

# GENERAL AGREEMENT ON TARIFFS AND TRADE

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

1. The Committee has conducted the 1963 consultation with Yugoslavia. The Committee had before it (a) a basic document prepared by the Yugoslav authorities (BOP/31/Rev.1\*), and (b) documents provided by the International Monetary Fund, as noted in paragraph 3 below.
2. In conducting the consultation the Committee followed the Plan for such consultations recommended by the CONTRACTING PARTIES (BISD, 7S/97-98). The consultation was completed on 9 December 1963. The present report summarizes the main points of discussion during the consultation.

### 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 with Yugoslavia. In accordance with the agreed procedure the representative of the Fund was invited to make a statement supplementing the Fund's document 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> relating to the last consultation with Yugoslavia under Article XIV of the Fund Agreement and the background material prepared in connection with that consultation.

"With respect to Part I of the Plan for Consultations, relating to balance of payments position and prospects, and with respect to Part III, relating to system and methods of the restrictions, the Fund calls the attention of the CONTRACTING PARTIES to the Executive Board decision of August 16, 1963, taken at the conclusion of its recent consultation with Yugoslavia, and particularly to paragraph 5 which reads as follows:

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\* English only (French text is numbered BOP/31).

<sup>1</sup> Annexed to the report.

'At the beginning of 1962 the special tourist rate was abolished, but the three categories of export premia established at the time of the exchange reform were retained unchanged. The import licensing system also remained unchanged in 1962, although certain import quotas were applied more restrictively. The Fund believes that a reduction in the reliance on bilateral agreements is feasible and urges the Government to take early steps toward the elimination of such agreements, especially those with Fund members. The Fund also hopes that as the improvement in the monetary reserves permits, Yugoslavia will further reduce its reliance on restrictions and discrimination.'

"On September 23, 1963, the Fund agreed to a drawing by the Government of Yugoslavia equivalent to \$30 million, and authorized a two-year postponement of a \$15 million repurchase by Yugoslavia which would have become due by January 2, 1964. In this way the Fund gave support to Yugoslavia's effort to maintain stability and to strengthen its external payments position, which had been subjected to new burdens resulting from the earthquake disaster at Skopje.

"With respect to Part II of the Plan for Consultations, relating to alternative measures to restore equilibrium, the Fund draws attention to the decision taken at the conclusion of its last Article XIV consultation with Yugoslavia. The Fund has no additional alternative measures to suggest at this time."

#### Opening statement by the representative of Yugoslavia

4. The representative of Yugoslavia noted that this was the first time that his country had had a consultation with the Committee on Balance-of-Payments Restrictions. Much of the information given by Yugoslavia in connexion with its application for Provisional Accession in 1962 was still relevant. He considered it useful, however, to provide a short outline of recent developments in the Yugoslav economy.

5. After a slight slowing down in the rate of growth of the Yugoslav economy during the first half of 1962, developments in the second half of that year and in the first half of 1963 were more favourable. In the first six months of 1963 production was even larger than had been anticipated. Production in the industrial sector had risen by 14 per cent in this period and it was considered likely that for the whole year the increase would be 15 per cent compared with an original estimate of 10 per cent. Activity in the construction industry had also increased markedly, giving in the first six months of 1963 an increase of 15 per cent as against an expected 2 per cent. It was calculated that the increase in the construction sector for the year would be 19 per cent above the 1962 figures. However, in the agricultural sector, it was unlikely that the estimated increase of 11 per cent in production would be achieved and that a 10 per cent figure was probable. In view of these developments it was estimated that the gross social product would increase during 1963 by 12 per cent instead of the 10 per cent planned.

6. It was noteworthy that of the expected 12 per cent increase in gross social product, only 4 per cent would be attributable to an increase in the labour force. The growth in labour productivity resulted from special incentives introduced by the authorities and from a more rational allocation of labour originating in the efforts made by Yugoslavia to integrate its economy more fully into the world economy.
7. The representative of Yugoslavia recalled that his Government had introduced a foreign exchange reform in 1961 whereby the multiple exchange practices previously in force had been eliminated. This reform, together with measures taken in the domestic economy, had helped to increase productivity and economic growth.
8. The Yugoslav authorities had recently made strenuous efforts to bring supply and demand in the economy into balance. In this connexion, the representative of Yugoslavia stated that the Federal and individual Republic Governments had, in 1963, introduced more balanced budgets. In the first half of 1963, the Federal budget showed a surplus of 84 billion dinars against a deficit of 45 billion dinars in the same period in 1962. As a result of the measures taken to achieve economic stability, prices had not risen in 1963 at the same rate as in the previous year. Retail prices of industrial products remained unchanged in the first six months of 1963 while prices of agricultural products showed an increase smaller than in preceding years.
9. Turning to his country's balance-of-payments position, the representative of Yugoslavia indicated that considerable progress had been made in the second half of 1962 and the first half of 1963 in reducing the size of the deficit in the Yugoslav balance of payments. Exports had increased in the second half of 1962 and this trend had continued in the first half of 1963. It was estimated that total exports for 1963 would amount to \$760 million and of this figure \$362 million, or 47 per cent, were effected in the first six months of the year, giving an increase in exports of 26 per cent in comparison with the same period of 1962. Imports had also shown a marked tendency to rise in the first six months of 1963 amounting, in this period, to \$527 million as compared with an estimated total import figure for 1963 of \$945 million. It had been estimated that the balance of payments for 1963 would show a current account deficit of about \$67 million. It was estimated that this amount would be covered by foreign borrowing and that it would, at the same time, be possible to increase reserves which were still very low.
10. The representative of Yugoslavia then dealt with the economic effects of the Skopje earthquake. It was estimated that the direct damage caused by the earthquake would amount to 750 billion dinars and that total production would decrease by about 20 billion dinars (1 per cent of the gross social product) in 1963 and by about the same amount in 1964, as a result of this disaster.

Moreover, the tasks of finding shelter for the inhabitants of Skopje and the rehabilitation of industry, schools, health and other public services would impose a burden on the Yugoslav economy of about 100 billion dinars in both 1963 and 1964. The greater part of this exceptional expenditure would have to be borne by the Yugoslav economy and people (by reductions in personal consumption and investment, by the issuing of a public loan and by the introduction of special taxes, etc.). It was, however, impossible for the Yugoslav economy to carry the whole burden alone without its being severely disrupted. For this reason, it would be necessary to obtain foreign aid to meet these exceptional circumstances. In this connexion the representative of Yugoslavia expressed the appreciation of his country for the relief received from abroad.

11. As a result of the earthquake, it would seem probable that instead of an estimated \$67 million deficit in the Yugoslav balance on current account the figure would amount to between \$130-\$140 million. This development would of course impose a restraint on further liberalization of imports. In this connexion, the representative of Yugoslavia stated that despite these unfavourable developments, his country had in September 1963, in accordance with its policy, decreased the number of restrictions by removing from the restricted list twenty-two items, mainly capital goods, representing between 30 to 40 per cent of total yearly average imports of capital goods. It was, he continued, the hope of his Government that conditions would soon be established for further improvements and simplifications of the import control system.

#### Balance-of-payments position and prospects

12. The Committee took note of the opening statement by the representative of Yugoslavia as well as the material provided by the IMF, which together gave a clear description of the position and prospects of Yugoslavia's balance of payments. Only a few points required clarification and these were discussed with the representative of Yugoslavia as noted below.

13. A member of the Committee enquired what the prospects were for Yugoslavia's gold and foreign exchange reserves in 1964. In reply, the representative of Yugoslavia emphasized that Yugoslavia's reserves were extremely low. In August 1963, they amounted to \$80 million, an amount insufficient to cover the cost of one month's imports. The position had improved slightly since that date and it was hoped that reserves would exceed \$100 million in the course of 1964.

14. A member of the Committee observed that the recent expansion of Yugoslavia's exports had been impressive. Exports of industrial products<sup>1</sup> were 28 per cent higher in 1962 than in 1961 and in the first six months of 1963, export earnings were 26 per cent higher than the same period of 1962. The representative of Yugoslavia stated that the Yugoslav authorities did not feel that this rate of increase could be maintained. The bulk of the increase in exports had been in the manufacturing sector. In 1962, exports of industrial products<sup>1</sup> amounted to \$543 million and in 1963 it was estimated that they would reach a total of \$602 million. On the other hand, exports of agricultural products were tending to level off mainly because of increased domestic demand.

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<sup>1</sup>Refers to all products except those of agriculture and forestry.

15. In reply to a question concerning the prospects for growth in receipts from invisibles and particularly tourism, the representative of Yugoslavia stated that his Government hoped to increase receipts from invisibles in the future. A growing source of earnings in this sector was that derived from remittances from Yugoslav workers abroad. It was expected that tourism would yield \$67 million in foreign exchange in 1963. In 1964, it was hoped that this figure would reach about \$90 million. To encourage the tourist industry, the Yugoslav Government had undertaken an investment programme in roads, aerodromes, hotels and other tourist facilities. The tourist industry was still not fully developed and it was considered that the full potentialities of the industry would only be realized in the next few years.

Alternative measures to restore equilibrium

16. In his opening statement the representative of Yugoslavia had mentioned that internal prices had remained relatively steady in 1963. Referring to this, members of the Committee asked about the policy of the Yugoslav Government in relation to agricultural prices and the effect of any price rise on agricultural production. In reply, the representative of Yugoslavia stated that agricultural prices in Yugoslavia were in the past low and had tended to lag behind those in the manufacturing sector. As a result of the relatively low price paid for agricultural products in the past, agricultural production had tended to stagnate. He cited, in this connexion, the fact that cattle population had actually declined. However, it was the policy of the Yugoslav Government to increase prices for agricultural products in order to stimulate production and to bring them into line with the prices of manufactured goods and international agricultural produce prices. A position had now been reached where agricultural prices were generally considered satisfactory. Yugoslav prices for wheat and maize were similar to those prevailing on the world market and for some other products were even higher than world prices. In the view of the Yugoslav Government, it was unlikely that the new prices for agricultural products would lead to over-production, although production had increased in the last year. In this connexion, he pointed out that Yugoslavia still imported a high proportion of its requirements of certain basic foodstuffs.

17. A member of the Committee noted that, at the time of the foreign exchange reform in 1961, Yugoslavia had introduced a system of subsidies on exports amounting to 10 per cent, 22 per cent or 32 per cent of the cost of production. He further observed that about 57 per cent of Yugoslavia's exports benefited from these subsidies and asked the representative of Yugoslavia for his views of their effects on exports. The representative of Yugoslavia explained that the subsidies had been introduced to offset the detrimental effect for Yugoslav exporters arising from the removal of multiple exchange rates in

the foreign exchange reform. The representative of Yugoslavia did not consider, however, that the rise in Yugoslavia's export earnings on manufactured goods could be attributed to the maintenance of the subsidies. Yugoslavia, he pointed out, was becoming more industrialized and as industrial production grew so it would be expected that exports of manufactures would increase.

18. Members of the Committee enquired whether the export subsidies would be removed in 1965 as had been earlier envisaged. In this connexion, they enquired whether it was the intention of the Yugoslav authorities to phase out the subsidies gradually and whether there existed any criterion for assessing the need for a subsidy in particular instances. In reply, the representative of Yugoslavia indicated that it was still his Government's intention to remove all export subsidies in 1965 if this proved practicable. He was not, however, in a position to give any firm undertaking on this point. The criterion employed in assessing the need for a subsidy was that of increased labour productivity. Thus, if it were found that labour productivity in the production of a particular commodity had, since the date of the introduction of the subsidy, increased to such an extent as to offset the effect of lower export realizations, the subsidy would be removed. In this connexion, the representative of Yugoslavia recalled that it was the general policy of his Government to bring its industrial and, generally speaking, its agricultural prices into line with world prices. However, only two years had elapsed since the 1961 foreign exchange reform and, partly as a result of unfavourable developments, it was still too early to forego the use of the subsidies.

#### System and methods of restrictions

19. A member of the Committee asked whether there was any limitation on the allocation of foreign exchange for the importation of goods listed as free importation items (Annex I of BOP/31/Rev.1). In reply, the representative of Yugoslavia indicated that all authorized enterprises could import such goods without such limitation from any source. In some cases, however, imports from countries with which Yugoslavia had bilateral payments agreements were restricted to a certain negotiated quota.

20. In connexion with importations under general licence, a member of the Committee enquired as to how the percentages fixed for individual enterprises were calculated. In reply, the representative of Yugoslavia stated that enterprises received an allocation on the basis of a percentage of the allocation to that enterprise during the previous year. The actual percentage depended on the type of business conducted. In amplification, the representative of Yugoslavia pointed out that it had been observed in the past that some enterprises had received allocations larger than they could employ. He also stressed that not all foreign currency available for importation under general licences was allocated to the individual enterprises so that there was a reserve with the authorized banks on which enterprises, needing to import more than was possible under their individual allocations, could draw.

21. A member of the Committee asked how quotas were allocated for those goods whose importation was subject to quota. The representative of Yugoslavia stated that, in fact, all allocations of quotas were agreed by the enterprises themselves and that, to date, the Federal Government had not needed to intervene. Replying to a further point, he stated that convertible currency quotas were entirely non-discriminatory but there were, in addition to these, quotas for bilateral sources of supply (see paragraph 24 below).

22. A member of the Committee asked how an authorized enterprise could obtain the necessary foreign exchange to make importations of those goods under restrictive licence. The representative of Yugoslavia stated that such foreign exchange could be obtained from general licence allocations or, less commonly, from entitlements resulting from exportation. Another member of the Committee asked what happened to goods removed from the restrictive list. The representative of Yugoslavia stated that such goods were then placed under general licence. In reply to a further question, he informed the Committee that goods subject to restrictive licence constituted about 1.8 per cent of Yugoslavia's import in 1962 and that of this percentage, about half would be capital goods.<sup>1</sup>

23. A member of the Committee observed that there appeared to be three ways of obtaining foreign exchange for the importation of equipment; viz. by means of contracts with authorized banks; by purchasing foreign exchange with dinar holdings in the form of depreciation funds; and in the form of foreign currency receipts from an individual enterprises' own exports.<sup>2</sup> He asked whether, in granting licences, for the importation of equipment, the authorities had introduced any system of priority related to the source of the foreign exchange. The representative of Yugoslavia replied that there was no system of priority.

24. Some members of the Committee recalled that the International Monetary Fund, in the Executive Board decision of 16 August 1963, expressed the belief that a reduction in the reliance on bilateral payments agreements by Yugoslavia was feasible and had urged the Yugoslav Government to take early steps towards the elimination of such agreements, especially those with Fund members. They asked what the prospects were for lessening the reliance on bilateral agreements by Yugoslavia. In his reply, the representative of Yugoslavia reminded the Committee that his country had close trading relationships with neighbouring countries in Eastern Europe which conducted their trade through State-trading mechanisms and with whom it was necessary to have bilateral agreements. It had

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<sup>1</sup>The representative of Yugoslavia informed the Committee that the list of items deleted from the list of imports subject to restrictive licence as set out on page 5 of BOP/31/Rev.1 should not include wrapping paper and packing paper which remained subject to restrictive licence.

<sup>2</sup>A full description is contained in pages 3 and 4 of BOP/31/Rev.1 under the heading "(g) Importation of equipment".

also been found necessary to enter into bilateral agreements with certain countries with whom Yugoslavia was trading for the first time. It was the policy of the Yugoslav Government to dispense with bilateral agreements as soon as this proved feasible. However, it had to be borne in mind that not all Yugoslavia's bilateral partners were prepared to terminate agreements. In the last twelve months, the bilateral agreements with Chile and Finland had been terminated.

25. A member of the Committee asked whether it would be possible for Yugoslavia to introduce greater element of flexibility into bilateral agreements in force. In particular he asked whether it would be possible for Yugoslavia to move away from the rigid non-convertible swing balance type of payments agreement. He pointed out in this connexion that a number of Yugoslavia's bilateral partners in Eastern Europe had recently announced a system of transferability of balances. The representative of Yugoslavia explained that Yugoslavia had attempted to depart somewhat from the rigidity imposed by strict non-convertibility of currency by having inserted, into a number of agreements a clause providing for the transferability of balances into convertible currency. On the question of transferability of balances accruing in the trade of Eastern European countries, he pointed out that the CMEA Bank had only just been created and it was perhaps too early to judge what success it would have in introducing transferability. He emphasized that, to a very great extent, bilateral agreements were necessitated by the need on the part of one or both partners to export goods at prices above world prices. It was the intention of the Yugoslav Government to ensure that trade conducted under bilateral agreements should progressively be carried out at prices which were related to world prices so that eventually the need for an agreement would fall away.

#### Effects of the restrictions

26. A member of the Committee enquired as to what effect the removal from the restrictive licence list of those items appearing on page 5 of BOP/31/Rev.1 had had on imports of these items. The representative of Yugoslavia replied that it was still too early to attempt to assess the effects of this liberalization move, but it was likely that such imports would increase.

#### General

27. The Committee thanked the representative of Yugoslavia for the full and frank answers he had provided to the questions they had posed. It was pleased to note the success that had met Yugoslavia's efforts to improve her exports and general economic situation following the foreign exchange reform of 1961. It welcomed the liberalization measures which Yugoslavia had introduced in the past

twelve months. The Committee expressed its sympathy to the representative of Yugoslavia over the Skopje earthquake and wished the Yugoslav authorities success in overcoming the severe setback to the Yugoslav economy brought about by this disaster. Finally, it expressed the hope that the Yugoslav Government would find it possible to proceed with a reduction in its import restrictions and particularly to dismantle discriminatory devices and to reduce reliance on bilateral agreements.

28. The representative of Yugoslavia thanked the members of the Committee for their understanding of the problems confronting Yugoslavia and undertook to draw his Government's attention to the views they had expressed.

ANNEX

International Monetary Fund Executive Board Decision  
Taken at the Conclusion of the Fund's Consultation  
with Yugoslavia on 16 August 1963

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 1961 there was a substantial slowdown in the rate of growth of the economy, partly because of the unfavourable harvest. However, the slowdown was also caused by weaknesses in certain institutional arrangements which favored sharp increases in personal incomes, a large credit expansion and tended to lessen the emphasis on productive investments. To correct these shortcomings, and to obtain an increased rate of growth, the Government took a series of measures in the spring of 1962, which included steps to improve the management of economic enterprises, to keep personal incomes within the limits set by improvements in productivity, to restrain non-directly productive investment, and to stimulate production and investment through an expansion of exports. These measures, which are being continued, had a beneficial effect; the real social product in 1962 rose by 5 per cent as against 4 per cent in 1961 and, in the first four months of 1963, the rate of growth has accelerated. The volume of fixed investment did not change between 1961 and 1962, while personal consumption rose slightly. Agricultural prices continued to rise in 1962, but industrial prices remained stable throughout the year. In 1962 a substantial deficit emerged in the budget of the Federal Government, amounting to Din 71 billion or some 12 per cent of total expenditures. This was partly offset by surpluses in the Republican budgets amounting to Din 28 billion. The Government deficit was financed by the central bank as also were some expenditures of the General Investment Fund. Largely as a result of these two factors, the money supply increased by 29 per cent in 1962, compared with 20 per cent in 1961.
3. In 1962 exports rose by 21.5 per cent to \$691 million while imports declined by 2 per cent to \$888 million. There was also a substantial improvement in net earnings from invisible transactions, especially tourism. The balance of payments deficit on goods and services account declined from \$285 million in 1961 to \$113 million in 1962. Net borrowing abroad exceeded this deficit and holdings of gold and convertible foreign exchange increased to \$88 million at the end of 1962, compared with \$42 million at the end of 1961. The largest expansion of exports occurred in the categories receiving the two highest export premia of 22 and 32 per cent on the settlement rate of Din 750 per US\$1. Since early 1962 exporters have also enjoyed a simpler procedure in the refund of internal turnover taxes.

4. The Fund notes the strengthening of the balance of payments achieved in 1962 and early 1963 and the steps taken by the Government to secure the further sustained growth of the economy in conditions of internal stability. It believes, however, that the situation needs careful watching, especially with regard to the possibility of an excessive credit expansion leading to further price and cost rises. It is also important that the Government's policy of achieving a balance in its budget should be pursued with determination. A careful financial policy, in the view of the Fund, would facilitate the Government's efforts to organize the economy in a manner conducive to the most effective utilization of available resources and the achievement of external balance.

5. At the beginning of 1962 the special tourist rate was abolished, but the three categories of export premia established at the time of the exchange reform were retained unchanged. The import licensing system also remained unchanged in 1962, although certain import quotas were applied more restrictively. The Fund believes that a reduction in the reliance on bilateral agreements is feasible and urges the Government to take early steps toward the elimination of such agreements, especially those with Fund members. The Fund also hopes that as the improvement in the monetary reserves permits, Yugoslavia will further reduce its reliance on restrictions and discrimination.

6. In concluding the 1962 consultations, the Fund has no other comments to make on the transitional arrangements maintained by Yugoslavia.