yugoslav trade was with the convertible currency area which accounted for 55 per cent of Yugoslavia's exports and for about 63 per cent of Yugoslavia's imports in 1964. The CMEA countries took 35 per cent of Yugoslavia's exports and provided 29 per cent of Yugoslavia's imports in 1964, remaining trade being with other bilateral agreement countries.

12. The representative of Yugoslavia then examined certain questions connected with Yugoslavia's balance-of-payments situation. He pointed out that the foreign trade balance was the decisive factor in the balance of payments of his country but that a larger deficit in the foreign trade balance could, to a certain extent, be neutralized by surpluses on services and invisibles. However, the deficit on current account had increased from \$110 million in 1963 to \$208 million in 1964. During 1964 receipts from transport increased by 19 per cent, from tourism by 30 per cent and from emigrants' remittances by 50 per cent, only private transfers being smaller than in the previous year. The net inflow attributable to transport, services, and invisibles amounted to \$173 million in 1964 against \$159 million in 1963 but was, of course, insufficient to cover the large deficit in the trade balance.

13. Two other important factors influenced the Yugoslav balance of payments. These were the level of monetary reserves and repayments of foreign debts. The Yugoslav gold and foreign exchange reserves had reached their highest level in the last four months of 1963 when they amounted to \$146 million. They had started to decrease since that time for the reasons already mentioned and at the

end of 1964 amounted to \$88 million. At the end of the first half of 1965 they were reduced to \$82 million which meant that only about 6 per cent of the total value of imports at the level of 1964 could be covered by reserves. Since that time an improvement had occurred mainly as a result of the drawing from the International Monetary Fund in August. The insufficiency of the monetary reserves was one of the main factors hindering the implementation of a more liberal policy in Yugoslavia's foreign trade relations. A second factor which was particularly relevant to the balance-of-payments situation was the repayments of foreign debts. The structure of foreign loans and credits in respect to their conditions and terms was not always the best for the economy. The obligations of his country on these loans and credits burdened the balance of payments considerably, especially as they were concentrated on the next few years. About 53 per cent of total Yugoslav indebtedness had to be repaid in the years 1965 to 1968. This represented over 20 per cent of total Yugoslav exports at the present level of exports. The representative of Yugoslavia considered it unnecessary to point out that his country had always met its obligations on the due date and that it would continue to do so in the future. He wished, however, to underline that, in spite of the unfavourable situation in the balance of payments and in spite of natural disasters, steps had been taken since the last consultation in this Committee for a further decrease in import restrictions by his country. However, the considerable deficit in the balance of payments, and the relatively low level of monetary reserves did not permit the Yugoslav authorities to eliminate entirely the existing restrictions without fear of provoking new disequilibria in the economic development of the country.

14. Earlier this year consultations had taken place with the International Monetary Fund and contracting parties had been informed of these consultations and their results. In conclusion, he expressed the belief that the CONTRACTING PARTIES would approach the present consultations with their customary understanding of the situation of his country.

Discussion

15. The Committee thanked the representative of Yugoslavia for the full information supplied in the documentation and in his opening statement. The Committee also expressed its appreciation of the difficulties which had faced the Yugoslav authorities and welcomed the determined efforts which had been made to overcome these difficulties. In this connexion special reference was made to the measures taken within the framework of the comprehensive reform of the economic system which had been introduced in July 1965 which had been summarized by the representative of Yugoslavia in paragraph 10 above. The Committee noted that efforts had been made which were designed to enable Yugoslavia to move towards a system in which market laws could operate more freely and to play a larger part in the international division of labour. The introduction of the new Yugoslav customs tariff was also welcomed. Certain delegations underlined the importance of following through the important measures that had been taken, in particular by the progressive liberalization of imports as and when the balance-of-payments situation permitted.

16. One member noted that the proposed introduction of the new dinar which equalled one hundred old dinars had parallels in reforms recently carried out by other countries represented on the Committee and said that his country was sharing its experience in this respect with Yugoslavia. The representative of Yugoslavia expressed his appreciation.

17. Some members of the Committee noted that in his opening remarks the representative of Yugoslavia had stated that the present consultation was being carried out under Article XVIII of the General Agreement; it was the understanding of these members that no formal decision had, in fact, been taken on this matter. The representative of Yugoslavia agreed that no formal decision had been taken but pointed out that it was now an accepted practice that Yugoslavia should consult every second year as required under Article XVIII.



Balance-of-payments position and prospects

18. The material supplied to the Committee provided a clear picture of the position of and prospects for Yugoslavia's balance of payments. Certain additional points were raised with the representative of Yugoslavia.

19. In reply to questions, the representative of Yugoslavia confirmed that trade with the Eastern European countries had recently increased more rapidly than trade with Western Europe and that such trade was carried out entirely under bilateral agreements. These agreements had, however, been in existence for a very long time and the increase was attributable not to the existence of the agreement as such, but to improvements which had been made in the commodity lists contained in the agreements and especially to the interest shown by these countries in Yugoslav consumer goods and equipment. In reply to further related questions he also confirmed that one of the main factors limiting exports to Western European markets was the existence of import restrictions, particularly on certain agricultural products.

20. It was noted that as part of the economic reform steps would be taken to terminate bilateral payments agreements with Fund members. In answer to questions the representative of Yugoslavia recalled that one bilateral payments agreement, that with Austria, had recently been terminated but said that termination of the agreements did not depend on his Government alone. He emphasized that the inclusion of lists of commodities or quota figures in trade and payments agreements was purely indicative. The agreements were primarily an indication that the trade should as far as possible balance bilaterally. In answer to further questions he said that his Government was in favour of including a degree of multilateralization of payments in bilateral agreements. However, very few of its agreements in fact provided for any multilateralization of payments and his Government had experienced some difficulties in obtaining this from certain of its trading partners.

Alternative measures to restore equilibrium

21. The representative of Yugoslavia explained in reply to questions on the use of the interest rate as an alternative measure to restore equilibrium that in the past the nature of the economic system had prevented the full use of this tool. Measures had, however, recently been introduced to bring about the decentralization of the banking system and it was also hoped to create a certain form of capital market. This would make it possible in future to make fuller use of the interest rate.

System and methods of restriction

22. Some members of the Committee referred again to the programme of economic reform introduced in July of this year. It was noted that the International Monetary Fund Executive Board Decision of 25 July 1965 referred to the fact that the Yugoslav authorities would eliminate quantitative restrictions on imports of raw materials and spare parts and would liberalize imports of capital goods and to the fact that some liberalization would also be made in the field of invisible payments. Certain members of the Committee underlined the importance which they attached to these measures. It was also noted that in his opening remarks the representative of Yugoslavia had indicated that measures taken within the framework of the economic reform would be introduced gradually; members asked whether it was possible to provide more precision on the time-table which was envisaged.

23. The representative of Yugoslavia stressed that the reform was extremely comprehensive and would have its effect on all aspects of economic life in Yugoslavia. It was therefore to be expected that its implementation would take a certain time as to put all the measures connected with the reform into effect too rapidly might damage the economy. Certain instruments basic to the reform, such as the new parity rate, the customs tariff and the new fiscal and credit policies had already been introduced. The balance-of-payments situation and the

relatively low level of monetary reserves had prevented the full implementation of the liberalization measures to which reference had been made and it was the estimation of his Government that a period of two to three years might be necessary before the reform could be put into effect in full. Only three months had passed since the introduction of the reform and it was too early to estimate its effect; certain data, including data on foreign trade, indicated however that it was proceeding as originally planned.

24. In reply to questions on the restrictive licensing system, the representative of Yugoslavia said that the number of items in this category had been considerably reduced in recent years. Only nineteen non-essential items were at present subject to restrictive licensing and the list might be further reduced or abolished. These possibilities were now under consideration.

25. One member of the Committee noted that the number of enterprises engaged in foreign trade had increased and asked if there was an upper limit to this number. The representative of Yugoslavia pointed out that the relevant legislation imposed no such limit, simply specifying certain minimum requirements which had to be fulfilled before an enterprise could engage in foreign trade. Details would be circulated in the document to be presented in connexion with the Yugoslav request for full accession. In answer to enquiries the Yugoslav representative said that the system employed did not permit discrimination against new enterprises in the allocation of global quotas.

26. In answer to questions on the operation of the exchange contract machinery, the representative of Yugoslavia said that this had been introduced shortly before the economic reform to assist in the correction of the disequilibrium between imports and exports. He gave details of its operation and explained that under this system enterprises giving an undertaking to export a certain quantity of goods were accorded priority in the allocation of foreign exchange which, however, had to be used to import raw materials or other goods used in the production of the goods for export. The primary aim was to stimulate exports, but the system also had positive effects on the import side.

27. In reply to a question, the representative of Yugoslavia confirmed that it was the intention of his Government to use the customs tariff as the sole protective measure.

General

28. The Committee expressed its thanks to the representative of Yugoslavia for the full and frank answers given to the questions they had posed it and welcomed the measures taken by the Yugoslav authorities since the time of the last consultation in the Committee, designed to allow the freer play of the market mechanism and the more complete inclusion of Yugoslavia in the international division of labour, and wished the Yugoslav Government success in the implementation of the reform programme.

29. The representative of Yugoslavia thanked the members of the Committee for their understanding of the situation of his country and undertook to draw his Government's attention to the views that had been expressed.

ANNEX

International Monetary Fund Executive Board Decision  
Taken at the Conclusion of the Fund's Consultation  
with Yugoslavia on 23 July 1965

1. The Government of Yugoslavia has consulted the Fund under Article XIV, Section 4, of the Fund Agreement concerning the further retention of its transitional arrangements.
2. In 1964 economic expansion continued at a high rate. Real social product increased by 12 per cent and industrial production by 16 per cent, about the same as in 1963. Credit policy continued to be relatively easy until the middle of the year and this, together with institutional changes such as the creation of larger disposable resources in the hands of the economic organizations, provided stimulus to the expansion. Despite the impressive increase in production, inflationary pressures which had appeared in late 1963 gained in intensity throughout 1964, as both investment and personal incomes increased sharply. Prices and the cost of living rose significantly, and the balance of payments deficit on goods and services increased from \$143 million in 1963 to \$255 million in 1964. To restore stability, the authorities tightened credit policy in June and October 1964, and import restrictions were intensified to restrain the sharp increase in imports. The restrictive credit measures produced some results, but did not fully eliminate the pressures on resources which continued through the early months of 1965. The authorities concluded that in order to ensure the sustained growth of the economy, fundamental measures of economic reform would have to be undertaken. To stabilize the economy prior to the introduction of the reform, further restrictive measures affecting bank credit, government budgets, and investment were taken in March 1965. At the same time, to prevent speculative increases in prices, and to gain time for the implementation of the new measures, a temporary freeze was imposed on most prices.
3. The proposed economic reform is intended to correct price distortions inherited from the period when the economy was closely directed by administrative means and to increase reliance on the market mechanism. It involves a further reduction of the rôle of the political authorities in investment decisions and a substantial adjustment of the external restrictive system. It is expected that these measures will

lead to a more efficient utilization of resources and a strengthening of the balance of payments and thereby will help to sustain a high rate of growth. The Fund welcomes the reform proposals and emphasizes the need for utmost resolution in the pursuit of incomes, credit, and fiscal policies with a view to maintaining the stability of the economy without which the objectives of the reform could not be attained.

4. As part of the reform, the Yugoslav authorities will eliminate quantitative restrictions on imports of raw materials and spare parts, and will liberalize restrictions on imports of capital goods. Some liberalization will also be made in the field of invisible payments. Further, steps will be taken to terminate bilateral payments agreements with Fund members. These changes have an important rôle in ensuring the success of the reform, and the Fund urges the Yugoslav authorities to undertake further liberalization of restrictions as the balance of payments position improves.

5. In concluding the 1965 consultations, the Fund has no other comments to make on the transitional arrangements maintained by Yugoslavia.