

GENERAL AGREEMENT ON TARIFFS AND TRADE

Limited Distribution

Committee on Balance-of-Payments Restrictions

TRADE ASPECTS OF THE YUGOSLAV FOREIGN EXCHANGE ALLOCATION SYSTEM

Secretariat Background Paper

Addendum

1. In its report on the 1981 consultation with Yugoslavia (BOP/R/122), the Committee on Balance-of-Payments Restrictions asked the secretariat "to prepare, in collaboration with the Yugoslav authorities and in consultation with the International Monetary Fund, a factual addendum to the secretariat background paper (BOP/W/57) describing the trade aspects of the Yugoslav exchange allocation system".

2. The present paper, prepared in response to that request, was originally drafted in 1982 following a secretariat mission to Yugoslavia. Since then, the exchange allocation system has been modified and the importance of republican and provincial bodies in the process has considerably diminished. This paper thus describes both the system in effect up to 1982 and the modifications in force since 1983.

I. The institutional framework of the Yugoslav exchange allocation and import systems

3. In 1974, Yugoslavia adopted a new constitution which largely replaced the regulatory powers of the state by a system of co-ordination among enterprises and regions. The role of the state in economic affairs became residual: it is now only to establish the legal framework for decision-making, to decide on issues that cannot be resolved through self-management, and to act in situations of disruption or crisis. The purpose of these constitutional changes was to extend the principle of self-management, which until then had been applied only to relations within enterprises, to economic policy making. The new constitution was implemented in the area of international trade and exchange relations by two laws passed in 1977: the Law on Trade in Goods and Services with Foreign Countries, governing export and import policy, and the Law on Foreign Exchange Operations and Foreign Credit Relations, governing the acquisition and disposal of foreign exchange.

(a) Operation of "self-management" in Yugoslavia's foreign trade and exchange system

4. The functioning of the foreign trade and exchange mechanism cannot be understood without some knowledge of the Yugoslav economic system. The smallest entity in the Yugoslav economic system is the "Basic Organization of Associated Labour" (BOAL), a production unit within an enterprise

generating a technically and economically identifiable output. BOALs generally consist of 50 to 500 workers and most enterprises are made up of several BOALs. The BOALs co-operating in one enterprise are separate legal entities with their own balance sheets and income statements. They retain permanent control over the investment resources they have generated and can, under certain circumstances, split off from the enterprise to join another enterprise or to create a separate new enterprise. Groups of BOALs can be formed by association under self-management agreements; as such, they take joint business risks, produce joint income, and act as agents in foreign trade. Foreign exchange belongs to the organizations of associated labour which participate in the production of exported goods or services; foreign exchange realized by groups of BOALs is allocated among the participating BOALs (see paragraph 13 below).

5. The BOALs within an enterprise, and in many instances enterprises themselves, are not linked through a competitive market but rather through mutually agreed contracts reflecting medium-term plans. Prices in these contracts are established on the basis of total costs of production, including the agreed level of planned personal incomes. These are not, therefore, necessarily in line with competitive market conditions. Prices for some basic commodities are set by decree. For most consumer goods and minor industrial intermediate goods, price formation is in principle left to the producing enterprises, but in recent years varying degrees of price control were frequently applied.

6. Supply and demand in the market is organized to a large extent through a unique system of planning, often referred to as "self-management planning". Unlike the process of planning in a centrally planned economy, planning in Yugoslavia is carried out "bottom-up", that is, it starts from the expectations and goals of the enterprises and Communes rather than those of a central planning authority. In contrast to the system of indicative planning in mixed economies, Yugoslav enterprises and Communes must by law participate in the planning process. Unlike individual enterprises' plans in market economies, which are generally drawn up without knowledge of plans of other enterprises, Yugoslav enterprises that are either vertically linked or compete on the same market are obliged to exchange information on their respective plans and to "harmonize" them. The government interferes in this planning process only by setting certain macro-economic parameters to be taken into account by all planning agents. The government also acts as arbiter if deadlocks arise in the planning process.

7. In the area of domestic economic activities the main fora for this planning process are the sectoral and branch Associations, to which all enterprises must belong, and the Chambers of Economy formed by these Associations at the republican or regional levels. In the area of foreign economic relations the main fora of self-management planning are the national and regional Communities of Interest for Foreign Economic Relations (CIFERs), established under the 1977 Law on Foreign Exchange Operations and Foreign Credit Relations. All organizations earning or using foreign exchange participate in regional CIFERs. Up to 1982, the regional CIFERs were principally responsible for planning the use and

allocation of foreign exchange within the annual Resolution on Foreign Exchange Policy, on the basis of uniform, officially published criteria agreed by them within the Yugoslav CIFER. The result of the planning and co-ordination efforts is laid down in the unique legal instruments of Social Compacts and Self-Management Agreements. The Chambers of Economy participate in the conclusion of Social Compacts regulating general economic matters, such as principles and criteria for price formation, for employment policies and for the distribution of enterprise income between personal income and accumulation. Social compacts have the force of law and are binding upon signatories. Many such compacts, however, do not envisage sanctions, so that adherence is ensured through broader social pressures. The regional CIFERs co-ordinate their activities in the nationwide Yugoslav CIFER where they develop common policies and procedures for dealing with deviations from such common policies.

(b) Export and import policy

8. The Law on Trade in Goods and Services with Foreign Countries¹, as amended in 1978 and 1982, establishes the institutional framework for the formulation and implementation of the export and import policy. Under this Law, the long-term (five-year) programme regulating exports and imports is established within a "Social Compact" concluded among the Federal Executive Council, Executive Councils in the Republics and Provinces, the Chamber of Economy of Yugoslavia and its General Associations, the Yugoslav and regional CIFERs and the Federal Community for Prices. This programme, in compliance with the Social Development Plan of Yugoslavia, defines the main objectives and criteria regulating foreign trade and establishes quotas for exports and imports. Decisions on the volume of quotas, the specific goods which are to be imported within quotas, the use of quotas over time and the allocation of these goods among domestic economic organizations are made jointly by representatives of all the enterprises concerned. In exceptional cases, in order to ensure market stability and to ensure sufficient domestic supplies, as well as to remove major disruptions in production and consumption of certain goods, the Federal Executive Council of Yugoslavia (FEC) may set time-limited quotas for imports or exports and determine their allocation.

(c) The right to engage in foreign trade

(i) Organizations

9. Only economic organizations, not private persons, may engage in foreign trade for commercial purposes. An organization wishing to participate in foreign trade must register for this purpose. In addition to organizations specialized in foreign trade, most major industrial organizations have registered (in total about 1,300 organizations). To be eligible for registration an organization must have a qualified professional staff. The standards to be met are set by the Yugoslav Chamber of Economy.

¹Official Gazette of the Socialist Federal Republic of Yugoslavia, (SFRY) Nos. 15/77, 17/78, 5/82.

10. Organizations specializing in foreign trade may only register if they have concluded long-term and large-scale "self management agreements on the association of labour and resources" with manufacturing organizations, under which the trading and manufacturing organizations jointly share the gains and losses from such operations. The co-operative agreements must cover a period of at least five years. Foreign trade organizations must earn at least 50 per cent of their annual income under such agreements. The requirement of close association between trading and producing organizations is to ensure that foreign exchange receipts - and any scarcity rents associated with them - accrue not only to trading houses but also to the producing organizations, thereby stimulating them to reorient their production towards export markets.

(ii) Private individuals

11. Private individuals may import goods for their own use or for the use of close relatives residing with them. Self-employed Yugoslav nationals may import machinery for small farms, equipment for handicraft production and manufacturing components up to certain maximum amounts. However, private individuals may not engage in foreign trade as a public activity. Individuals pay customs and other duties at the same rate as organizations of associated labour. Exceptions are private imports for personal use or for use in small industries, of a value up to 30,000 dinars, as published in an official list, for which individuals pay customs duties at a uniform rate of 15 per cent, even where the normal rate is higher. Individuals pay excise tax on the value of imported items at the same rate which applies to the equivalent domestically produced item.

II. Foreign exchange operations

(a) The right to engage in foreign exchange operations

(i) Organizations

12. The Law on Foreign Exchange Operations and Foreign Credit Relations, which extended the principle of self-management to international financial matters, established new criteria for the acquisition and disposition of foreign exchange. Previously, exporting organizations could retain part of their exchange receipts, which could then be spent freely on imports without import restrictions or licensing procedures. The retention quotas were highly valued because with them exporters obtained the scarcity rents associated with an over-valued exchange rate and import restrictions. The retention quotas favoured the final exporter over the organizations that contributed indirectly to foreign exchange earnings and they were therefore gradually reduced in the 1970's and abolished in 1977.

13. The system established in 1977 is based on the broad principle that the rights to foreign exchange earned through exports of goods and services belong jointly to all the entities that participated in the production of those goods and services. If the foreign exchange is earned through the independent performance of an organization of associated labour, it belongs

to that organization. In the more usual case, in which an organization exports goods and services to the production of which other organizations have contributed, all the organizations principally involved must conclude a self-management agreement providing for a sharing of the foreign exchange earnings, generally in accordance with the value added by each organization.

14. Proceeds from exports must normally be repatriated within 90 days and credited to a foreign exchange sight-deposit account with an authorized bank of the organization's choice. For 1982, the repatriation period was shortened to 60 days. With effect from 1 January 1983, the 90 days period was again restored.

(ii) Private individuals

15. While organizations are subject to various constraints in the use of foreign exchange, private citizens are free in their disposal of foreign exchange received from abroad or brought into Yugoslavia. They may sell it to an authorized bank, put it into a foreign exchange account or foreign exchange savings deposit, purchase securities with it or spend it on imports. Yugoslav workers abroad who sell foreign exchange to an authorized bank may use the dinar proceeds to buy locally manufactured goods free of turnover tax. Up to 1 January 1984, the foreign exchange accounts bore interest in foreign exchange (or in dinars, if the depositor wished). From 1 January 1984, foreign exchange accounts of Yugoslav resident citizens bear interest only in dinars; interest denominated in foreign exchange may accrue only to foreign exchange accounts held by Yugoslav citizens temporarily employed abroad, during their stay abroad and at the request of the depositor. All such foreign exchange accounts are guaranteed by the Federation and benefit from strict bank secrecy regulations. Because of the relatively large number of Yugoslavs working abroad, the amount of foreign exchange covered by these regulations is quite substantial. In 1981, workers' and emigrants' remittances amounted to US\$5,100 million or the equivalent of one-third of Yugoslavia's total import expenditures of US\$15,800 million. Private individuals thus in principle enjoy much greater freedom in their use of foreign exchange for import purposes than do organizations of associated labour. However, in 1982 provisions were introduced for a deposit of Dinars 5,000 for the first trip, increasing by Dinars 2,000 for each successive trip, to be made by Yugoslav nationals travelling abroad, in order to reduce private imports of consumer goods. Since 1 January 1984, no deposit is required for the first trip abroad: the deposit requirement is applied with effect from the second journey.

(b) The formulation of foreign exchange policy

16. For each year the Federal Assembly adopts a joint foreign exchange policy for the republics and provinces, together with the joint economic policy. The joint foreign exchange policy covers not only financial matters, such as exchange rates, foreign exchange allocation and foreign credits, but also trade matters, such as import policy, protection of domestic industry and export promotion. To provide a factual basis for the formulation of foreign exchange policy, all economic organizations earning or spending foreign exchange submit projections of their foreign exchange receipts and expenditures to their local CIFERs.

17. Up to 1982, each republican or provincial CIFER drew up its own foreign exchange projections and policy proposals on the basis of the information provided by the economic organizations. Then within the federal CIFER, a joint balance-of-payments projection and joint policy proposals for the whole of Yugoslavia are drawn up as the main input in the formulation of the joint foreign exchange policy by the Federal Assembly. The 1982 foreign exchange policy was based on the following projections of foreign exchange receipts and expenditures of the republics and provinces:

FOREIGN EXCHANGE RECEIPTS AND PAYMENTS PLANNED FOR 1982
(BILLIONS OF DINARS)¹

	<u>Receipts</u>	<u>Payments</u>	<u>Balance</u>
Bosnia & Hercegovina	91.9	90.5	1.4
Crna Gora	11.6	15.5	-3.9
Croatia	177.5	155.8	21.6
Macedonia	30.7	37.7	-7.0
Slovenia	112.1	103.7	8.4
Serbia	214.2	215.8	-1.6
Serbia proper	160.8	144.4	16.4
Kosovo	13.4	19.4	-6.0
Voivodina	39.9	51.9	-12.0
Central Federation	7.3	40.0	-32.6
Total Yugoslavia	645.7	659.3	-13.6

¹ Calculated by Yugoslav authorities at an exchange rate of 1 US\$ to 27.30 dinars.

18. The overriding objective of the 1982 exchange policy was to reduce the current account deficit to US\$500 million from the US\$1.4 billion recorded in 1981. External sector policies were directed at promoting a 12 per cent increase of exports to the convertible currency area. On the import side, priority was to be given to imports of raw materials and intermediate goods, especially those needed by the export industries.

19. As a result of an amendment to the Law on Foreign Exchange Operations and Foreign Credit Relations at the end of 1982 (Official Gazette of the SFRY No.77/82), the practice of establishing individual payments and foreign exchange balances for each of the republics and provinces was ended. Regional CIFERs are thus no longer regulating mechanisms in planning the use of foreign exchange.

(c) The implementation of foreign exchange policy

20. Up to 1982, the implementation of foreign exchange policy was the responsibility of the regional CIFERs. They monitored the realization of payments projections and kept the competent authorities informed of any deviations from these. In the event of deviation, the competent authority of the republic or province - in general the local CIFER - had to take corrective actions. The Federal Executive Council, in agreement with the regional authorities and after having heard the opinion of the national CIFER, could lay down general criteria for the corrective actions to be taken. As a general guideline, it was decided in 1979 that corrective measures, effective in the next quarter, would be taken as soon as the balance for the republic or province for one quarter was expected to fall short of the projected level by more than 5 per cent. It was also established that 70 per cent of any unplanned excess in foreign exchange earnings could be used to raise the level of imports in the republic or province. The remaining 30 per cent was, in principle, to be transferred to the Federation for national purposes, including payments for oil and other energy-related imports, servicing the debts of republics and provinces whose level of foreign indebtedness was above the Yugoslav average, reduction of the overall Yugoslav deficit and replenishment of foreign exchange reserves. In 1979, this proportion was, however, solely used to reduce the overall deficit. In 1982, the proportion to be transferred was increased to a minimum level of 37.9 per cent; 17 per cent for payments for energy imports; 5 per cent for the foreign exchange expenditures of the Federation and, from May 1982, a further 15.9 per cent for a joint pool of foreign exchange (solidarity fund) for the more indebted republics and provinces. Foreign exchange earnings on foreign investments, barter and co-operation deals, are not taken into account in calculating the amount to be transferred to the Federation.

21. Up to 1982, each regional CIFER also distributed the foreign exchange remaining after the transfer to the Federation was made, among its members through self-management agreements. The CIFERs first had to agree on the proportion of foreign exchange earnings the exporting organizations could keep and the proportion which they should make available to organizations which did not generate sufficient foreign exchange to meet their import needs. Thus in 1982, payment of foreign debt was a priority and the responsibility for this was divided between debtor organizations (primarily responsible) and (secondarily) all other entities in the same republic or province. Exporting organizations' retention rights thus depended on the total value of foreign obligations by all organizations in the republic or province. No republic or province had retention rights of less than 23 per cent in 1982.

22. Shortfalls frequently arose in the early months of the year and were then corrected by cuts in exchange allocation in the later months. In the second half of 1981, in order to keep export and import within planned proportions, regional communities of interest had to reduce their payments to the amount of their foreign exchange inflow. In 1982, the possibilities for economic organizations to make payments abroad depended on their actual foreign exchange retentions. Lower exports than planned resulted in lower import possibilities. In global terms, imports in 1982 were some 8.2 per

cent lower than in 1981 in U.S. dollar value. The practice of cutting exchange allocations in the later months of the year to correct overruns in the earlier months appears to have encouraged economic organizations to spend their annual exchange allotments as early in the year as possible.

23. In April 1983, Yugoslavia introduced new Uniform Criteria for the distribution of foreign exchange, in an amendment to the Law on Foreign Exchange Operations and Foreign Credit Relations, with the aim of creating a strict link between the volume of exports and imports and of establishing a greater export orientation in the Yugoslav economy. Under these criteria, any exporting organization has the right of access to foreign exchange, subject to strict conditions. The proportion of foreign exchange to be surrendered to the federal government, to National Bank of Yugoslavia reserves, to the energy-import fund, and to the republics or autonomous regions was raised to 40 per cent. Defined formulae were also established to calculate the percentages of total expenditure which could be used for repayment of foreign debts or for the import of goods and services, based on the ratio between obligations in 1983 and foreign exchange in 1982 plus 20 per cent in the case of debt repayments, and on the ratio between 1981/82 imports and 1981/82 export receipts plus 25 per cent, in the case of imports. Extra revenue could be allocated for imports and foreign borrowing depending on the percentage of exports to convertible currency countries made by each enterprise.

24. The Uniform Criteria provide for associations of BOALs to determine (not on a regional basis but on an industry basis) the proportions of their foreign exchange allocation which should be distributed to each participating organization for its import requirements. All such agreements must be approved by the CIFER of Yugoslavia. Foreign exchange allowances for needs of individual organizations of associated labour classified within activity sectors could be adjusted upwards provided that the total for all such organizations did not exceed the total foreign exchange held by the sector as a whole. Foreign exchange could thus be reallocated within sectors to meet mutually recognized needs. However, because of problems in defining activities and classifying organizations of associated labour into particular activity sectors, this element of the provisions of the Uniform Criteria was only partly applied in 1983.

25. Modified criteria introduced in 1984 provide for a higher proportion (54.1 per cent) of total foreign exchange revenue to be set aside for general requirements. These include imports of petroleum, drugs and raw materials for production of medicaments, detergents, fertilizers and pesticides, protein animal feed, sugar, sugar beet, edible oils and coffee, which are centrally controlled. Production requirements must be met by associations of BOALs from the remaining 45.9 per cent. The formulae mentioned above by which such associations should calculate the amount of foreign exchange available to them for imports and debt repayment were revised, and were for 1984 based on the ratio between the value of exports in 1982/83 and imports plus foreign loans in the same year, adjusted by the projected growth of trade in 1984. In practice, this means that to be able to import the same value of products as in 1982/83, an increase of 11 per cent in exports has to be realized. Exporting organizations which earn a surplus of foreign exchange over and above their jointly agreed import and

debt servicing requirements must sell this amount to an authorized bank to be put on the market. BOALs which do not earn foreign exchange, or earn an insufficient amount to meet their import needs, may purchase foreign exchange on the market in proportion to the total national foreign exchange inflow and the volume of foreign exchange available on the market. Some large industrial groups or sectoral associations of industry (for example, the textile industry or steel industry associations) are able to benefit from extra incentives to increase exports to convertible currency areas. Any increase over 20 per cent in hard-currency export earnings by these groups may, subject to the general taxation requirement, be retained for their own use and is not required to be resold to a bank for putting on the market.

(d) Relationship between foreign exchange and trade régimes

26. Foreign exchange available for imports can be used within the bounds of the import régime established through the consultative process described in Paragraph 9. No special permission is needed to import liberalized goods, which account for 4,542 out of a total of 5,886 tariff lines. Goods not on the liberalized list can only be imported within quota allotments or under import licences. Products subject to quota have been notified to the GATT Group on Non-Tariff Measures, and are included in document NTM/W/6/Rev.1. Products subject to import licences have also been notified by Yugoslavia to GATT and are listed in document L/5146/Rev.1.

27. Import quotas, which may be determined in terms of quantity or value, are intended to safeguard the development of domestic industry. The Yugoslav authorities in their notification to the Group on Quantitative Restrictions and Other Non-Tariff Measures refer to Article XVIII:C. Their volume depends on the level of planned production, consumption and export of products for which import quotas are required. In accordance with the Law on Trade in Goods and Services with Foreign Countries, the products which may be imported within quotas, as well as the value and timing of the quota, are determined by the self-management agreements concluded within general economic associations and the Chamber of Economy of Yugoslavia, among the organizations producing, consuming, exporting or importing the products in question. Distribution of the quotas among enterprises is carried out on the basis of these self-management agreements. In this way, all concerned organizations which participate in the self-management agreement are aware of the value of the quotas and their distribution. Quotas may be determined in terms of quantity or value.

28. The list of products whose import is subject to import licence, is approved by the Federal Executive Council. Licences are granted by the Federal Secretariat for Foreign Trade. This list includes products covered by international commodity agreements, narcotics, arms, explosives and ammunition.

29. Foreign exchange may be either (i) earned abroad, (ii) obtained through co-operative arrangements with other organizations, or (iii) purchased on the official foreign exchange market, in which authorised banks and the National Bank of Yugoslavia take part to settle foreign exchange transactions through interbank meetings.

30. In 1981 and 1982, no such interbank meeting was held within the foreign exchange market, because economic organizations were in general not interested in selling foreign exchange on the foreign exchange market, and this was the main reason why the Interbank Meeting was dissolved. Economic organizations used their foreign exchange for arrangements with other organizations which needed foreign exchange to honour their foreign obligations and in their common interest in production and export. In certain cases, contrary to the regulations in force, arrangements were concluded which allowed the organization which possessed foreign exchange to earn the dinar equivalent above the official exchange rate.

31. New regulations brought into effect in 1984 require BOALs to sell to authorized banks any foreign exchange earned over and above their jointly agreed production requirements. This foreign exchange is then put on the market. The type of arrangement referred to above between organizations is no longer permissible.

III. Trade effects of the foreign exchange allocation system

(a) Effects on imports

32. Up to and including 1982, the members of regional CIFERs were able, through their joint action, to determine Yugoslavia's global import priorities and to exert a primary influence on the level of imports through the allocation of foreign exchange within self-management agreements. In practice, the individual CIFERs acted in different ways; some assigned priority only to imports of raw materials for export goods; others simply established the total value of exchange funds available for imports without establishing precise priorities. Decisions of CIFERs were not published; only CIFER members, through internal bulletins, were officially informed of them. As of 1983, regional CIFERs no longer have responsibility for such decisions. Global import priorities are based on the Uniform Criteria adopted by the Yugoslav CIFER, published in the Official Gazette.

33. In the period up to 1982, CIFERs thus used their exclusive foreign exchange allocation rights both to ensure that the region's global foreign exchange expenditures were compatible with its export earnings and to determine the imports of raw materials, intermediate products, capital goods and consumer goods. In conditions of foreign exchange scarcity, regional CIFERs were able to allot priority to raw materials and intermediate goods as against less "vital" consumer goods. This indirectly protected individual BOALs which manufactured consumer goods in question.

34. To what extent this autonomy was used to direct the pattern of imports away from what it would have been under a market allocation of foreign exchange is difficult to assess. The CIFER decisions are in principle not imposed on enterprises but reflect the plans of the enterprises, brought into harmony with one another and determined in relation to the regions' foreign exchange constraints. The difference between the CIFERs' allocation of foreign exchange and a market allocation therefore need not necessarily be great. However, it appears extremely unlikely that the

pattern of imports resulting from the process of discussion and negotiation within a CIFER is the same as the pattern of imports resulting from the sale of foreign exchange to the highest bidder.

35. The CIFERs are part of the Yugoslav system of self-management planning. One of their main functions is to provide a forum and procedures to integrate import plans and production plans of all enterprises in a region. The CIFERs' exchange allocations therefore tend to reflect co-ordinated medium-term plans. This will attenuate and delay the effects of short-term changes in world market conditions on import-competing industries in Yugoslavia. Organizations of producers, importers and consumers (including final consumers) are represented in the regional CIFERs. However, given the fact that manufacturing organizations receive the major portion of foreign exchange earnings, trade organizations in all regional CIFERs were entitled to narrower foreign currency allocations for imports. This affects most severely the market for consumer goods. For vital products (food, medicines and similar) a certain percentage of foreign exchange is, as mentioned in Paragraph 25 above, specifically earmarked and the supplier may retain the total amount of its foreign exchange earnings. The problem of effectively taking consumer interests into account is, of course, common to all countries, and so is the problem of import barriers rising with the degree of manufacturing. However, these problems appear to be accentuated in Yugoslavia because they seem to have manifested themselves not only in the tariff and quota régime at the federal level, but in addition (at least up to 1982) in the CIFER decisions at the republican and provincial levels.

36. In the period up to 1982, protective action at the regional level could, in certain circumstances, be nullified by the actions of other CIFERs, because there are no formal barriers to trade among the regions of Yugoslavia. However, a number of factors discouraged such trade; including certain aspects of the exchange allocation system itself. It was not normally possible for BOALs which held foreign exchange retention rights in excess of their own requirements to import raw materials or equipment for the purpose of reselling it to other BOALs which lacked foreign exchange. The economic equivalent of such a resale could of course be achieved through a self-management agreement between the two BOALs. In principle, organizations were able to conclude co-operation agreements and pool their foreign exchange with organizations in any part of the country. Thus a BOAL with foreign exchange available should have been able to receive the most attractive co-operation offers from organizations in regions in which foreign exchange was most scarce, and this mechanism should in principle have compensated for regional differences in the overall availability of foreign exchange or in the allocation of foreign exchange for specific import categories. While such short-term co-operation agreements were concluded among BOALs from different regions of the country, and did not require the approval of regional CIFERs, there is no doubt that in practice the CIFERs exerted an influence on the conclusion of such agreements and mainly encouraged those which helped to solve foreign exchange problems within the region in question.

37. If, as a result of the CIFERs' exchange allocation decisions, particular products were no longer (or only in reduced quantities) available in any part of Yugoslavia, private imports of this product should in principle increase. This could, at least partially, offset restrictive effects of CIFER decisions on imports of consumer products. However, the fact that private citizens may use foreign exchange at their disposal only for imports for their personal use or the use of close relatives residing with them, together with the deposits to be made when travelling abroad, discourages the import of consumer goods by private individuals.

38. The changes in the regulations for foreign exchange made in 1983 and 1984 should have helped to alleviate the problem of regional shortages of foreign exchange and, in general, make the import system more flexible. However, the increasing proportion of foreign exchange earnings retained for national purposes could mean that the overall funds available to organizations for imports would, at least relatively, diminish. It remains, in addition, the case that the overall planning process for import policy leading to licensing and quota systems, which operates in tandem with the exchange allocation policy, could tend to act against the import of goods competing with local production.

(b) Effects on exports

39. In the period up to 1982, the regional CIFERs influenced the pattern of exports mainly by allocating exchange retention rights. An exchange retention right could convey a profit if, and to the extent that, the scarcity value of the foreign exchange exceeded the value set by the official exchange rate, which was the case for a number of years in Yugoslavia. Granting the right to retain foreign exchange could therefore have effects similar to a direct subsidy. Since the CIFER determined, within limits, the percentage of foreign exchange earnings which a particular exporting enterprise might retain, it could influence the pattern of exports. (It can be argued that the subsidy element in the retention rights more or less compensated exporters for the handicap imposed by the absence of a market-determined exchange rate; that consideration does not, however, alter the above conclusion.)

40. The system of foreign exchange allocation tended to encourage organizations to engage in barter arrangements. By exporting through a barter arrangement, an organization could avoid the need to obtain a foreign exchange allocation. It could also avoid having to forego part of the benefits arising from exporting by having to transfer foreign exchange to the Federation and local governments. Imports entering Yugoslavia under barter deals are subject to the same customs duties as any others. The approval granted by the competent authority for barter arrangements provided an opportunity for importation of goods subject to quotas, outside the quota allotment, which was otherwise determined and allocated within the general associations of the Yugoslav economy. Barter deals became attractive in the course of 1982 and 1983, because the organizations of associated labour had the possibility of importing more, in relation to their exports, than in normal trade. Allocation of foreign exchange in case of barter deals was not the same in amount as in regular trade deals. The import/export ratio in barter deals, approved by the competent federal authority, was 1:1 in quantity terms, provided however that the value of

Yugoslav exports was somewhat higher. Compensatory arrangements require the approval by the Federal Secretariat for Foreign Trade. An arrangement may be approved, inter alia, if it ensures the sale of certain goods the export of which has become difficult, exports to new markets, or a more balanced trade with foreign countries (cf. L/5435 for the 1982 Decision on Compensatory Arrangements with Foreign Countries). The incentives to barter arising from the exchange allocation system combined with these criteria for the approval of barter arrangements, would normally result in a different geographic and product pattern of exports than would exist under a functioning foreign exchange market.

(c) Effects on resource allocation in Yugoslavia

41. The system of planning imports and allocating foreign exchange imposes an unusually heavy administrative burden on an organization wishing to engage in foreign trade. To obtain import rights, it has to participate actively in CIPHER meetings. It has to prepare projections of its exports and imports for each year and, since the exchange allocations are based on these projections, it is largely bound by them since imports deviating from the original plans - if permitted - require additional administrative steps. This introduces a certain rigidity in the import plans of the organization. The costs of such rigidity obviously are much higher in a constantly changing trading environment than in one which is stable and predictable. The import rights of the organization are normally dependent on the realization of its export plans. Fluctuations in its export earnings are thereby translated into variations in its import possibilities. This creates additional uncertainty.

42. The present foreign exchange allocation system operates at two levels, on the basis of the abovementioned uniform criteria. Overall foreign exchange earnings are allocated on an agreed basis, following negotiations, among the sectoral industrial associations or large industrial entities. Within these groupings, foreign exchange is again allocated to individual enterprises or associations by a process of negotiations among the bodies concerned pursuant to the relevant self-management agreements. The rôle of CIPHERs in relation to the external sector is not to distribute foreign exchange, but to monitor the realization of import and export plans.

43. Many of these administrative costs do not increase in proportion to the size of the organization or the size of the individual transaction. The system therefore favours trade by large organizations engaging in large or routine transactions. In other words, the overall administrative burdens increase the cost of trading (and hence reduce the organizations' export potential), to a relatively greater extent for small and innovative organizations.

44. Since most exports represent the combined work of several organizations, it is also necessary to follow the complex regulations governing the allocation of foreign exchange among them. If the exporting organization has many suppliers of inputs, the negotiation of the exchange distribution agreement can be time-consuming and costly. Moreover, the foreign exchange which the organization is allowed to retain but does not need cannot simply be sold to the highest bidder; the organization can realize the true scarcity value of its foreign exchange holding only by

concluding long-term and large-scale co-operation agreements with other organizations, which again may be very time-consuming. This could be avoided if the foreign exchange market were functioning as foreseen in the Law on Foreign Exchange Operations and Foreign Credit Relations. In particular, if foreign exchange could be sold and bought freely, the suppliers of inputs would see no advantage in being paid in foreign exchange rather than dinars and they would therefore not insist on separate identification of their part in the export receipts. The overall effect of the administrative costs associated with foreign exchange allocation is to reduce the level of both imports and exports. This in turn reduces the extent to which Yugoslavia can take advantage of an international division of labour to increase the efficiency with which national resources are employed. The measures introduced in 1984 to revitalize the foreign exchange market are, therefore, a step in the right direction.

Conclusions

45. The changes made to the foreign exchange allocation system in 1983 and 1984 seem to be intended to lead to a better matching of real needs and available imported inputs and to avoid regional scarcities or imbalances due to the lack of correspondence between the geographical and sectoral distribution of production. Joint planning of imports on an industrial basis rather than a regional basis should permit better allocation of resources to enterprises which may account for a relatively small part of the output of a particular region. However, the tightening up of foreign exchange policy, with overall import possibilities now strictly tied to export growth and stricter limitations on imports of consumer goods, could be expected to continue to bias the structure of imports in favour of industrial inputs and capital equipment.